

MEMORANDUM

To: Members of the Audit Committee CS/AU/18-18 (Addendum 1)

From: Secretary General **Date:** 22 May 2018

Subject: **Infrastructure Project Preparation Facility – thematic evaluation –
Management comments**

Attached for consideration by the Audit Committee at its meeting on 29 May 2018 are management comments on the above.

Questions relating to this document may be addressed to Matthew Jordan-Tank (Ext 7498).

Distribution

President
Executive Committee
Directors and Alternate Directors

EvD Study: Infrastructure Project Preparation Facility Management Comments

Executive Summary

- Management thanks EvD for its insightful report. Management appreciates the study findings highlighting both the positive results achieved by Infrastructure Project Preparation Facility (IPPF) to date in policy engagements and supporting efficiency and delivery of operations in the infrastructure sector as well as identifying challenges in particular in the area of development of Public Private Partnership (PPP) given countries' capacity.
- Management welcomes the opportunity to discuss ways of enhancing Bank's infrastructure performance including the operational business model, results to date, and future consideration about the IPPF's remit and organisational structure within the Bank.
- The study recommendations focus particularly on the development of PPPs proposing the Bank takes a more centralised organisational approach in its support. Management would like to highlight that while support to PPPs is an important part of the IPPF, it is important to emphasise that the IPPF features three "Windows": a 'Sustainable Infrastructure Window' for public sector projects; a 'PPP Window' to boost private sector investment, and a 'Policy Window' to address upstream needs. The IPPF's key objective is to provide high-quality, efficient project preparation delivery for clients. The three 'Windows' all work in combination with focused policy advice for the Bank's public sector clients.
- Management agrees in principle with most recommendations, including that IPPF could be expanded to other sectors and the upstream project preparation capacity in countries could be strengthened through robust diagnostics of infrastructure needs and implementation gaps as part of the enhanced country strategy process, though applying a standard methodology is difficult given the different country contexts.
- Management recognises the importance of Value for Money (VfM) analysis for authorities to compare the value of using PPP procurement delivery and private financing vs deployment of traditional public sector procurement and implementation. This is the principle endorsed by the IPPF PPP Window: all PPPs prepared by IPPF perform a VfM analysis to ensure that the choice is appropriate and provides positive benefits for the client versus the traditional public sector procurement alternative.
- Management believes that it is critical to support client countries in applying, and strengthening if necessary, their own VfM methodologies, ensuring they are aligned with acceptable international practice. Where the authorities ask for the Bank's assistance at the very onset, or the Bank assesses that the VfM capabilities of the counterpart fall short of international best practice, the Bank will agree to upfront collaboration with the authorities or will provide technical assistance in developing the VfM methodology.
- Management believes that the PPP preparation is an area of EBRD niche expertise that could be strengthened and expanded in the context of strategic discussions on the future of the Bank, specifically in relation to strengthening innovation and public sector engagements. If the enhanced role is agreed in principle by the Board, the alternative proposed arrangement, including changes in structure, governance and resourcing of the function, needs to be carefully assessed against the desired improved effectiveness of the IPPF and discussed in the relevant fora of strategic and budgetary planning. Management notes that achieving its core objective of improved efficiency, speed and enhanced delivery is anchored on its close relationship to and strong synergies with the Bank's regular investment activities.

Management's extensive comments provided to the draft study have been reflected by EvD in this final version of the study. Management's response to recommendations is provided below.

Recommendation 1: Develop standard methodologies to assess country-level readiness to support various forms of procurement and project delivery, and include these in its country strategies and updates.

Management partially agrees with the recommendation. Management supports several elements of the proposed recommendation. A suitable approach could be to strengthen the existing ATQs (Assessment of Transition Qualities) and country diagnostics with assessment of project implementing capacity (including procurement) and PPP readiness, using a mix of in-house analysis and external sources. The results of such assessment could then be presented to the Board in the context of country diagnostics workshops that feed into the relevant country strategies.

Based on past experience, achieving a fully standardised methodology has not been feasible. The Bank has in the past made efforts to contribute to MDB efforts to measure PPP readiness in a more standardised approach across organisations. As a result the Economist Intelligence Unit (EIU) is commissioned by MDBs every few years to undertake *Infrascope*, a PPP readiness assessment of countries. Combining *Infrascope* with other internal work, such as the LTT commissioned 'PPP Laws Assessment', provides a more cost and resource effective approach to assessing the procurement and project delivery tailored to the suitability of the topic to the country context.

