Consultancy Services for the Consolidation, Strengthening and Harmonization of the Policy, Legal and Institutional Framework for the Public-Private Partnership (PPP) Programme in Kenya
Contract No. 7141918

August 12, 2007

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RE: Final Report

Consultancy Services for the Consolidation, Strengthening and Harmonization of the Policy, Legal and Institutional Framework for the Public-Private Partnership (PPP) Programme in Kenya

Dear Ms. Bordón:

Enclosed is the Final Report for your Review, Approval, and No Objection for Payment.

If you have any questions or comments, please do not hesitate to contact me. My direct line is 1-202-728-4740 and my email is twhite@ip3.org.

Thank you in advance for your time and attention to this matter.

Sincerely,

Thomas H. White
Chief Executive Officer

Cc: Lewis Brandt
IP3 Team Leader
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This copyright will remain in full effect until such time as the Client Representative approves the report and the contractual amount of the financial remuneration is successfully transferred to IP3.
Acronyms & Terms

AG      Attorney General
DCF      Discounted Cash Flow
DG Procurement  Functional title for the head of Public Procurement Oversight Authority
DGIE   Department of Government Investment and Public Enterprises
DMD     Debt Management Department, Ministry of Finance
EIRR    Economic Internal Rate of Return
ERB     Electricity Regulatory Board
FIRR    Financial Internal Rate of Return
IFC     International Finance Corporation
IMF     International Monetary Fund
KAA     Kenya Airports Authority
KAF     Kenyan Association of Manufacturers
KPA     Kenya Ports Authority
KPSA    Kenya Private Sector Alliance
LGU     Local Government Unit
MOF     Ministry of Finance
MOT     Ministry of Transportation
MPND    Ministry of Planning & National Development
MRPW    Ministry of Roads & Public Works
MTEF    Medium-Term Expenditure Framework
MWNR    Ministry of Water & Natural Resources
NCC     Nairobi City Council
NPV     Net Present Value
OGM     Operations Guidelines Manual
PC      Privatization Commission
PPDA    Public Procurement & Disposal Act
PPOA    Public Procurement Oversight Authority
PPP     Public-Private Partnership
PPP Unit  Generic term for a body created to be national focal point for PPP
P3U / P3CU  Acronyms for PPP Unit or PPP Central Unit – both generic terms
PPP Secretariat  Legal (non-generic) term for Kenya's PPP Unit
PDF     Project Development Facility
PPIAF   Private Participation in Infrastructure Advisory Facility
PPOA    Public Procurement Oversight Authority
ROE     Return on Equity
ROI     Return on Investment
SCAC    State Corporations Advisory Committee
WRB     Water Regulatory Boards
WB      World Bank
Executive Summary

This Executive Summary presents an overview of the contents of the Final Report. The report is concise but comprehensive, and contains considerable detail regarding the IP3 team's recommendations, along with options analysis where appropriate. Readers are therefore urged to review the report in its entirety, as this Executive Summary section only presents the concepts in the Report and not their many important details.

Approach

The IP3 team's approach to preparing the Final Report differs from that of the previous reports in this consultancy, in that awareness-building material was provided in the previous reports to enable all stakeholders to understand the new key concepts associated with Kenya’s nascent coordinated national PPP program. In this Final Report, such awareness-building material has not been included. The Report is thus shorter in length as compared with previous reports, and focuses exclusively on specific recommendations, along with options analysis and discussion sections where appropriate, and most of the detailed technical material is in the Appendices.

PPP Policy Framework in Kenya: Essential Elements and Prerequisites

This Final Report includes the Draft Policy Framework and Statement for PPP in Kenya. The purpose of the PPP Policy Framework is to:

1. Articulate Government's commitment to PPP;
2. Provide a policy basis for the PPP Legal Framework; and
3. Provide a policy foundation for the PPP Institutional Framework.

Articulate Government's commitment to PPP: is an absolutely essential component of any national PPP program. The simple statement that “Government is in support of PPP” can have far-reaching implications on how future infrastructure and service delivery activities will be conducted throughout the country. By publishing the PPP Policy in the national Gazette, the PPP Policy is formally introduced as Public Policy.

Provide a policy basis for the PPP Legal Framework: is achieved when the PPP Policy is published as official Public Policy in the national Gazette. The process of publishing includes submission to Cabinet and Parliament for concurrence before the publishing can be made, and such concurrence gives the Policy the force and effect of law. Once the PPP Policy becomes official Public Policy, then it can be used as the basis of a wide array of legislative initiatives required for mobilizing and implementing the PPP program.
**Provide a policy foundation for the PPP Institutional Framework:** this is an essential key step in making the program coherent and transparent. In the mobilization and implementation of a new national PPP program people in the various institutions of Government, private sector stakeholder organizations, and perhaps most importantly the general public, will be exposed to an otherwise bewildering array of new institutional arrangements. Examples are the national PPP Advisory Committee, the PPP Secretariat, the line ministry and local government PPP Nodes, along with the expanded roles of the Public Procurement Oversight Authority, Debt Management Department, and Ministry of Planning & National Development. The rationale of the PPP Institutional Framework, described in this report, lays out the “rules of the game” for government agencies, investors, lenders, and consumers so that the operating procedures and process for implementing successful PPPs are clearly understood by all stakeholders in the new “partnership” economic paradigm.

The components of the PPP Policy Framework are:

1. PPP Policy; and
2. PPP Operational Policies

**PPP Policy:** is the national PPP Policy, published in the Gazette. A draft of the PPP Policy is provided in Appendix 1 of this report. The components of the PPP Policy are worded in a manner designed for ease of comprehension, and the statements are kept as basic as possible (and most statements contain information that readers of this report are already intimately aware) because the audience for the Policy includes the general public.

**PPP Operational Policies:** provide guidance on how decisions are to be made by the PPP program's national focal point for the PPP program. Operational Policies are not to be confused with Public Policy, which is a completely separate body of knowledge. In this report, we have provided a draft national PPP Policy. That is the Public Policy. In the section on PPP Institutional Framework, we have provided Operational Policies, within which there are two categories for which details are provided: (1) relationships with other PPP stakeholder institutions; and (2) internal operational policies for the PPP Secretariat.

**PPP Legal Framework in Kenya: Enabling or Constraining?**

There are no explicit restrictions or enabling mechanisms for public private partnership (PPP) arrangements in the laws of Kenya. This is not surprising as most laws were enacted prior to when PPP was contemplated as an option for public infrastructure projects or services. While the current legal regime is not restrictive, there is room to modernize, streamline, harmonize, and further develop the PPP legal apparatus, for which an important added benefit would be an improvement in the policies and procedures for fiscal management and public investment planning. The process of developing the legal framework can be incremental, as the PPP program builds in maturity and scale. In the interim, this consultancy has diagnosed some legal initiatives that would enable and facilitate PPP, and recommends a practical legal strategy to launch PPP while solidifying its status legally and institutionally.
Changes to the legal framework are proposed here to take place over a period of years as PPP evolves in Kenya. This phased approach to changing the legal framework reflects the approach taken in many other countries, such as South Africa, Mexico, the U.K., and Australia, which have now been systematically engaged in PPP for almost a decade. There are some internal changes to the By-Laws of the City Counsels that are needed to facilitate PPP, and those are described in the Appendix on Current PPP Project Opportunities. We have not drafted those changes because such By-Laws are internal City Council matters.

At this early stage of PPP in Kenya, an amendment to the current Finance Bill is proposed. The amendment specifically proposes to exempt PPP arrangements from the capacity building levy of 1.5% on the value of a contract procured under the Public Procurement and Asset Disposal Act 2005. Consequential amendments to the Public Procurement and Disposal Act, Government Contracts Act, and Permanent Secretary to the Treasury (Incorporated) Act flow from that proposed amendment. Subsidiary legislation, in the form of regulations made under powers given in various Acts will serve to formalize a legal basis for managing the PPP program.

The legal framework that is proposed for the initial phase of public-private partnership arrangements in Kenya includes the following steps:

1. The Minister for Finance inserts an amendment (if the Bill is already published) or a section (if not yet published) to the Finance Bill, 2007 currently before Parliament. The amendment modifies the Public Procurement and Disposal Act 2005 by stating that the capacity building levy shall not apply to a public private partnership arrangement that is recorded in writing in accordance with Section 7A of the Government Contracts Act.

2. Consequential amendments that flow from this amendment are contained in a Schedule to the Finance Bill, including:
   • A definition of Public Private Partnership Arrangement is inserted in the Public Procurement and Disposal Act.
   • Section 7A is inserted in the Government Contracts Act to: (a) provide that a contract for a public private partnership arrangement is not binding on the Government unless signed or counter-signed by the Permanent Secretary to the Treasury (to ensure adequate consideration is given to contingent liability and other potential fiscal risks to Treasury); and (b) give power to the Minister for Finance to make regulations for public private partnership arrangements.

3. Regulations are made under powers given in the Public Procurement and Disposal Act, Privatisation Act, Government Contracts Act, State Corporations Act, and Government Financial Management Act to provide for:
   • The Public Procurement Oversight Authority, when considering a specially permitted procedure for a public private partnership arrangement, to confine itself to the procurement aspects thereof, rather than the merits of the public private partnership arrangement being sought through the procedure;
   • The Privatisation Commission to bring to the attention of the Minister for Finance any potential liability (actual, potential, hidden or contingent) for Government if it is proposed to adopt public private partnership as a method of privatisation;
• Place obligations on State entities that may be considering projects for public private partnerships to bring the projects to the attention of the Treasury;
• Place an obligation on State Corporations to bring proposals for public private partnership arrangements to the attention of their parent Ministry who in turn must inform Treasury;
• To lay down the steps to be taken by different players in Government in assessing projects for public private partnership arrangements; and
• To clarify that the responsibility of Accounting Officers, under the Government Financial Management Act, to ensure the “efficient and effective” use of public funds, includes the requirement to consider Public-Private Partnerships as a means of potentially leveraging public funds with private investment.

4. This framework places the Treasury at the centre of the PPP process, and gives it a gate-keeper function so that it can ensure proper fiscal management and public investment planning. It enables Treasury to monitor and control current and future commitments and obligations, many of which are likely to be of a contingent nature. It establishes a consistent and coordinated approach to PPP arrangements. Scope for overlap between the different parts of Government is reduced, by specifying the extent and limits of their respective roles in the identification, promotion, development, assessment, procurement, implementation, monitoring, and contract compliance for PPP projects.

5. These legislative initiatives should take place simultaneously with the issuing of a policy statement, and the setting up of the PPP Steering Committee and its PPP Secretariat.

6. The existence of current PPP proposals, many of an unsolicited nature, should not set in motion a habit of accepting and evaluating such proposals if doing so would undermine the development of a longer term, sustainable approach to PPP procurement. Guidance on the handling of unsolicited PPP proposals is provided in Appendix 3.

7. As Government policy and institutions evolve, and with growing knowledge of the type of transactions that are emerging, legislation can be prepared such as the example given in this report of the State Entities (Public Private Partnership Arrangements) Bill. This Bill avoids the need for piecemeal amendment of laws relating to State corporations and local government bodies, and provides certainty about the legal capacity to enter into public-private partnership arrangements.

PPP Institutional Framework in Kenya: Proposed Structure and Linkages to Existing Institutions

A PPP Steering Committee and related Secretariat are clearly needed in Kenya to both protect the Government from the potential risks of PPPs, especially fiscal risks, as well as to take the lead in coordinating the overall policy and legal & regulatory framework for PPPs in Kenya. Without a PPP Committee and Secretariat to both establish the PPP Framework and to systematically review and either approve or disapprove of proposed PPPs, the record of PPPs in Kenya would likely turn out to be one of both a very limited number of PPP projects proposed and approved, and of important uncertainty about the Government’s exposure to risks from the PPP transactions.
To ensure the PPP Committee and its Secretariat remain focused on their designated roles, and the Secretariat operates as an efficient organization with a small core professional staff, the criteria referenced below will serve as guiding principles for the institutional design:

1. Not become another layer of bureaucracy, but rather an efficient reviewer and process management body, with a streamlined administrative process, spearheaded by a small technical staff, protecting Treasury from unanticipated demands;

2. The existing resources and institutional arrangements needs to be fully utilized, without duplication of functions, while respecting spheres of accountability;

3. Although a gatekeeper, the PPP Secretariat should also function as coordinator for PPP activity, establishing the overall PPP Framework, providing advice and assistance to Ministries and other state entities considering PPP proposals, while also performing its core function of reviewing and assessing specific PPP project proposals;

4. The institution should be focused on managing the process rather than attempting to be a kind of boutique investment bank managing the transactions;

5. Considerable use should be made of outsourced technical expertise at the various stages of the PPP project life cycle, thereby enabling a relatively small core staff;

6. Clear division of responsibility should be maintained between the development of new PPP projects and the assessment of those projects, to prevent conflict of interest;

7. Utilize the PPP project assessment methodologies of Affordability, Risk Allocation, and Value for Money to improve and further develop the GOK’s fiscal management and public investment planning;

8. Take appropriate measures for ensuring its independence from potential political, financial, and/or industrial capture.

