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Sharing knowledge, experiences, and innovations in public-private partnerships in infrastructure

Unsolicited infrastructure proposals

How some countries introduce competition and transparency

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Unsolicited proposals for infrastructure projects from private investors can introduce innovative ideas—but also risks, such as opportunities for corruption. Some countries disallow unsolicited proposals. Others manage them in ways that introduce competition and transparency. Governments' decision to allow unsolicited proposals should depend on individual circumstances and overall development policies, but when they do allow them, governments will have several important issues to consider.

Many governments have recognized that the private sector can be an important source of technical and managerial expertise as well as financing. Sometimes private companies directly approach governments with new project ideas, typically called *unsolicited proposals*.

Opposition to unsolicited proposals rarely stems from the project concept originating in the private sector. Instead, there are often perceptions that the projects serve special interests or are associated with corruption. Unsolicited proposals often become controversial when—or if—governments negotiate the project rights directly with the original proponent without sufficient transparency or competing proposals.

Some countries have developed effective systems to channel unsolicited proposals into processes that incorporate transparency and competition. These systems attempt to provide incentives for the private sector to come forward with innovative infrastructure solutions while retaining the benefits associated with awarding the project through a transparent and competitive tender.

Managing unsolicited proposals

Most countries with formal systems for managing unsolicited proposals follow a similar process.

The two main stages

The system generally involves two main stages: the first focuses on the government's internal project approval process, and the second on a competitive tender to determine the final project developer and operator.

Stage 1: approval. Unsolicited proposals are approved in a four-step process:

- *Step 1.* The private proponent first submits a preliminary description of the project to the appropriate government agency or ministry. In some countries this description contains only general concepts (Argentina, Chile, Costa Rica); in others it provides detailed information (Republic of Korea, South Africa).

- *Step 2.* After a stipulated review period, the responsible agency or ministry gives a preliminary response, usually assessing whether the project serves a "public interest" or fits in the strategic infrastructure plan.

- *Step 3.* If the initial project description receives preliminary acceptance, the proponent is usually given formal recognition for the concept and a set period to present a full, detailed proposal.

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Table source: Authors.

TABLE 1

Unsolicited proposals and results in selected countries, various periods

Country	Period	Presented	Accepted	Under review	Rejected	Tendered or completed
Chile	1995–March 2006	200+	26	38	140+	12
Korea, Rep. of	July 1999–April 2006	141	101	7	33	65
South Africa	1999–2006	4	0	3	1	0
Taiwan, China	March 2002–May 2006	193	29	22	142	29

- *Step 4.* The detailed proposal is reviewed and may be approved for a competitive process or rejected. If accepted, the project is awarded through an open competitive tender (stage 2). If rejected, the project is not necessarily dead; the proponent may submit a modified version in some countries, or the government may use the concept in a public bid after a stipulated period (three years in Chile).

Stage 2: competitive tender. The project is competitively bid, typically under one of three systems: bonus, Swiss challenge, or best and final offer.

Bonus system

Chile and Korea use a system to promote unsolicited proposals that awards a bonus in the tendering procedure to the original project proponent. This bonus can take many forms, but most commonly it is an additional theoretical value applied to the original proponent's technical or financial offer for bidding purposes only.

Take the hypothetical example of an unsolicited proposal for a toll road where the original proponent receives a bonus of 10 percent. If the firm bidding the lowest tariff per kilometer offers US$0.19 a kilometer, the original proponent would be awarded the project if it bid US$0.20, because its bid would be within 10 percent of the lowest one.

Swiss challenge system

The Swiss challenge system—most common in the Philippines and also used in Guam, India, Italy, and Taiwan—is similar to the bonus system in that it uses competitive tendering to determine the project developer. But instead of a predetermined advantage, this system gives the original proponent the right to countermatch any better offers.

In the Philippines and Guam, for example, once a lower-priced proposal is submitted and approved, the original proponent has 30 days to match the price (in some countries, such as India, the government determines the time frame case by case). If the original proponent does not match the better price, the project is awarded to the third party. In the Philippines the project is immediately awarded to the original proponent if it matches the price.

The challenge is to promote innovation while preserving competition and transparency

TABLE 2

Considerations in balancing incentives for potential proponents and challengers

Influencing factor	Issues
Value of bonus (bonus system)	• Large bonuses will discourages challengers; small ones will discourage unsolicited proposals • Bonus may be used for technical (Korea) or financial score (Argentina, Chile)
Ability to match price (Swiss challenge)	• Challengers reluctant to allocate resources for counterproposals that can be matched • Developing counterproposals takes time
Amount and timing of information disclosed	• Information on the original proponent's financial offer may entice challengers to offer counterproposals, especially if the tariff is very high • If original proponent's bid not disclosed, challengers more likely to present best offers. The sooner vital information is available to challengers, the smaller the advantage to the original proponent in project preparation
Process transparency	• Challengers less likely to bid if they feel that information is withheld or that the process is corrupt • Transparency will aid challengers to raise international financing and partners