Recommendation 2: Develop and apply a Value for Money approach to support infrastructure funding proposals presented to the Board for large infrastructure projects in excess of EUR50mn that maybe suitable for development as PPPs.

Management agrees broadly with the recommendation, with a focus on upstream VfM support for large projects. Value for Money analysis concept is used in infrastructure for comparing the value after risk transfer of using PPP structures vs traditional state-led procurement. It is therefore important that the VfM methodology is used as an assessment tool and that our CoOs use adequate standards and methodologies when deciding which structure to use. This is the principle currently endorsed by the IPPF under its PPP Window: all PPPs prepared by IPPF perform a VfM analysis to ensure that the choice is appropriate and provides positive benefits for the client versus the traditional public sector procurement alternative. As such, Management believes that it is critical to support client countries in applying, and strengthening if necessary, their own VfM methodologies, ensuring they are aligned with acceptable international practice.

Going forward (including in the context of the Facility's renewal) Management will dedicate resources to develop a robust VfM approach for clients centred around the following approach: a) engaging early in the project cycle (i.e., prior to CRM preparation), ideally within the context of pipeline preparation and prioritisation, with national PPP units in our CoOs; b) identify critical risks in the project cycle for large, complex projects; c) develop a more robust understanding of full-life costing of infrastructure projects, capturing operation and maintenance costs; and d) development and training with respect to VfM methodologies by working upstream directly with central PPP units (typically located in ministries of finance).

This work will include active participation of the Bank's staff, including Operation Leaders, Sector Economists, and other Specialists to ensure that this more robust ex-ante VfM approach using the IPPF is socialised widely among Bank staff. It is expected that over time it will help optimise the choices made by our CoOs regarding procurement methods (all-in life cycle costs of projects by PPP versus traditional public sector delivery) that emerge from the Bank's clients prior to formal requests for financing.

Recommendation 3: Revise the current structure of the IPPF by transferring the PPP preparation function and associated funding to a new unit independent of banking operations where its services are available to all infrastructure banking operations within EBRD and establish the following sub-functions within it:

- a centralized PPP Policy Unit;
- a PPP Advisory Unit to provide upstream services to government on a fee for service and through the provision of a range of grant, loan and guarantee instruments;
- PPP transaction advisory on a fee for service and grant basis; and
- a PPP consultant management unit. Commit to sector-level diagnostics/analysis from which sector-level challenges and objectives will be derived;

Management agrees with the recommendation. Management acknowledges that the IPPF could be expanded to other sectors (such as Power and ICT as recommended by EvD). Management also agrees that upstream project preparation capacity in countries could be strengthened through robust diagnostics of infrastructure needs and implementation gaps as part of the enhanced country strategy process.

Management believes that PPP preparation is an important area of the Bank's niche expertise and leading position that could be strengthened and expanded in the context of strategic discussions on the future of the Bank, specifically in relation to strengthening innovation and public sector engagements. The question of structure, governance as well as overall scale in terms of funding and resources for the proposed expanded PPP advisory function, if deemed by the Board as appropriate for further consideration, would need to be assessed, analysed and discussed in the relevant fora of strategic and budgetary planning. Such analysis, , could be reflected in the upcoming annual report on activities (to be prepared in Q3 2018) and request for IPPF replenishment, while ensuring continuation of the Sustainable Infrastructure Window in the transition phase is important to avoid disruptions of existing business.

Recommendation 4: Prepare an end of term Business Case report on IPPF for the Board that identifies the VFM generated by SSF funds allocated to each of its projects, which is set in the context of all TC funds available to IBG, with a view to determining the amount and sources of funds required for future IBG project preparation support for traditional public sector projects; and

Prepare a Business Case for the Board providing details on the organization structure, staff, resources and sources of funding required for the establishment and operation of a new PPP Unit with a bank wide remit.

Management agrees with this recommendation. Management will allocate resources to prepare a brief 'business case fiche' for all projects under preparation by the IPPF, showing the justification for usage of the IPPF. Consistent with the principles agreed for IPPF deployment, these fiches would focus on the justification for IPPF resources of all projects addressed to date, showing the lack of alternative donors to fund such preparation in a timely manner.

In addition, Management will prepare a Business Case within the updated IPPF Strategy document during Q3 2018 that will detail potential changes to the organisation structure, staffing, sources and needs of funding for a new organisational structure of the IPPF with a Bank-wide remit, as the case may be.