There are a number of additional operational policies we recommend should be adopted by the PPP Secretariat, including:

1. The PPP Secretariat will need to solidify the links between the various stages of the PPP project life cycle by working with sector ministries and local government bodies, and providing technical assistance and capacity building where necessary;

2. The staffing of the PPP Secretariat should be demand-driven, based on deal-flow and PPP framework development demands, and structured for matrix management rather than management based on fixed departmental divisions of responsibility;

3. Specialist technical expertise in economic analysis, financial analysis, engineering, and law should be contracted externally based on demand, rather than building up a permanent, expensive internal capacity within the PPP Secretariat;

4. That all ‘large’ capital investments in infrastructure must consider the PPP option before undertaking any new public investments and/or borrowings – this can be enforced by the PS-Treasury’s oversight of Accounting Officers in the various GOK bodies;

5. The PPP Steering Committee should have final approval/veto power over PPP projects, except for PPP projects of a size and/or nature that requires Cabinet approval;
6. The PPP Secretariat should improve the quality of PPP projects by testing them for Affordability, Risk Allocation, and Value for Money;

7. Consultants to the PPP Secretariat should be engaged to design and draft Manuals of Required PPP Procedures, one for the PPP Secretariat and another for the PPP Nodes, featuring PPP options analysis, models, templates, and standard procedures to be used in the identification, development, structuring, and assessment of PPP projects;

8. The process of identifying and of preparing and proposing specific projects as PPPs should be decentralized as far as possible to the Sector Ministries, State Agencies or SOEs using the resources of their PPP Nodes, where available; and

9. The PPP Secretariat should have a close, consultative relationship with Treasury’s Debt Management Department, the Public Procurement Oversight Authority, and the Ministry of Planning & National Development. These relationships will be facilitated by housing the PPP Secretariat (the Technical Unit for the National PPP Steering Committee) within the Ministry of Finance offices, and by having the PS-Treasury serve as Chairman of the National PPP Steering Committee.

The primary purpose of the PPP Secretariat is assessing and mitigating risks, which means that its policies and procedures will focus on project assessment, rather than on project development. The assessment function is not only focused upon the internal aspects of each project, but more importantly is focused on the questions of whether undertaking the proposed project may create unacceptable contingent liabilities on the Treasury, whether the acceptance of direct and indirect liabilities associated with the proposed projects will be consistent with sound fiscal management practices, and whether the process of putting the project into the Medium Term Expenditure Framework and National Budget reflects established principles of sound public investment planning.

The role of the PPP Secretariat in fiscal management and public investment planning, as part of the national Treasury, will focus on the following:

- Identify potential PPP fiscal risks in view of Kenya’s overall fiscal capacity;
- Employ safeguards to ensure effective financial control of PPPs, by separating activities related to PPP promotion from activities related to technical oversight and financial control;
- Perform a gateway function enabling Treasury to control fiscal exposure from PPP projects;
- Advise on options to limit PPP related-risks to the Government (e.g., ceilings on exposure to PPPs—stocks and flows);
- Establish and enforce criteria and procedures for prioritizing investment projects and selecting PPPs;
- Determine whether donor support is likely to be involved in the PPP process, and if so, what are the implications for fiscal risks and control; and
- Start operations with small, manageable PPP projects, rather than "one or two large" ones) in order to build-capacity and limit fiscal risks.
The chart below provides a summary of this consultancy’s recommendations for development of the Policy, Legal, and Institutional Framework for PPP in Kenya.

### Table 1: Summary of Recommendations

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<th>No.</th>
<th>Recommendation</th>
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<td>1</td>
<td>Adopt a PPP Policy &amp; Publish it through the National Gazette</td>
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<td>2</td>
<td>Adopt (a) Immediate and Short-Term PPP Legal and Regulatory Framework and (b) Long-Term PPP Legal and Regulatory Framework</td>
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<td>3</td>
<td>Institutionally Separate the Functions of PPP Project Proposal vs. the Function of PPP Project Review and Approval/Disapproval</td>
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<td>4</td>
<td>Location of National PPP Secretariat Should be in the Ministry of Finance (MOF)</td>
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<td>5</td>
<td>Adopt a Phased Approach to the PPP Secretariat Development</td>
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<td>Recommendation #6: Adopt a Phased Approach to Staffing Identification, Development, Growth, and Training:</td>
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<td>6.2</td>
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<td>Remuneration &amp; Status for PPP Secretariat Should be Commiserate with the Envisioned High Level Status</td>
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<td>Utilize a Project Matrix Management Structure &amp; Modus Operandi for the PPP Secretariat</td>
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<td>Capacity Building of Staff of the PPP Secretariat Staff &amp; PPP Nodes is Critical for Success</td>
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<td>7</td>
<td>The PPP Secretariat Must Develop Effective Institutional Relations with All Critical Stakeholders</td>
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<td>PPP Secretariat Operational Procedures and Policies Need Definition and Development</td>
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<td>8.1</td>
<td>All ‘large’ capital investments in infrastructure must consider PPP options analysis before undertaking any new public investments and/or borrowings</td>
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<td>8.2</td>
<td>The PPP Secretariat access to Government decision-making process should have final approval / veto power over all PPP projects</td>
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<td>8.3</td>
<td>The PPP Secretariat should improve the quality of potential PPP projects by requiring clear standard procedures for ‘affordability and value for money and ensure the appropriate risk transfer’</td>
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<td>8.4</td>
<td>The PPP Secretariat will design implement PPP models, templates and standard operating procedures (SOPs)</td>
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<td>8.5</td>
<td>The PPP process should be decentralized as far as possible to the Sector Ministries’, State Agencies’ or SOEs’ own PPP Node</td>
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<td>8.6</td>
<td>The PPP Secretariat needs to be output focused rather than focused only on administration and monitoring</td>
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<td>9</td>
<td>The PPP Secretariat Must be Active in Fiscal Management &amp; Public Investment Planning</td>
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<td>Establish a Dedicated Source of Funds Available to Sector Ministries to Complete their Own PPP Project Analyses &amp; Proposed Structures: The PPP Project Development Facility (PPP PDF)</td>
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<td>12</td>
<td>Develop, Officially Adopt, and Distribute a Manual of Required PPP Procedures for Kenya’s PPP Framework</td>
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Chapter 1. Introduction

The Office of the Investment Secretary, Ministry of Finance has engaged a consultancy to develop the Policy, Legal, and Institutional Framework for Public-Private Partnerships in Kenya. The Institute for Public-Private Partnerships (IP3), with grant funding from Private Participation in Infrastructure Advisory Facility (PPIAF) administered by The World Bank, has been assisting in the development of this important new framework.

The consultancy’s key components include:

- Defining a national PPP policy for Kenya;
- Assessing the capacity of the various spheres of Government to enter into contracts with the private sector for long-term service delivery, identifying legal impediments to PPPs, as well as appropriate legal initiatives required to develop the fiscal management and public investment planning framework;
- Developing an institutional framework for national and sub-national PPP activity, and an institutional design for national and sub-national PPP Centres, and
- Defining the appropriate steps for conducting PPP transactions, including PPP project conceptualisation, identification, development, assessment, and contracting.

The Consultant produced an Inception Report as well as a First Interim Report on policy & legal issues, and a Second Interim Report on institutional design and PPP initiation steps. A Draft Final Report was then produced, in which specific recommendations of the Consultant Team were presented, based upon the feedback received from the Government of Kenya’s Steering Committee for this Consultancy and from the World Bank, PPIAF, and the IMF.

The final recommendations were presented at a second workshop, which became a decision-makers’ meeting, during which feedback was obtained from participants including the key members of this project’s Steering Committee, the World Bank, PPIAF, IMF, and other key stakeholder organization decision makers. This Final Report incorporates their feedback, along with written comments received from WB/PPIAF/IMF and Treasury.

Organization of this Final Report

This report has been organized to feature an overview description and summary of the key recommendations of the Consultant Team combined with a series of more detailed action items in the Appendices to complement the recommendations. Each recommendation is presented according to a consistent outline structure.
Chapter 2. Recommendations

A. PPP Policy Framework

Recommendation 1: Adopt a New National PPP Policy & Publish it through the National Gazette

This Final Report includes the Draft Policy Framework and Statement for PPP in Kenya. The purpose of the PPP Policy Framework is to:

1. Articulate Government's commitment to PPP;
2. Provide a policy basis for the PPP Legal Framework; and
3. Provide a policy foundation for the PPP Institutional Framework.

Key Issues and Options Considered

PPPs are not new to Kenya. Since the mid-1990s Kenya, like many other emerging market economies, has engaged in a number of contracts and awarded licenses to private operators to provide new telecommunications, electricity, railways, municipal services, and other key public services. However, Kenya’s experience to date with PPPs has largely been done on a case-by-case basis, and each individual PPP contract has required considerable effort to prepare and complete with varying levels of completeness. There is a clear need to provide a framework in which PPP can be can be implemented in a more consistent manner, with appropriate standards and procedures enabling fiscal control. That will require a National PPP Policy.

Possible options regarding a National PPP Policy include:
1. No official PPP Policy – ad hoc PPP activity;
2. Develop sector-by-sector PPP policies; or
3. Establish a new, cross-sector PPP Policy.

No official PPP policy - ad hoc PPP activity: while it could be argued that because a number of PPP contracts have already been signed in Kenya, and more are being considered, perhaps a new policy framework is not necessary. This option was not developed as a serious option, because of the enormous issues surrounding PPPs in Kenya. Not only are there uncertainties within Government about the legality of PPPs, but also uncertainties about the fundamental goals of PPPs and even the definition of just what a “Public-Private Partnership” is. A
fundamental goal of this consultancy and indeed a key reason for its existence is that a new foundation of a clear policy on PPPs is indeed needed.

**Develop sector-by-sector PPP policies:** some countries have chosen to adopt sector-by-sector approaches to PPPs. This has included separate policies for each sector of infrastructure, along with separate sector laws, regulations and institutions. While this approach can allow policy reformers to focus more easily on one sector at a time, it often misses a very important opportunity to create a uniform system that takes advantage of economies of scale across sectors. Clearly a new cross-sectoral PPP policy in Kenya is needed.

**Rationale for Recommendation: Adopt a New, Cross-Sector PPP Policy**

A new, cross-sectoral PPP policy is needed to establish a clear and consistent approach for the numerous efforts taking place within line ministries, state corporations, local governments, and public authorities to prepare and propose new long-term public-private partnership projects. This is especially needed to protect the interests of Government and the public to ensure that all future PPP projects actually achieve the key goals of better value for the public’s money and protection of Kenya’s limited public financial and other resources that are contributed to these projects. The international record on PPPs, as well as the current level of experience with the early PPP transactions in Kenya reveal that without a clear and cross-sectoral policy, legal & regulatory, and institutional framework for PPPs, PPP contracts may get signed and implemented that do not deliver more or better services, and which may cost the Government more than it anticipated, in terms of both direct financial costs and exposure to high levels of risks throughout the PPP contract’s term.