TABLE 3

Advantages and disadvantages of offering reimbursement for development costs

Advantages

- Legal respect for intellectual property rights essential to sustainable private sector development
- Reimbursement maintains private sector interest in the project development phase
- Ideas for projects not limited to large companies or developers with deep pockets
- Financial compensation for project development costs determined through the project's estimated market value or an independent audit
- Developers will allocate needed resources to ensure professional development of the project
- Reimbursement encourages innovation

Disadvantages

- Number of frivolous projects may increase as developers might intend only to profit from a project concept without actually bidding.
- Original project proponents may exaggerate project development costs to discourage challengers
- Challengers are at a financial disadvantage because reimbursement adds extra project finance expenses into the tariff calculation
- The government must allocate additional resources to determine accuracy of requested reimbursement

Managing unsolicited proposals requires dealing with many tradeoffs

In Guam, if the original proponent matches the better price, the government awards the project on the basis of technical merit.

Best and final offer system

In the best and final offer system the key element is multiple rounds of tendering, in which the original proponent is given the advantage of automatically participating in the final round.

In South Africa the two most advantageous bids are selected for a final bidding round. If the original proponent is not one of these two, it will still automatically be allowed to compete in the final round. In Argentina, if the original proponent's offer is within 5 percent of the best offer, the original proponent will immediately win. But if the difference between the best bid and the original proponent's offer is more than 5 percent but less than 20 percent, the two bidders will be invited to submit their best and final offers in a second round. In all cases the final round is an open competition during which the preferred bid will be selected with no bonuses or advantages given.

Weighing policy choices

Unless a government disallows unsolicited proposals by law, it should expect that the private sector will come forward with its own ideas. In many countries unsolicited proposals are even quite common (table 1).

TABLE 4

Time allocation for approval and bidding

Country	Preliminary approval	Final approval	Call for open tenders	Challenge or counter	Additional time	Total time
Argentina	90 days		60 days	Undetermined	n.a.	n.a.
Chile	45 days	12 months	12 months	Approx. 2–4 months	n.a.	27.5–29.5 months
Costa Rica	45 days	4 months	12 months	n.a.	n.a.	17+ months
Guam (U.S. territory)	Undetermined	Undetermined	Undetermined	60 days	n.a.	n.a.
Italy	4 months	2 months	3 months	n.a.	n.a.	n.a.
Korea, Rep. of	15 days	4 months	Undetermined	Approx. 2–4 months	n.a.	6.5–8.5+ months
Philippines	2 months	3 months	Undetermined	2 months	1 month to countermatch	8+ months
South Africa	1 month	9 months	3 months	2 months	2 months to evaluate	17 months

n.a. Not applicable.

TABLE 5
Considerations for time allocation

Process	Issues
Approve preliminary proposal	• Governments typically use a short initial period to screen out unnecessary proposals • Process allows proponents to test concepts without putting large resources into project development
Negotiate and finalize project	• Government may require new information and outside experts to improve the project • Time is required to repackage an unsolicited proposal as a government-managed, solicited public tender (Chile, Costa Rica) • With no final project approval times specified, some projects are negotiated over several years without threat of a looming deadline • A proponent often needs to obtain permits or licenses from other departments
Put project out to bid	• Delays allow the original proponent additional preparation time, not permitted to challengers • With an unspecified deadline, some projects remain inactive for indefinite periods • Government inactivity may lock up a proponent's financing, i.e., guarantees and bid bonds
Submit counterproposals	• The challenge period (60 days in the Philippines) not always sufficient to conduct technical due diligence and to develop the business plan, financial model, and financial bid • Challengers may need substantial time to raise financing

Developing an effective system to manage unsolicited proposals is not easy, however. Governments are faced with many tradeoffs. Policy makers must determine the appropriate incentives for the private sector to initiate projects, the amount of reimbursement (if any) to the original proponent for project development costs, and time constraints during the approval and challenge processes.

Finding appropriate incentives

There are many issues to consider when attempting to strike the right balance between incentives for the private sector to propose beneficial projects and enough chance of success for third-party challenges (table 2).

Reimbursing project development costs

If unsuccessful in the bidding process, the original proponent might expect reimbursement of its development costs from the government, the winning bidder, or both. Proponents invest time and money in the projects and expect to be compensated for their efforts. However, determining the true value of the project concept and development is not easy, and there are several issues to consider when deciding the amount (table 3).

Establishing time constraints

To make the process move forward, governments often set deadlines for completing certain stages of the approval and bidding phases. Infrastructure laws usually limit the number of months allowed for issuing preliminary project approval, completing a final proposal, putting the project out to public bid, and specify a closing date for challengers to submit counterproposals (table 4). Many issues arise regarding how much time to give potential challengers to present counterproposals. The original proponent has an obvious competitive advantage because it has spent much time and effort preparing the project (table 5).

Conclusion

Unsolicited proposals may contribute to the overall infrastructure goals of countries, particularly where governments have limited technical and financial capacity to develop projects. However, unsolicited proposals also pose challenges and risks, particularly when projects are negotiated with the original proponent without sufficient transparency or competition. Channeling all unsolicited proposals into a transparent, competitive process that gives other companies a fair chance of winning the tender can reduce the risks while preserving the potential for innovative solutions.

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