A cross-sector PPP Policy is clearly consistent with Kenya’s other key priority public policies, especially the long-term infrastructure and service provision goals of Vision 2030. The Minister for Finance linked those goals to the PPP program in his 2007/2008 Budget Speech, as follows:

“Macro-economic stability must also be accompanied by deep structural reforms in order to maximize growth. Therefore, to consolidate the recent gains in the public sector, the Government will implement structural reforms to further improve efficiency in the use of public resources and ensure effective service delivery. We will focus on priority areas of: (i) public expenditure and financial management; (ii) public sector restructuring and privatisation; (iii) deepening financial intermediation; and (iv) private sector competitiveness. The implementation of these measures is expected to improve business environment, encourage private sector investment - both domestic and foreign and expand its capacity to create more jobs and reduce poverty amongst our people.”

“To attract more financial and management resources to enhance our productive capacity, the Government is in the process of finalizing the policy, legal, and institutional framework for the implementation of Public Private Partnerships. This framework is intended to allow private sector participation in the provision of key infrastructure services such as water, energy, road and other transport services and is critical for the financing of the flagship projects under Vision 2030. We will also create an institutional framework to assess the fiscal risks associated with these PPP projects.”

-Hon. Amos Kimunya, E.G.H., M.P., Minister for Finance
It is important to note from the above that the policy goal of the PPP program is “to attract more financial and management resources to enhance our productive capacity” and that the creation of an institutional framework for PPP is to “assess the fiscal risks associated with PPP projects.”

For these reasons, we have designed a PPP policy and legal framework that will enable Kenya to attract financial and management resources from the private sector, while also ensuring more rigorous financial management and public investment planning, and we have designed a PPP institutional framework that will enable the GOK to assess the fiscal risks of PPP projects.

The role of the PPP Steering Committee and its PPP Secretariat is thus focused on assessment of risks associated with PPP projects, rather than on promotion of PPP activity.

The key aspects of a National PPP Policy should be:

**Procedural clarity:** The new PPP policy needs to be clear, unambiguous, and relatively simple to understand. It should not call for complex procedures or burdensome requirements that constrict the ability to prepare and complete PPPs.

**Better Value for the Public’s Money:** The new PPP policy must provide clear for protection of Kenya’s limited resources, especially scarce public financial resources, from many of the commercial risks of PPPs. While there will often be the need for important contributions by the Government toward PPPs, the PPP policy should promote the careful, systematic analysis of any risks being borne or shared by the Government. This includes calling for them to be explicitly stated in contracts, and calling for their use only to maximize the economic benefits from PPPs and to enable them to be “bankable” to the private sector.

**Clarify the roles of stakeholders:** The new Policy should acknowledge that the sector ministries and local government bodies continue to conduct policy making, planning, and monitoring activities even if they contract with private partners through PPPs for the delivery of services. The division of responsibilities for the national PPP program will be that line ministries and local government authorities will focus on PPP project development, while National Treasury will focus on PPP project assessment. The project assessment role will be supported by the Debt Management Department, and the process of approving the project for inclusion into the Medium Term Expenditure Framework and National Budget will be supported by the Ministry of Planning & National Development.

**Fairness, transparency, and accountability:** The PPP Policy will need to provide emphasis on the importance of fairness, transparency, and accountability in the procurement of PPP projects. Although PPP transactions are different from conventional procurement, because a partnership is formed rather than an arm’s length purchase of goods or services, and are different from privatisations, which are arm’s length sales transactions, the procurement component of any PPP transaction (the tender phase) must conform to the same standards of fairness, transparency, and accountability standards that apply to any transaction involving the use of public funds. There is, therefore, an important oversight role for the Public Procurement Oversight Authority in the implementation of PPP transactions.
Summary Description of the Recommendation

The following is a summary description of the main components included within the recommended new PPP Policy Statement. PPP Policy is the official national PPP Policy, published in the national Gazette. A draft of the PPP Policy is provided after this section. The components of the PPP Policy are worded in a manner designed for ease of comprehension, and the statements are kept as simple as possible (and most statements contain information that readers of this report are already intimately aware) because the audience for the Policy includes the general public. The full text and details of this recommended PPP Policy Statement is included in Appendix 1 to this Report.

The key elements of this recommended PPP Policy include the following:

Formally Confirm Government’s Official Support for PPP: is an absolutely essential component of any national PPP program. The simple statement that “Government is in support of PPP” has far-reaching implications on how infrastructure and service delivery activities will be conducted throughout the country. By publishing the official PPP Policy in the national Gazette, the PPP Policy is formally introduced as Public Policy.

Definition of “Public-Private Partnership”: This PPP Policy establishes the definition of a “public-private partnership” as a commercial joint venture, between a public institution and a private party, in which project risks are allocated amongst the parties based on which party is best equipped to manage each category of such risks, and in terms of which the private party:

• Performs an institutional function on behalf of the state; and/or
• Is allowed the use of state property; and
• Assumes substantial financial, technical, and operational risks in connection with the performance of the institutional function and/or use of state property; and
• Receives a benefit for performing the institutional function and/or from utilizing the state property.

“Commercial” means a benefit is received for performing the services. “Joint venture” means a joint or mutual undertaking, not necessarily via a Special Purpose Vehicle or other legal body that may or may not be established for the venture. Allocation of risks is an essential element of the definition because that process establishes the “partnership,” without which there is no PPP. Without the partnership aspect, the arrangement could still be a service provision contract or concession, but would be a privatisation (sale) or procurement (purchase), and not a PPP.

This definition of PPP is not intended to be a comprehensive definition for general use. It is the definition of PPP for the purposes of PPP Policy. This definition is necessary because the Policy requires people to do certain things if a PPP exists. The Policy would be unacceptably vague if it did not define what PPP was, for purposes of the Policy. Similarly, in the legal sections of this report, a definition of “PPP Arrangement” is provided. That too is not intended to be a general definition of PPP; it is intended to define what a PPP Arrangement is for purposes of the PPP Legal Framework and not a comprehensive definition of PPP for general use. The definition of PPP Arrangement is necessary because the Legal Framework requires people to do certain things if a PPP Arrangement exists, so what constitutes such an Arrangement must be defined.
Explain the Rationale for PPPs in Kenya, including the Basis for Avoiding PPPs that are not consistent with sound fiscal management and public investment planning: While PPPs can play an important role in furthering Kenya’s priority goals of expanding and improving its key infrastructure sectors, the new PPP Policy is based upon the understanding that not all PPPs are “good PPPs” and not all are necessarily in the interests of the Government, or the public, of Kenya’s taxpayers, or of other key Kenyan stakeholder groups. Thus, while the policy establishes the Government’s support for PPPs, it also establish the policy basis for being able to “reject” and stop PPPs that do not provide better value for the public’s money, that are not affordable, or that expose the Government to imprudent levels of fiscal risk. Given the robust private sector in Kenya, and the already existing pipeline of PPP Project Opportunities (details are provided in Appendix 5) the facilitation role of the PPP Steering Committee and its related PPP Secretariat will be subordinated to its “gatekeeper” role of protecting fiscal resources.

Provide a Policy basis for the new PPP Legal & Regulatory Framework: is achieved when the PPP Policy is published as official Public Policy in the national Gazette. The process of publishing includes submission to Cabinet and Parliament for their concurrence before the publishing can be made, and such concurrence gives the Policy the full force and effect of law, though of course legislation is required to clarify how the Policy provisions are to be interpreted and enforced. Once the PPP Policy becomes official Public Policy, then it can be used as the basis of a systematic framework of sequenced legislative initiatives required to implement the PPP program. The full explanation and details of the Consultancy’s recommended Legal & Regulatory Framework are described in the next section below.

Explain the Purpose of the PPP Institutional Framework: In mobilization and implementation of a new national PPP program, people in the various institutions of Government, private sector stakeholder organizations, and perhaps most importantly the general public, will be exposed to a system of new institutional arrangements. As noted in the new PPP Policy, these new institutions and their powers and procedures are necessary to ensure the independence, the accountability, and the transparency of the entire PPP framework. Examples are the National PPP Committee, its PPP Secretariat, the sector ministry and local government PPP Nodes, plus the expanded roles of the Debt Management Department, the Public Procurement Oversight Authority, and the Ministry of Planning & National Development. The full explanation and details of the Consultancy’s recommended Institutional Framework are provided in this report.

National as well as Local-Level PPPs in Kenya: Local governments in Kenya are governed and regulated under a separate legal status, led by the Ministry of Local Government. However, PPPs are being prepared and proposed for both national Government infrastructure sectors like electricity, roads, ports, airports, railways, etc. as well as for some local Government sectors like water & wastewater, street lighting and municipal services. The new PPP Policy recognizes the need for the new PPP Framework’s regulatory safeguards, procedural requirements, and its institutional capacity to be available to local governments as well.

Defining The PPP Project Life Cycle in Kenya: The PPP framework defines the minimum requirements for key stages and procedures in the PPP Project Life Cycle including. This definition not only establishes a broader, common understanding of the process of

<table>
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<th>Key Stages of PPP Project Life Cycle</th>
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<td>1. Project selection &amp; identification</td>
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<td>2. Project analysis and preparation</td>
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<td>3. Tendering &amp; procurement</td>
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<td>4. Contract finalization and project financial closure</td>
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<td>5. Post-Award contract compliance and performance monitoring</td>
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implementing PPPs in Kenya, but also establishes the need for a Manual of Required PPP Procedures, which is described and explained in the Appendices.

**Ensuring the Affordability of PPPs:** Sometimes PPP appears more affordable to Sector Ministries and even to Government planning and financing units because PPP avoids the procedures of sovereign borrowing that is usually required used to finance traditional, public infrastructure projects. However, PPP contracts often bind Sector Ministries to make minimum payments to PPP contractors over periods of up to 20 years or more. This new PPP Policy establishes the basis for requiring that the proposed payments required by PPP projects are transparently reported and consistently analyzed to confirm that they are affordable to Sector Ministries and the National Treasury. There is another form of Affordability test that must be passed when a new PPP projects is proposed; that is the test of affordability to end-users. Agencies proposing the project must conduct Consumer Demand, Affordability, and Willingness to Pay Surveys to ascertain that projected tariffs will be achievable and sustainable. This requirement to test for such end-user Affordability is provided in the PPP Policy.

**Managing Government's Fiscal Risks in PPPs:** This policy recognizes that many PPPs require important public sector contributions in order to become “bankable” by private financiers, and that such contributions will often expose the Government of Kenya to risks to its limited fiscal resources. For example, transport PPPs facing market or demand risks may propose that the Government, through the Ministry of Finance, guarantee a minimum level of traffic or ridership needed to meet the project’s debt service until the loans are repaid. This PPP policy directs that any such requests for risk-sharing by the Government in a PPP shall be transparently identified, systematically valued, and that they remain limited, coverable, and are clearly needed to provide key value for money benefits.

**Ensuring Stakeholder & Labour Consultation:** this PPP policy calls for minimum standards for consulting and communicating with key PPP stakeholders, especially labour, to ensure that everyone affected by the PPP program is aware of decisions that are being made and which may have a significant impact on their lives. Transparency and accountability are the themes for this communication, which is essential to ensure public support for PPPs in Kenya. Specific standards will be required for labour-related matters, such as the requirement for GOK project sponsors to prepare a Labour Impact Analysis and a Labour Management Plan for each project being proposed. The PPP Policy shall also ensure that the needs of poor and low-income end users are accommodated in the design and implementation of PPP projects.

**Competition & Transparency in the Procurement of PPPs:** This Policy calls for competition in the procurement of PPP contractors wherever possible to maximize the important value for money benefits, including requirements that unsolicited PPP proposals be exposed to clear competitive analyses and bidding mechanisms. The Consultancy’s specific recommendation for new legal requirements and regulations for the procurement of PPPs are described and explained within this report below.

**PPP Capacity-building:** As PPPs in Kenya require that important new skills be sourced and developed in the public sector, this PPP Policy calls for supporting systematic and on-going PPP training & capacity-building. Most PPP “deal flow” comes from the sector ministries and local government bodies, which are “close to the ground” where PPP deals can be conceptualised,
identified, prioritised, and fed up into the national PPP framework for investment decisions. In order to perform this critical role, PPP Nodes (or Knowledge Centres) need to be formed need to be established in sector ministries and local governments, and skills within those Nodes must be developed through a long-term commitment to training and capacity building.

**Local Participation & Foreign Control Issues in PPPs:** The PPP Policy seeks to enable foreign participation in the financing and operation of PPPs, as well as to promote opportunities for local financial, operational, and labour-participation. There is no requirement for any fixed percentage of local ownership in PPP projects. Experience with such minimum percentage local ownership requirements has demonstrated that the kind of local ownership enabled by such requirements is often not of the quality necessary to add value to the project.
B. PPP Legal and Regulatory Framework

Recommendation 2: Adopt (a) Immediate and Short-Term PPP Legal and Regulatory Framework and Later, (b) Long-Term PPP Legal and Regulatory Framework

Changes to the legal framework are proposed here to take place over a period of years as PPP evolves in Kenya. This phased approach to changing the legal framework reflects the approach taken in certain other countries, such as South Africa, Mexico, the U.K., and Australia, which have now been successfully engaged in PPP for over a decade. There are some internal changes to the By-Laws of the City Councils that are needed to facilitate PPP, and those are described in Appendix 5 of this report. We have discussed this matter with Nairobi City Council and the Head of their Legal Department. The next steps are up to them; they have ongoing technical assistance from an in-house legal reform consultant.

The South African success with using their Public Finance Management Act (PFMA) as the primary legal vehicle for the PPP program has led to speculation that in Kenya the same thing might be done using the Government Financial Management Act (GFMA) but the PFMA and GFMA are significantly different laws, in terms of purpose and substance, and operate within different Constitutional frameworks. The GFMA is focused on conventional accounting matters. South Africa’s PFMA establishes the National Treasury, and is an Act that is geared towards financial management through monitoring the results of expenditure, and holds Accounting Officers accountable for those results. The GFMA focuses on accounting for monies spent more than the results of the expenditure. These factors make Treasury Regulations under PFMA to be a powerful legal mechanism for managing and controlling PPP activity, whereas passing such Regulations under the GFMA would not be such a good fit with the focus of the Act.

The GFMA does, however, provide that Accounting Officers are responsible for the “efficient and effective” use of public funds. The Permanent Secretary - Treasury, to whom all the Accounting Officers report, may interpret that responsibility to include a requirement to formally consider/evaluate the potential use of Public-Private Partnerships whenever investing public funds, as a means of leveraging those funds with private investment. This is a key recommendation of the IP3 team, and it can be achieved without amendment to the GFMA. Although this requirement could be created by GFMA regulations, it would likely be sufficient for the Permanent Secretary - Treasury to simply issue a Notice informing all the Accounting Officers that such an interpretation and requirement now exists. In this manner, Government can be assured that all investments of public funds will be subjected to formal analysis of potential for PPP. If such formal analysis indicates acceptability for PPP, yet the Accounting Officer proceeds without the use of PPP, then the PS-Treasury will have grounds for rejecting the transaction. This approach does not have the power of South Africa’s PFMA to require PPP activity, but it does at least compel a formal consideration of the PPP option.

At this initial stage of PPP in Kenya, an amendment to the current Finance Bill is proposed. The amendment specifically proposes to exempt PPP arrangements from the capacity building levy of 1.5% on the value of a contract procured under the Public Procurement and Asset Disposal Act 2005. Consequential amendments to the Public Procurement and Disposal Act, Government
Contracts Act, and Permanent Secretary to the Treasury (Incorporated) Act flow from that proposed amendment. Subsidiary legislation, in the form of regulations made under powers given in various Acts will serve to formalize a legal basis for managing the PPP program.

Our legal and regulatory recommendations follow two parallel courses. The first, described in section (a) below, is an interim legal & regulatory framework for PPPs in Kenya be established through a system of relatively simple measures that can be accomplished in a short period of time. These include amendments to Acts or making regulations under existing laws. This interim procedure establishes a firm foundation for PPPs and for recommended institutional measures and procedures to protect the public interest in PPP arrangements. The second parallel course, described in section (b) below, provides an opportunity to enact new legislation if the need arises as the PPP program matures.

(a) Immediate and Short-Term

The following immediate and short-term legislative initiatives are proposed for the initial phase of the public-private partnership program:

- The Minister for Finance inserts an amendment (if the Bill is already published) or a section (if not yet published) to the Finance Bill, 2007 currently before Parliament. The amendment modifies the Public Procurement and Disposal Act 2005 by stating that the capacity building levy shall not apply to a public private partnership arrangement that is recorded in writing in accordance with Section 7A of the Government Contracts Act.

- Consequential amendments that flow from this amendment are contained in a Schedule to the Finance Bill, including:
  - A definition of Public Private Partnership Arrangement is inserted in the Public Procurement and Disposal Act.
  - Section 7A is inserted in the Government Contracts Act to: (a) provide that a contract for a public private partnership arrangement is not binding on the Government unless signed or counter-signed by the Permanent Secretary to the Treasury (to ensure adequate consideration is given to contingent liability and other potential fiscal risks to Treasury); and (b) give power to the Minister for Finance to make regulations for public private partnership arrangements.

- Regulations are made under powers given in the Public Procurement and Disposal Act, Privatisation Act, Government Contracts Act, State Corporations Act, and Government Financial Management Act to provide for:
  - The Public Procurement Oversight Authority, when considering a specially permitted procedure for a public private partnership arrangement, to confine itself to the procurement aspects thereof, rather than the merits of the public private partnership arrangement being sought through the procedure;
  - The Privatisation Commission to bring to the attention of the Minister for Finance any potential liability (direct, indirect, explicit, implicit, contingent) for Government if it is proposed to adopt public private partnership as a method of privatisation;
• Place obligations on State entities that may be considering projects for public private partnerships to bring the projects to the attention of the Treasury;
• Place an obligation on State Corporations to bring proposals for public private partnership arrangements to the attention of their parent Ministry who in turn must inform Treasury;
• To lay down the steps to be taken by different players in Government in assessing projects for public private partnership arrangements; and
• To clarify that the responsibility of Accounting Officers, under the Government Financial Management Act, to ensure the “efficient and effective” use of public funds, includes the requirement to consider Public-Private Partnerships as a means of potentially leveraging public funds with private investment.

**Gatekeeper Role of Treasury**

This framework places the Treasury at the centre of the PPP process, and gives it a gatekeeper function so that it can ensure proper fiscal management and public investment planning. It enables Treasury to monitor and control current and future commitments and obligations, many of which are likely to be of a contingent nature. It establishes a consistent and coordinated approach to PPP arrangements. Scope for overlap / duplication between the different parts of Government is reduced, by specifying the extent and limits of their respective roles in identification, development, assessment, procurement, implementation, monitoring, and contract compliance for PPP projects.

These legislative initiatives should take place simultaneously with the issuing of a policy statement, and the setting up of the Kenya National PPP Steering Committee and its PPP Secretariat, within the Ministry of Finance.

**Unsolicited Proposals**

The existence of current PPP proposals, many of an unsolicited nature, should not set in motion a habit of accepting and evaluating such proposals if doing so would undermine the development of a longer term, sustainable approach to PPP procurement. Guidance on the handling of unsolicited PPP proposals is provided in the section on Recommendation 7 in this report, in the sub-section entitled “Private Sector Project Sponsors.” That material gives some details on how unsolicited proposals could be allowed and treated. In Appendix 3 we have provided details on how to handle unsolicited proposals at the stage when the full PPP framework is already in place, and competitive selection methodologies have thus been fine tuned to the point that they are so efficient it is no longer necessary to reward private sector innovation by accepting unsolicited proposals. Our advice regarding unsolicited proposals is thus sequential: (1) initially follow the guidelines in Recommendation 7; and (2) when the PPP framework is in place and competitive section processes are fully developed and quite efficient, then follow the guidelines in Appendix 3.

**Public-Private Partnerships Arrangements Bill**

As Government policy and institutions evolve, and with growing knowledge of the type of transactions that are emerging, legislation can be prepared such as the example given in this report of the State Entities (Public Private Partnership Arrangements) Bill. This Bill avoids the need for piecemeal amendment of laws relating to State corporations and local
government bodies, and provides certainty about the legal capacity to enter into public-private partnership arrangements.

(b) Medium and Long-Term

While the interim approach to the legal framework is fully adequate for the immediate needs of Kenya’s PPP Framework, it has been consistently recommended by stakeholders throughout Kenya’s public sector, that PPPs should be given the explicit recognition and status in a dedicated PPP Law. The Consulting Team understands that (A) the process of enacting a comprehensive PPP law would take time while there is a pressing need to deal with PPP proposals and projects that are emerging and (B) that a comprehensive law is not essential at this stage of the evolution of PPP in Kenya. As PPP evolution takes place and as a pattern of projects and issues emerge PPP legislation can be developed to suit changing needs and to take account of experience. The interim PPP legal & regulatory framework that is recommended is adequate to meet the current needs of the PPP Framework in Kenya.

Key Issues and Options Considered

The analysis and recommendations regarding Kenya’s PPP legal & regulatory framework are based on the foundational principles resulting from the recommended PPP Policy. The analysis was done to determine what the specific legal and regulatory constraints to PPPs in Kenya have been, and how the existing enabling factors can be further developed to enable sound fiscal management and public investment planning within the PPP process.

The analysis identified key requirements for the legal & regulatory foundations for Kenya’s New PPP Framework, including those in the box to the right. The analysis has featured a comprehensive review of the PPP-related provisions of a broad range of existing laws and implementing regulations, including but not limited to the following:

- The Constitution
- The Government Contracts Act (Cap 25)
- The Permanent Secretary to the Treasury (Incorporation) Act (Cap 101)
- The Government Financial Management Act (No. 5 of 2004)
- The Local Government Act (Cap 265)
- State Corporations Act (Cap 446)
- Public Procurement and Disposal Act 2005 (PPDA)
- Privatization Act (Act No. 2 of 2005)
- The Investment Promotion Act, 2004
- The Companies Act (Cap 486)
- Kenya Railways Corporation (Amendment) Act, 2005

Key Requirements for Kenya’s New PPP Framework

1. Create a comprehensive framework to deal with the entire PPP project life cycle
2. Provide a direct legal basis for PPP contracts
3. Specify the rights of the public and private partners and private investor including distribution of risks
4. Clarify PPP procedures to be followed by government agencies/local authorities
5. Address labour and manpower issues that may result from PPP arrangements
6. Address any other concerns of not only the public and private sector partners but also of any financiers and local communities

**Rationale for Recommendation**

Overall, this analysis revealed that while PPPs are not prohibited in Kenya, there is a need to create certainty regarding how they should be structured & proposed, reviewed & approved/disapproved, tendered, and monitored. Moreover, the legal framework needs to be further developed, not only to facilitate PPP arrangements, but to strengthen the Government’s capacity to contain risks to Kenya’s limited public financial resources through PPPs and to ensure better value for money through PPPs. Such further development of the legal framework would improve Government’s fiscal management and public investment planning capacity, in all areas, in addition to areas of PPP undertakings. This will assist the GOK in performing the tasks agreed with the International Monetary Fund, as well as assist in attaining performance standards associated with the Millennium program.

The key options identified to address the legal & regulatory needs for a new PPP Framework for addressing these constraints included:

- Draft and enact a comprehensive PPP law covering all aspects of PPP institutions, project life cycle, procedures etc; and
- Draft, and enact amendments to existing laws and make regulations under existing laws to enable Kenya to set up a PPP institutional framework and way of working within Government that can enable PPP projects to proceed effectively and efficiently.

Our conclusions were that a comprehensive PPP law was not needed at the present time, but if there is a need for such a law in the future, Government could consider use of a draft of such a law we have provided in the Appendices to this report. From a legal standpoint, such umbrella laws are not required to undertake PPP in a common law system, but Government may choose to enact such a law in order to facilitate national consensus regarding how PPP arrangements are to be undertaken, or to simultaneously fill gaps in existing legislation.

For the immediate and interim terms, we have drafted certain amendments to existing laws and regulations, and have provided those drafts in the Appendices to this report. Those should be sufficient to mobilize the national PPP program, and leave intact sufficient flexibility within the legal framework to adapt to changing demands as the PPP program evolves.
C. PPP Institutional Framework

Introduction

Many of the Sector Ministries and State-Owned Enterprises have already implemented, or have begun the development of, PPP projects. While this situation bodes well for future PPP project “deal flow,” the development of such projects in the absence of a fully developed national PPP framework has created, and will continue to create, potential unforeseen fiscal risks to the national Treasury. For this reason, the IP3 team has emphasized fiscal management, public investment planning, and careful analysis of contingent liabilities in its design of the national PPP framework. The institutional set-up of a National PPP Steering Committee and its related technical unit in the Ministry of Finance, the PPP Secretariat, is designed to introduce systems that will enable PPP activity to continue, without creating undue and/or unanticipated fiscal burdens in the years to come.

In establishing the PPP Secretariat, we suggest a phased approach to its staffing according to PPP framework development needs and “deal flow” demand. In the early stages of the new PPP program, the Secretariat will be involved in a lot of activity relating to development of the new PPP framework, conducting legislative initiatives, preparing guidelines, disseminating information, and building capacity in sector ministries and local government bodies, from which future PPP deal flow will originate. As such capacity builds, the deal flow will increase, and the Secretariat will become more focused on the management of PPP project life cycle processes and procedures.

The PPP Secretariat will need to immediately process certain PPP transactions that have been proposed by sector ministries, local government bodies, and private sector sponsors. There is a perception that Treasury has been an impediment to the progress of those transactions. In reality, Treasury has appropriately been waiting for this consultancy to complete its design of the new PPP framework so that the transactions can be handled in the proper manner.

Key roles recommended for the PPP Steering Committee and its Secretariat are:

**PPP Framework**
- Champion the PPP process and promote understanding and awareness of PPP among key stakeholder groups, especially labour;
- Development of the PPP policy, legal, and institutional framework;
- Establishing of PPP standards, guidelines and procedures; and
- Remediation of constraints to implementation of PPP arrangements.

**PPP Information Dissemination & Standardization**
- Serving as a resource centre for best PPP practices in Kenya;
- Oversight of the application of standards, guidelines, and procedures at all stages of the PPP project life cycle;
- Development of standard procurement and contract documents; and
• Development of standard procedures for conceptualisation, identification, prioritisation, development, assessment of PPP projects.

**PPP Communications & Capacity Building**

• Promoting and marketing of sound PPP projects for use in infrastructure development;
• Communicating the Government's PPP policies to government Ministries and departments, potential private investors and other stakeholders, including consumers;
• Support capacity building in PPP project; planning, co-ordination and contract monitoring skills for Kenya’s public sector; and
• Work as the focal reference point for PPP advice.

**Establish and Enforcing Standards for PPP Projects**

• Manage the design and development of PPP Policy & Procedures Manuals to be followed by Sector Ministries, PPP Nodes, and the PPP Secretariat itself;
• Lead, drive, and co-ordinate the PPP programme through the full project cycle;
• Establish standards for monitoring and compliance of PPP contracts to ensure that key risk factors pertaining to Treasury financial exposure do not get out of hand during the concession period; and
• Conduct studies to determine whether a Project Development Facility (PDF) should be established, and if so then what should be the funding.

**Fiscal Accountability & Approvals**

• Coordinate with the Office of the Accountant General regarding PPP project financial reporting, and with the Office of the Controller and Auditor General regarding audits of PPP projects per the Public Audit Act, 2003;
• Assess direct and indirect liabilities and contingent liability risk exposure of the Treasury for proposed PPP projects, and consult with the Debt Management Department (DMD) in the MOF, to agree the acceptability of such liabilities;
• Consult with the Ministry of Planning & National Development to ensure that all PPP projects fit into the Medium Term Expenditure Framework; and
• Coordinate with the Public Procurement Oversight Authority to ensure that all tender phase activities of PPP projects conform to procurement regulations.

The functions of the PPP Steering Committee and its Secretariat specifically exclude the following functions performed by other stakeholders in the PPP program:

• Promotion, sponsorship, and development of individual PPP Projects;
• Direct PPP Project Management (the PPP Secretariat only monitors contractual factors that could create potential financial exposure to Treasury);
• Technical advice on specific projects that are within the capacity of sector ministries, state agencies, public enterprises, and local government bodies;
• Decisions regarding major (or flagship) projects will remain with the Cabinet; and
• Final Procurement oversight and appeals will be responsibility of the PPOA.
The PPP Steering Committee and its Secretariat will take primary responsibility for media and public awareness activities, as such are appropriately performed by the national focal point of the PPP program. Other stakeholders will, however, be expected to contribute logistical, financial, in-kind, and other kinds of support to such activities wherever possible.

**Key Supporting Structures to the establishment of a National PPP Secretariat**

To strengthen the capacity of PPP delivery, there are a number of supporting structures, which need to be developed, these are:

**PPP Nodes**: located in sector ministries, state agencies and Public Enterprises. Their focus is the starting point of PPP deal flow generation. While the PPP Secretariat reviews and either approves or disapproves proposed PPP projects, the PPP Nodes play a critical role in selection, promoting, sponsoring and development of PPP projects. Within each such Government ministry, agency, or enterprise, there should be at least one person who is designated as the person in responsible for a particular PPP project. The designation of the person to perform this role in each organization will be its Accounting Officer, as defined in the Government Financial Management Act.

**Steps in PPP Secretariat Project Appraisal**

The PPP Nodes will focus on PPP project conceptualisation, identification, prioritisation, and pre-feasibility analysis. They will “feed” new PPP deals up to the national PPP Steering Committee via its PPP Secretariat in the Ministry of Finance. The Secretariat will perform project appraisal activities. There will be several levels of such appraisal activities. The first level will be an evaluation of the pre-feasibility study prepared by the public sector agency promoting or sponsoring the project. Secretariat approval at this stage clears the sponsoring agency to publish a Request for Qualifications.

The next step in the project appraisal process is a review of the feasibility study, which should have been prepared by independent consultants contracted by the sponsoring public agency. Secretariat approval at this stage clears the sponsoring agency to publish a Request for Proposals. The final step in project appraisal is the Secretariat reviews the selection process and clears the sponsoring agency to enter into contract negotiations with the Preferred Bidder. The PPP Secretariat will play an advisory role in the contract negotiations, and will invite a representative of the Debt Management Department to join in the negotiations, to ensure that contract negotiations do not result in a financial exposure that will be unacceptable to Treasury.

**Political Limitations to PPP Secretariat Appraisal/Approval**

All of the above-described PPP project appraisal procedures apply to a situation in which Treasury funds and/or acceptance of direct or contingent liabilities are required. If the sponsoring agency or enterprise proposes to fund all of the public sector costs of the project from its own budget, it will not be required to pass through the Secretariat’s project appraisal and approval processes. This is a matter of considerable political sensitivity. Funds allocated to sector ministries in the budget process are not supposed to be without “strings attached” but in practice sector ministries treat such funds as their own and resist interference in their spending decisions. Similarly, accumulate profits of
public enterprises are supposed to be paid to Treasury as dividends, after deducting the amounts agreed for investment programs, but in practice the public enterprises tend to treat such funds as their own and resist interference in their internal spending decisions. These political factors preclude this Consultancy from designing a PPP Framework that has the full authority to ensure proper fiscal control over PPP projects. Perhaps as the national PPP framework develops, sector ministries and public enterprises will become more willing to accept PPP Steering Committee and Treasury oversight into how they invest their funds in PPP projects, but for now the role of the PPP Steering Committee and its PPP Secretariat will have to remain one of an advisory nature when the public sector investment requirements for a PPP project are to be funded entirely from the funds available internally in sector ministries and public enterprises.

The factors described above apply even more to local government bodies, because much of their funds are derived from local revenues. There are some budget allocations from Treasury to local government bodies, but not enough to enable the new PPP framework to require local government authorities to subject themselves to project appraisal and approval by the PPP Steering Committee and its PPP Secretariat.

**Project Development Facility (PDF):** It might be appropriate to set up a PDF if there is a need for funding to cover feasibility studies. At the present time, there appears to be no need for such a Facility, as government bodies sponsoring PPP projects have been funding feasibility studies from their own budgets, but as the PPP program progresses, increased volume of PPP activity might begin to strain the internal financial resources of public sector project sponsors and a PDF will need to be considered. In this report, we have included a PDF in the organization design, to accommodate a potential future need for such a Facility. In order to access PDF funds, projects will have to pass through the PPP Secretariat’s project assessment process, up to the point that feasibility studies are required. In practice, this will mean the project sponsors will have to finance their own pre-feasibility studies, which the PPP Secretariat will review and decide if the project has sufficient merit to proceed to the next (feasibility) stage. Then the PDF will use its own criteria to decide whether to provide funding for the feasibility study.

**Clarification of Decision Making for PDF**

The PPP Secretariat does not serve as the first step in obtaining approval by the PDF for use of its funds to support feasibility studies. PDF management makes its own decisions regarding which applications for assistance will be accepted. However, as a practical matter, the PDF is not going to consider any application from a project that has not been appraised by the PPP Secretariat up through approval of the pre-feasibility study and clearance to publish the Request for Qualifications. Without this requirement, the PDF would have to duplicate appraisal work that should already have been performed by the PPP Secretariat. Similarly, applications for PDF assistance cannot go directly to the PDF; they must come from the PPP Secretariat. Without this procedure, the PDF would be inundated with scores of applications for assistance with projects that have not been subjected to the Secretariat’s project appraisal process.

The IP3 team appreciates the importance of segregating the responsibilities of project development and project appraisal. For that reason, we have carefully segregated the
duties of the PPP Nodes and the PPP Secretariat; the former does development, and the latter does appraisal. In the case of a PDF, clearly the role of a PDF is development, so at first glance it might appear inappropriate to have the PPP Secretariat involved at any stage of a project’s move into the PDF system. But in practice, maintaining a complete segregation of duties between the two would require duplicating some PPP Secretariat project appraisal functions within the PDF, and that would be inefficient.

**The PDF Decision Process**

So the design is the PDF will contract directly with sponsoring agencies for the provision of consulting services to perform feasibility studies, but for the reasons cited above the sponsoring agencies may not apply directly to the PDF for funding. They must first pass through the pre-feasibility assessment phase of the PPP Secretariat, which will then assess whether the project has sufficient merit to request PDF assistance. Then the Secretariat submits its recommendation for assistance to the PDF. Then the PDF takes its own decision, based upon its internal evaluation criteria, regarding whether it will award such assistance and how much assistance will be granted. Such criteria include not only the merits of the project, but also the internal risk profile of the projects already in the PDF portfolio. Some will be high risk (with “risk” meaning probability of never reaching financial closure, so no winning bidder to reimburse the PDF its costs) but high reward (with “reward” meaning project benefits to the country) while others may be in the categories of low-risk-low-reward and medium-risk-medium –reward. The internal risk profile of the PDF project portfolio will have other characteristics, such as size and nature of services to be provided. PDF management will take its own funding decisions, based on such internal criteria, independent of PPP Secretariat preferences.

**Risk Management Assessment:** a National PPP Secretariat, as part of its fiscal approvals procedures, is required to assess known direct liabilities obligations, which commit Government’s under PPP private sector contracts. In addition, there are also indirect or contingent liabilities to which Government is subjected which should be assessed, in terms of appropriate ‘risk’ transfer in the PPP contract to the private sector. Indirect or contingent liability PPP contracts need to be reviewed by specialist risk management personnel, which need to be provided to the MOF’s Debt Management Unit (DMD). With such additional capacity, the DMD will advise the PPP Secretariat as to what contingent liabilities should be accepted, and what reserves should be booked.

**Consultative Nature of the Relationship**

It is important to note that the relationship between the PPP Secretariat and the Debt Management Department, Public Procurement Oversight Authority, and the Ministry of National Planning & Development is a consultative relationship, i.e. the Secretariat does not require their “sign-off” in order to recommend a PPP project to the PPP Steering Committee. As a practical matter, however, it is unlikely that the Steering Committee will approve a project submitted by its Secretariat if concurrence has not be obtained from these three government bodies. Similarly, the Committee is unlikely to approve a project recommended by its Secretariat if there is no clear concurrence from Investment Secretary and Permanent Secretary of Treasury. Technically, the Secretariat does not require their approval, but in practice the Committee is likely to be very cautious about a project proposal that does not have indications of such concurrence.
Below we provide more specific recommendations for creating the institutional framework.

**Recommendation 3: Institutionally Separate the Functions of PPP Project Proposal vs. the Function of PPP Project Review and Approval/Disapproval**

A key the preventing conflicts of interests in the development of PPPs in Kenya is through the clear separation of the functions of: (1) identifying and developing a PPP project proposal (sector ministry, public enterprise, or local government body, with its associated PPP Node); (2) reviewing and analysing the proposed PPP project (PPP Secretariat); and (3) either approving or disapproving the proposed PPP project (PPP Steering Committee and/or Cabinet). In keeping with their mandates of making infrastructure sector policies and of realizing key infrastructure goals, such as those contained within Vision 2030, each Sector Ministry will be responsible for identifying which projects it wants to implement and whether it intends to develop them through conventional procurement or through PPP. However, under the initiative we have proposed to be implemented via a Notice from the PS-Treasury that Accounting Officers must at least consider PPP as a means of “efficient and effective” use of public funds, per the Government Financial Management Act, all government agencies and public enterprises must at least consider PPP. At the local government level, such requirement is not conveyed by the GFMA, though cooperation with this concept is requested from Local Authorities and City Councils.

Each PPP project must be subjected to an objective, transparent, and systematic review. This is necessary to ensure that both the overall goals of the proposed PPP are consistent with national priorities offering attractive returns to the Kenyan economy, and especially to ensure that the proposed PPP will offer Kenya better value for the public’s money than other options for the project, or other alternative projects. It is not uncommon for Sector Ministries to prepare and actively promote new PPP projects based upon the planned technical, quality of service, and access to service benefits that they will provide in the sector, but not to fully consider the long term costs and contingent liabilities the PPP contract would impose on the Treasury’s limited fiscal resources. By having each PPP reviewed according to a clear, systematic, and transparent set of standards by the PPP Secretariat, this will ensure that only those PPPs that offer the clear benefits of better value for the public’s money can be approved. Such transparent standards would include analysis of such questions as those contained in the box to the right.

<table>
<thead>
<tr>
<th>Key Tests for Objective PPP Project Review</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Is the PPP affordable to the line ministry and end users?</td>
</tr>
<tr>
<td>2. Have all risks been adequately identified and analyzed and is there appropriate risk transfer to private sector?</td>
</tr>
<tr>
<td>3. What is the full value of Government’s contributions to the PPP, including all contingent liabilities it may bear during the entire contract term?</td>
</tr>
<tr>
<td>4. Does this PPP project offer the Government and end user’s better value for money than would other options?</td>
</tr>
</tbody>
</table>

Therefore, if a Sector Ministry has not adequately prepared a PPP project, such as confirming if it is affordable, or that the proposed risk-allocation structure offers the best possible value benefits for the public’s money – then the clear and transparent evaluation standards of the P3CU can determine this, independent of the interests of the Sector Ministry. Of course the Sector Ministry may proceed with the project if the public sector side of its costs can be funded 100% from the Ministry’s internal budget, but if national Treasury resources are required the project will require approval from the PPP Steering Committee in order to proceed.
Recommendation 4: Location of National PPP Secretariat Should be in the Ministry of Finance (MOF)

Although the PPP Steering Committee is a stand-alone entity, we propose that its technical unit, the PPP Secretariat, will be housed in the Ministry of Finance.

Key Issues and Options
In the second Interim Report, we suggested five possible locations, plus the option not to establish a National PPP Secretariat. The locations considered were the following:

- Ministry of Finance
  - Debt Management Department (DMD)
  - Department of Government Investment & Public Enterprises (DGIPE)
  - Establish own PPP Department/Unit or Secretariat
- The Public Procurement Oversight Authority (PPOA)
- The Privatisation Commission
- Ministry of Planning and National Development (MPND)
- Ministry of Trade and Industry / Kenya Investment Authority

Following an analysis of structures required for a PPP Secretariat, and following the July 2007 consultation with GOK decision makers on the PPP Policy, Legal and Institutional Framework, it was decided to establish an independent PPP Steering Committee and a PPP Secretariat in the MOF. Below is a recap of the identified advantages and disadvantages of this approach:

Table 2: PPP Secretariat in MOF – Advantages/Disadvantages

<table>
<thead>
<tr>
<th>PPP Secretariat in MOF</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Close to the existing resources within the MOF e.g. PPOA, DGIPE and DMD and reporting structure of new Privatisation Commission.</td>
<td>May be seen as part of bureaucratic organisation</td>
</tr>
<tr>
<td></td>
<td>Provides status and clear identity for the Unit.</td>
<td>Could be difficult in recruiting the level of staff required if place on civil service status</td>
</tr>
<tr>
<td></td>
<td>New organisation and flexible enough to support new concepts and share resources</td>
<td>Perceived poor track record in managing public awareness, education &amp; capacity building role required in PPP development</td>
</tr>
<tr>
<td></td>
<td>Has a combination of existing resources and own independent staff</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Keep overall operational cost reasonable low</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Simple as start up mechanism</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Legally simply to create and could commence work quickly</td>
<td></td>
</tr>
<tr>
<td></td>
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</tbody>
</table>

Establishing a PPP Secretariat within the MOF offered the simplest option for implementing a speedy start-up, urgently needed to respond appropriately to PPP projects already being proposed by various stakeholder government bodies and private sector sponsors. The only alternative option with merit was the establishment of a PPP Secretariat or Department within the Privatisation Commission, because technical skills in the PC would be similar to the technical skills required in a PPP Unit. The full analysis of his option is contained in the Second Interim Report, but we have provided a summary of the advantages and disadvantages below.
Table 3: PPP Unit in Privatization Commission – Advantages/Disadvantages

<table>
<thead>
<tr>
<th>PPP Unit in Privatization Commission</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Advantages</strong></td>
<td><strong>Disadvantages</strong></td>
</tr>
<tr>
<td>• The management skills and work closely correlate with the needs of a PPP Unit, in terms of transaction, project management, procurement, and contract negotiations</td>
<td>• PC may dominate the PPP Unit, which would then not have its own identity</td>
</tr>
<tr>
<td>• The need to communicate with stakeholders and ensure transparency, openness and fairness in its dealings</td>
<td>• Difficult to reconcile general sales of assets and PPP special support needs</td>
</tr>
<tr>
<td>• Strong procurement, pre-contract monitoring &amp; compliance role required</td>
<td>• The PC will come into conflict with PPP main clients and sponsoring stakeholders</td>
</tr>
<tr>
<td>• New organisation and flexible enough to support new concepts and share resources</td>
<td>• PPP Supporting and enabling role of sector ministries and SOEs etc in stark contrast to the PC's roles and relationships</td>
</tr>
<tr>
<td>• Working as semi-autonomous organisation</td>
<td>• Public, stakeholders, including labour unions etc. will not distinguish between privatisation and the more positive role of PPP</td>
</tr>
<tr>
<td>• Remuneration package sufficient to attract private sector experience and skills sets.</td>
<td>• Risk that the PPP will not act as unifying unit for PPP and line ministries will do their ‘own thing’</td>
</tr>
<tr>
<td>• The PC has currently no past ‘baggage’ of privatisation or conflict with sector ministries to date</td>
<td>• PPP Contracts and evaluation of private sector partners are critically different</td>
</tr>
<tr>
<td></td>
<td>• PPP projects are for 20 to 30 years and not just a ‘sale’ approach</td>
</tr>
</tbody>
</table>

The PC option has the advantage of housing PPP project appraisal activity within a semi-autonomous body, which has the capability of recruiting skilled personnel at compensation packages that can compete with the private sector. A PPP Secretariat housed within the MOF might be constrained in the area of compensation, and might also become tied up in the internal bureaucracy of Treasury. However, the PPP Steering Committee is a semi-autonomous body, and its technical unit, the PPP Secretariat is thus also semi-independent despite it being housed physically within the Ministry of Finance. We see no reason why, with the right classifications, the PPP Secretariat would be unable to offer compensation packages sufficient to compete with the private sector and attract skilled personnel. As regards internal bureaucracy, we have given details regarding the “consultative relationship” in a previous section of this report.

Based on our analysis and stakeholder consultations, our recommendation is to establish a PPP Secretariat in Treasury, reporting to the Permanent Secretary, with guidance from the Investment Secretary, and with consultative relationships with the Debt Management Department, the Public Procurement Oversight Authority, and the Ministry of Planning & National Development.

**The PPP Secretariat reports to the PS-Treasury in his capacity as Chairman of the PPP Steering Committee.** The PPP Secretariat is not a Treasury body, but it is physically housed in Treasury to facilitate its important consultative relationships with the Debt Management Department, Public Procurement Oversight Authority, and the Ministry of Planning & National Development. Although the PPP Secretariat will not need their approval to recommend a project to its Steering Committee, their concurrence will be very helpful to the Committee in determining that the proposed project involves sustainable, acceptable levels of debts and contingent liability exposure, has conformed to procurement rules and procedures, and has met the requirements for inclusion in the Medium Term Expenditure Framework.  

The role of the Investment Secretary is guidance regarding the investment requirements of proposed PPP projects, and facilitation of the PPP Secretariat’s operational requirements and relationships within Treasury.
Recommendation 5: Adopt a Phased Approach to PPP Secretariat Development

Key Issues and Options
We recommend there be two phases in the formation of the PPP Secretariat: a start-up phase, which we have set out below, and a longer-term “mature” phase. For the start-up phase, we recommend the recruitment of four professional staff and one support person. This core team will be supported by consultants, who will be engaged on an as-needed basis to accommodate the fluctuating workload associated with PPP framework development and deal flow activities. The core team of 5 persons is based on international models of successful PPP programs. Many such international models include 1-2 full-time, resident advisors during the first few years.

In the early start up phase of the PPP Secretariat, we recommend to give the PPP Secretariat a professional face with a more hands-on role, rather than just an administrative role, to support sector ministries, public enterprises, and local government PPP initiatives. While we do not see the need to appoint highly specialized technical staff, there may be a need to bring on, in short-term capacities, some of the skill set’s listed in the below text box.

The emphasis should be on self-supporting senior and experienced officers, without the requirement of large numbers of junior and support staff. A PPP Secretariat with strong core staffing level of general expertise should be a very effective unit, delivering a critical evaluation of the sponsored projects through the various feasibility financial approval/disapproval stages, while leaving the final decision for PPP projects to the PPP Steering Committee and the Cabinet.

There is no need to create formal department structures to accommodate different activities required for the appraisal of PPP transactions. Although there should be separate functional groups when the PPP Secretariat grows in response to increased demand for its services, the groups will need to be separated by rigid departmental lines. A ‘matrix management’ approach can be utilized, enabling technical and supervision activities to be conducted across functional boundaries. There will be a need for staff to multi-task and work in cross-functional areas, especially on large projects, rather than simply focusing on individual or specialist project-specific tasks.

Specialized Skills Requirements for PPP Secretariat

- Banking & investment
- Asset management (utilities engineer)
- Risk management and project structuring
- Economic and financial analysis
- Infrastructure development and service delivery
- Bid and tender procedures and documentation
- Project promotion and marketing
- Legal contracts
- Contract compliance monitoring and management
- Transaction negotiation and analysis
- Affordability, value for money, and risk allocation
- Risk management
- Media Communications/Public relations
- Capacity building

Recommendation 6: Adopt a Phased Approach to Staffing Identification, Development, Growth, and Training

Key Issues and Options
As mentioned above, the number of staff required for the start-up phase will be determined by the initial workload for PPP framework development and PPP deal-flow. Therefore, we need to
take a very pragmatic view of initial staffing needs and secure the services of few well skilled personnel. Then appoint additional personnel according to emerging needs until the Secretariat has a core nucleus of staff, as suggested below. It is assumed that some basic operational PPP procedures and guidelines will be prepared by consultants very early in the PPP program, so that there will be operational policies and procedures in place to enable the PPP Secretariat and PPP Nodes to be effective at this commencement phase of their work. Until PPP Nodes can be formally established, PPP Nodes will consist of the Accounting Officer, or his/her designee(s), as defined in the Government Financial Management Act.

There is a common misperception that over time the level of a national PPP Unit’s staffing can be reduced as capacity is developed in the PPP Nodes. This is not correct, because the role of a PPP Unit is project assessment, whereas the role of the PPP Nodes is project development. This also means that to create PPP deal flow there is an immediate, and continuing need, for staffing and building capacity in the PPP Nodes. This process does not have to put a strain on national PPP program budgetary resources if sector ministries, public enterprises, and local government bodies agree to focus internal resources upon development of PPP Nodes.

In some countries, PPP Nodes have been set up by simply assigning selected existing personnel to be responsible for PPP projects. In such cases, care must be taken to ensure that the assigned personnel are allocated the time required to perform their new tasks. In all cases, however, there is a lot of capacity building required and that costs money. Most sector ministries, public enterprises, and local government bodies have existing and planned training programs that can be leveraged, but some additional fiscal resources will still be required to build sufficient capacity for PPP Node activities, which are critical to the success of any PPP program.

**Sub-Recommendation 6.1: Start Staffing with Small, Tight Group**

We set out in Appendix 4 the person specifications and job outlines for the start-up phase. The job outlines are written as performance contracts, and may be used accordingly. It is proposed that during the start up the Head of the PPP Secretariat will be very much a ‘hands-on’ position. Recommended positions for the start-up of PPP Secretariat are provided below:
Table 4: PPP Secretariat Staffing Numbers at Start-Up

<table>
<thead>
<tr>
<th>Positions Identified during the initial start up stage of the PPP Activities</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acting Head of Unit</td>
<td>1</td>
</tr>
<tr>
<td>Technical Staff:</td>
<td></td>
</tr>
<tr>
<td>- Legal/Contracts Specialist</td>
<td>3</td>
</tr>
<tr>
<td>- Financial Analyst</td>
<td></td>
</tr>
<tr>
<td>- Transaction Coordinator</td>
<td>1</td>
</tr>
<tr>
<td>Administrative Assistant</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL (start up option)</strong></td>
<td><strong>5</strong></td>
</tr>
</tbody>
</table>

Thereafter the PPP Secretariat could develop to a full core staffing level of 10 over the coming year, depending on progress in developing the national PPP framework and the extent of PPP project deal-flow, while adding some specialized expertise in areas such as economic analysis, risk management, engineering, and public awareness.

**Sub-Recommendation 6.2: Beyond the Start Up Phase, Build PPP Secretariat Team based on Demand, Needs, and Required Capabilities**

The aim with this sub-recommendation is to establish a minimum core of professional staff to deliver on the PPP Secretariat mandate. This can be added to if necessary, while we expect additional staff to appointed if required on ad hoc project-by-project basis. Any additional positions we expect to be project transaction Coordinators, depending on deal-flow. A summary of the positions and roles can be found in the following table.

Table 5: Summary of PPP Secretariat Key Positions

<table>
<thead>
<tr>
<th>Position</th>
<th>Summary</th>
</tr>
</thead>
<tbody>
<tr>
<td>Head of Secretariat</td>
<td>Serve as Spokesperson and Coordinator for the national PPP Program. Manage the Secretariat, with individual responsibility for high profile PPP projects. Spearhead development of the PPP Policy Framework. Interface with PPP Steering Committee</td>
</tr>
<tr>
<td>Legal/Contracts Specialist</td>
<td>Development of the PPP Legal Framework, ensure procurement and contracting are done properly, coordinate with the PPOA, perform PPP contract monitoring and compliance activities for contract provisions relevant to Treasury exposure</td>
</tr>
<tr>
<td>Financial Analyst</td>
<td>Financial projections and financial performance indicators, test for Affordability to GOK and end users, ensure tariff levels will be sufficient to achieve market level debt and equity returns, ensure Value for Money is maximized</td>
</tr>
<tr>
<td>Economic Analyst</td>
<td>Economic analysis of proposed projects, with special emphasis on checking to see if projects not achieving necessary financial returns should nonetheless receive GOK support</td>
</tr>
<tr>
<td>Risk Management Specialist</td>
<td>Perform preliminary assessment of direct, indirect, explicit, and implicit, actual and contingent liability risks of proposed projects, coordinate with Debt Management Department, and ensure that proper Risk Allocation is present in all new PPP projects</td>
</tr>
<tr>
<td>Engineer</td>
<td>Ensure that detailed engineering designs proposed will be able to meet Performance and Service Delivery Standards required in the bidding documentation</td>
</tr>
<tr>
<td>Transaction Coordinators</td>
<td>Manage the process, not the transaction. Assist communication and coordination between parties to PPP transactions helping to</td>
</tr>
</tbody>
</table>
Table 6: Illustrative Mature Phase PPP Secretariat Staffing Numbers

<table>
<thead>
<tr>
<th>Positions Identified for Core Staffing</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Head of Secretariat</td>
<td>1</td>
</tr>
<tr>
<td>Technical Staff:</td>
<td></td>
</tr>
<tr>
<td>o Legal/Contracts Specialist</td>
<td>5</td>
</tr>
<tr>
<td>o Financial Analyst</td>
<td></td>
</tr>
<tr>
<td>o Economic Analyst</td>
<td></td>
</tr>
<tr>
<td>o Risk Management Specialist</td>
<td></td>
</tr>
<tr>
<td>o Engineer</td>
<td></td>
</tr>
<tr>
<td>Transaction Coordinators</td>
<td>2</td>
</tr>
<tr>
<td>Public Awareness Coordinator</td>
<td>1</td>
</tr>
<tr>
<td>Finance &amp; Administration Manager</td>
<td>1</td>
</tr>
<tr>
<td>TOTAL</td>
<td>10</td>
</tr>
</tbody>
</table>

Sub-Recommendation 6.3: Remuneration & Status for PPP Secretariat Should be Commiserate with the Envisioned High Level Status

There is recognition in this project that to attract the required calibre of personnel, the PPP Secretariat might have to offer attractive compensation packages: “… as the set of skills needed to implement PPP transactions are in very high demand, it is important in recommending the structures of the PPP unit that the consultant should recommend to government the methodology through which the PPP unit can pay market rates to the Unit’s staff” to quote one of the comments received during preparation of reports for this consultancy.

The PPP Steering Committee (and therefore also its PPP Secretariat) is a semi-autonomous body and is thus able to avail itself of compensation arrangements that fall outside of the standard civil service schemes. We have examined compensation schemes available for use in state enterprises and have found that if a personnel classification for PPP Secretariat staffing can be arranged that conforms to state enterprise management and technical personnel, then attractive compensation packages can be offered. Further, if classification of the PPP Secretariat is a financial services organization, which it could properly be awarded given that its primary function is to arrange the financing of infrastructure and other projects by leveraging public...
funds with private investment, then compensation packages that are competitive with the private sector can be offered.

The methodology we propose is, therefore:

- Obtain state enterprise personnel classification for PPP Secretariat staffing, based on its government ownership and its mandate to arrange commercial service delivery; and
- Obtain financial services personnel classification, based on its mandate to arrange the financing of commercial service delivery projects, using private investment to leverage public funds.

Using the methodology proposed above, the PPP Secretariat will be able to offer compensation packages that are as attractive as those in the Privatization Commission, and which will be able to compete with the private sector in the recruiting market.

Sub-Recommendation 6.4: Utilize a Project Matrix Management Structure & Modus Operandi for the PPP Secretariat

The PPP Secretariat will need to function in a non-rigid manner, using matrix management in handling its projects, with key personnel for various functions overseeing the various projects.

This internal management structure relies on clear points of accountability and responsibility within a project management structure rather than fixed lines within a management hierarchy. There is less reliance on line management but a heavy reliance on very good project management reporting and monitoring systems. Professional and technical support staffs undertake the main core organisational deliverables through a systematic project management model. Depending on the type of project, functional specialists (e.g. Financial, Legal, Economic, etc.) all can also be involved in project transactions. The Project Matrix Management approach places less emphasis on hierarchical line management, with a very flat structure and ‘hands on’ approach to work and deliverables against specific deadlines. As one project ends, a new team is formed you appoint team leaders according to the person specifications required and not strictly by hieratical management structures. Figure 1 below illustrates this approach. To complement this project management matrix the PPP Secretariat can add ad hoc externally consultants according to the PPP specific project needs.
Knowledge Retention & Transfer Through Matrix Management Structure

The new PPP Secretariat should be a small and agile, and development of underlying support structures will require backup persons taking responsibility for particular PPP transactions. The Secretariat should also support cross training and development of professional and technical staffs within the Secretariat and the PPP Nodes and projects. The best way to achieve this is to have at least one senior person shadow another person, which highlights the benefits of adopting a matrix project management structure outlined above. We suggest the ‘shadowing’ can be simply allocation of responsibility to ‘shadow’, this will not necessarily mean attending meetings, only to ensure regular briefings with their counterpart to go through files and report issues and support quality assurance of documentation etc. This is one of the best ways of cross training and developing supporting professional and technical staff. This will ensure that a lot of the details of project management are not lost, and that there is a better appreciation of project tracking, monitoring, and recording of transactions.

Personnel Recruitment

An open and transparent approach to recruitment at all levels is a requirement to obtain the full confidence of the industry and the public. For the PPP program to achieve optimum success the public service guidelines for recruitment must be strictly enforced, and resources will need to be sourced from the private sector. It will not be possible, nor would it be appropriate, to compete with compensation packages of highly skilled technical personnel in private sector. We are not trying to establish a new boutique investment bank. However, compensation packages should be at least on par with those offered by the Privatization Commission.
Sub-Recommendation 6.5: Capacity Building of Staff of the PPP Secretariat Staff & PPP Nodes is Critical for Success

Training & development should be an integral part of the PPP Secretariat operational plan, from which training needs can be formulated. The text box to the right provides a list of documents that should be used in this process. A number of initial interventions have been identified to support the initial capacity building needs of the PPP Unit and its PPP Nodes. The overall aim is to build a strong PPP project management approach to accelerate the PPP work program proposed. The program focuses on key technical ‘process’ competencies that need to be developed by staff working together on PPP supporting functions.

Training and Development: Required Documents

| Three year Rolling Business Plan with an Annual Detail Work Plan (reviewed quarterly,) |
| Design of Annual Communications Plan to meet the internal and external stakeholders needs; |
| Develop an Annual Training and Development Plan based on core personnel competency models for professional PPP staff (PPP Secretariat and Nodes) and general PPP awareness and education program for public sector stakeholders, linked to the Annual Communication Plan. |
| Writing of recruitment Person Specifications (which should be reviewed as each vacancy occurs); |
| Preparation of comprehensive performance focused Job Outlines, linked to KPIs (annual, with bi-annual review), incorporating: Key task objectives, Criteria for success (KPIs) and Accountability up dated annual following performance review; and |
| Bi-Annual Performance Planning and Review (PPR) system with two-way feedback, linked to individual annual performance contract. |

Training and development should not be viewed as just a ‘time-off-the-job’ seminar, lecture, conference or workshop, etc. To support the overall staff training and development more initial emphasis needs to be placed on in-house workshops and skills transfer via on-the-job training. The overall approach is to work to ensure the transfer of skills through effective in-house training and shared experience, rather than to provide academic exercises.

The Head of the PPP Secretariat should assume overall responsibility for the training and development program. The aim here is to ensure that the training is accessible to all staff and stakeholders, rather than just seeking single international training for one or two personnel. This should be reserved for specialization, with the core concepts being delivered in Kenya during this start-up phase.

One idea will be for the PPP Secretariat to “twin” with a mature and well established PPP Unit in either South Africa or Europe to support training and sharing of information. South Africa has the advantage of proximity, and Partnerships U.K. welcomes such arrangements.
Recommendation 7: The PPP Secretariat Must Develop Effective Institutional Relations with All Critical Stakeholders

Key Issues and Options
In developing the policy framework for PPP, it is necessary to define the relationships between key stakeholders in the national PPP program. This is a sensitive area, as the following issues illustrate, given the assumption that Treasury will take the lead in the national PPP program:

- Should a Sector Ministry be required to subject its PPP project proposals to PPP Secretariat assessment for approval when the funds for the proposed public investment into the project are to be derived from the ministry’s internal budgetary resources?
- Should a Public Enterprise be required to subject its PPP project proposals to PPP Secretariat assessment for approval when the funds for the proposed investment into the project are to be derived from the PE’s accumulated profits?
- Should a Local Government Unit be required to subject its PPP project proposals to the PPP Secretariat’s assessment for approval when the funds for the proposed investment are to be derived in whole or in part from the LGU’s accumulated local revenues?
- If the PPP Secretariat and the Debt Management Department fail to agree on the contingent liability risks associated with a proposed PPP project, e.g., the Unit recommends that certain risks be allowed and the related liability for the contingent liability should be booked as a reserve, but the DMD does not agree, who makes the final decision?
- How should the PPP Secretariat deal with Private Sector Project Sponsors when they express an interest in mobilizing a PPP project they have developed at their expense?
- How will the responsibility of the PPP Secretariat to conduct PPP procurement in the proper manner interface with the oversight role of the PPOA?
- If the PPP Steering Committee and its Secretariat are established as a semi-autonomous body, how will it interface with DGIPE in Treasury?
- How will the PPP Secretariat interface with the Ministry of Planning & National Development and how will the PPP Secretariat’s project assessment activities interface with the MPND’s Medium Term Expenditure Framework?
- How will the contract management function within the PPP Secretariat interface with the Sector Regulators also tasked with ensuring contract compliance, and how will it interface with the Public Sector Operating Partners, also monitoring contracts?
- If a Project Development Facility is established, what will be its relationship with the PPP Secretariat and how will the two bodies interact in making decisions on PDF funding?

We recommend a preliminary “relationship” structure as illustrated in Figure 2 below.
The following sections discuss the institutional relationships in detail.

**Sector Ministry**

In the absence of a clearly-defined PPP framework, some sector ministries have taken initiatives for developing PPP projects without necessary interaction with Treasury to ensure that direct and contingent liabilities associated with the proposed projects, and decisions on the investing of public funds, are made in accordance with principles agreed with the International Monetary Fund. For Treasury to now step in, which it must to fulfil its legal mandate for the protection of public funds, and assert control over the financial aspects of those projects, is going to be a very sensitive situation, potentially drawing criticism from sector ministries, and will require absolutely clear “rules of the game” for PPP having been put into place.

Putting the “rules of the game” into place must begin with a very clear PPP Policy statement, vetted publicly with all PPP stakeholders, and formally with Cabinet via a Policy Paper, and the subsequent publishing of the official PPP Policy in the Gazette. This process will take time and in the current election year environment we cannot afford the amount of time required to make formal policy as a pre-condition to implementing the PPP program. Accordingly, we advise that the Minister of Finance passes PPP Regulations immediately using the power already given to him in the relevant Act. When the Minster advises Parliament of the Regulations, he can put a PPP Policy Statement on top of the PPP Regulations, to explain the basis of the Regulations. We provided a draft of the PPP Policy Statement in the First Interim Report.
Regarding the ongoing relationship between the PPP Secretariat and the sector ministries, there will be some resistance on the part of the ministries to Treasury oversight, to the extent that project development costs, e.g., pre-feasibility studies, paid by the ministries, and the portion of the PPP investments that will come from funds already appropriated to the ministry in the budget process, serve to give the ministries reason to object to Treasury “interference.” The position Treasury will need to take is that the funds were appropriated to those ministries subject to the utilization of those funds in accordance with Treasury regulations. The role of the PPP Secretariat will, therefore, be similar to that of an economic regulator. It will oversee the line ministries' financial commitments as regards development of PPP projects, and it will assess the direct and indirect liabilities, along with explicit and implicit contingent liabilities, associated with those transactions. As is the case with a good economic regulator, the PPP Secretariat must take care not to allow the impression that its decisions are biased by any financial, political, or industry capture and it must allow for both private and public consultations on important issues. Its decisions will need to be publicly announced, with full disclosure of the reasons for those decisions.

Public Enterprises

The relationship between the PPP Secretariat and the Public Enterprises will also be sensitive. The perceived “interference” of Treasury into the PE's decisions about how to invest its retained earnings will create a lot of resistance to PPP Unit oversight. The PPP Secretariat, if our design is implemented, will report to the Permanent Secretary – Finance, acting in his capacity as Chairman of the PPP Secretariat. The PS has been incorporated to serve as a holding company for all Government owned assets. Therefore, in its interactions with the PEs, the PPP Secretariat will be operating under the authority of the owner of all the assets of those Public Enterprises, as well as the shares of ownership in the Enterprises themselves.

However, shareholders do not usually interfere in day-to-day decisions of the enterprises they own, whether the enterprise is public or private. They appoint the Board of Directors, which in turn appoints the management team. These terms vary by country but the principle is the same. The Board sets corporate policy and agrees strategic plans. The managers operate the company as they see fit, within the policies and plans set by the Board. As shareholder's representative, the PS-Treasury would properly interact with Public Enterprises only at the Board level. But the PPP Secretariat will need to interact directly with Public Enterprise management in order to fulfill its mandate to ensure the proper management of public funds in developing PPP projects.

There is a political dimension to this PPP Secretariat mandate dilemma. For example, suppose the PPP Secretariat were to inform the Managing Director of the Ports Authority that in developing the existing container terminal they must leverage their funds by partnering with a private investor. The response from the M.D. could be, quite appropriately, that the Secretariat had no right to dictate how the Authority should invest its own retained earnings. The counter-argument could be that the retained earnings were to a large extent made possible by the public monopoly, therefore to a large extent those funds are public funds, and as public funds they properly come under the Treasury’s purview. Another counter-argument would be that all of those accumulated profits should be paid to the Treasury as dividends, except for those funds necessary for investment, and the amount necessary for investment would be lowered if the funds were leveraged by an investment by the private sector, using the PPP methodology.
We have proposed that the PS-Treasury could issue a Notice to all Accounting Officers (as they are defined in the Government Financial Management Act) informing them that their duties to use public funds in an “efficient and effective manner” includes the obligation to consider the use of Public-Private Partnerships as a way of leveraging public funds with private investment. This will not compel Accounting Officers to use PPP, but it will compel them to at least consider the use of PPP in their projects, and if the decision is not made to use PPP then they must give an explanation as to why that decision was made. If the explanation is not persuasive, the PS-Treasury would have the right to block the transaction on the grounds that it did not represent an “efficient and effective” use of public funds.

The State Corporations Advisory Committee (SCAC) has been making good progress in its efforts to reform the boards and management teams of Public Enterprises, to make them more commercially oriented and responsive to the market. For this reason, we selected for the local attorney on our team the person who is counsel to that Committee. If the PPP program works in cooperation and collaboration with SCAC, we believe that the PPP program will eventually gain acceptance in the PE community, with significant beneficial effects to the economy. Such collaboration may also enhance the Privatization Commission's ability to fulfil its mandate.

Local Government Units

The problems described above regarding the relationship between the PPP Secretariat and Public Enterprises will be even more pronounced in dealing with LGUs. There are several reasons for this, including: (a) much, though not all, of the fiscal budget of LGUs comes from local taxes, fees, and other forms of income other than national budget allocations; and (b) there is a history of resistance to national intervention into sub-national governance. This resistance has been reinforced by a global trend toward decentralization. With the rising independence of local governments, resistance to national government intervention has naturally grown.

So the national PPP Secretariat is going to have a hard time imposing the fiscal responsibilities associated with a national PPP program on local governments. There are also issues of local government personnel's capacity to conduct the project conceptualization, identification, and prioritization activities necessary to generate high-quality PPP “deal flow.” A possible solution would be to invest in a lot of training and capacity building, and to set up PPP Nodes in the key LGU organizations, and then give the Nodes a lot of technical support. Another solution could be to set up a separate, municipal-level PPP Secretariat and a municipal-level PPP program. We are not convinced that the political orientation (a polite way of referring to what some would term corruption) and the technical capacity of LGU personnel is such that any of the possible options referenced above would be viable at the present time.

There is hope, however, via the Budget Officer system maintained by the Ministry of Planning & National Development. The MPND oversees Budget Officers at all levels of Government and there is an established system of those Budget Officers working with technical officers in the various national and sub-national Governmental bodies to identify and evaluate all projects requiring public investment, for inclusion in the Medium Term Expenditure Framework. The technical skills of the Budget Officers are quite good, though more focused on economics than project financial analysis, and they could become the platform for developing what eventually
would become a network of PPP Nodes in local government authorities. This is another reason why the relationship between the PPP Secretariat and the MPND is of critical importance.

**Debt Management Department**

Although the PPP Secretariat is tasked with monitoring and enforcing the fiscal management and investment planning requirements of PPP projects, it must share that authority with certain other government bodies. One such body is the Debt Management Department, which has the legal mandate to define which fiscal liabilities Government should accept. The PPP Secretariat will make its recommendations regarding these matters, and its staff will include capacity to perform such analysis and make such recommendations, but it should coordinate its analysis with the DMD so that appropriate reserves for such liabilities are recorded.

The DMD does not presently have the capacity to perform analysis of contingent liabilities, but they certainly have those capacities regarding direct liabilities, in fact very sophisticated skills in that area. It is essential that the PPP program include the necessary resources to build capacity in the DMD for dealing with contingent liabilities. From an efficiency perspective, one might recommend that such capacity is already needed in the PPP Secretariat, so why develop it again with the DMD, but in practice the risk management capacity in the PPP Secretariat will be of a more general nature than the specific, technical capability that will be needed in the DMD. In the PPP Secretariat, the Risk Management Specialist will provide a general assessment of risks associated with contingent liabilities and other risks having a potential adverse fiscal impact, but that person will not be tasked with performing the statistical probability analysis that will be required in order for DMD to recommend the exact amount of reserve required.

**Private Sector Project Sponsors**

For the private sector, the term Project Sponsor can be used to refer to either the prospective operating partner, or the prospective financier or financing consortium. How should personnel in the PPP Secretariat respond when a financial institution, investor, or a financing consortium and/or investment consortium expresses an interest in financing a project? Although it is tempting to simply accept the offer if the terms seem attractive, such offers should be treated in the same way as unsolicited proposals from prospective operating partners.

In this section, we provide guidance for dealing with unsolicited proposals in the near term and in practice that should include mostly proposals already received. One does not want to make the mistake of putting in place a system that may be perceived as encouragement of unsolicited proposals, implied via the acceptance thereof. People need to understand that such unsolicited proposals are not the best way to conduct procurement, and the acceptance of such proposals should be terminated as soon as the competitive selection procedures are efficient enough to make acceptance of unsolicited proposals unnecessary. In the Appendix to this report, there is guidance on how to handle unsolicited proposals once the competitive selection procurement system has been adequately developed. For now, as an emergency interim measure, given the existing backlog of unsolicited proposals awaiting response, we offer the following suggestions.

Unsolicited proposals must be allowed, because such allowance encourages private sector innovation, a key benefit of the PPP approach. However, sound fiscal management requires
that all projects and project financings be subjected to a competitive selection process, to ensure that maximum Value for Money is attained. It is essential that Government streamlines bidding processes to minimize the time and cost required for bidders. Projects below a certain value can be processed through limited competition, direct negotiation, and/or direct award based on prior experience. But projects above a certain value set by Government must be competed. In the case of unsolicited proposals, competition can be required but some benefit must be given to the party submitting the unsolicited proposal, in recognition of the following factors:

- There is an intellectual property value associated with the proposed project's design and the engineering costs that have been incurred in developing the design;
- The proposer coming forward could save Government considerable time and expense in conducting a marketing effort to search for interested parties, or the proposer may have proposed a project for which there is presently little interest in the private sector;
- The nature of the proposed project might be such that to do a competitive tender would cost Government a considerable amount of time and money; and/or
- Entering into contracts based on direct negotiations in response to unsolicited proposals can greatly increase the speed at which important projects are developed.

The only acceptable way to enter into direct negotiations without competition is to publish the proposed project for a specified length of time in media approved by procurement regulations. If no qualified bidders express an interest in the project, then direct negotiations can proceed. But if one qualified bidder expresses interest then a limited competition between the two parties should be undertaken. If at least two qualified bidders express interest based on the publication then full competition is required. The publication is treated as a “market sounding” and then an RFQ is issued and the standard procurement process begins.

But the move into a standard procurement process does not eliminate the need to compensate the proposer for the factors referenced above in the check list. International best practice in dealing with unsolicited proposals provides the following basic options: (a) Bonus System; (b) Swiss Challenge; and (c) Best and Final Offer (BAFO) access.

In the Bonus System, the original proponent is awarded bonus points in either their technical proposal or cost proposal, or both. The bonus is usually in the 5-10% range. In the Swiss Challenge approach, third parties may compete for the project but the original proponent has the right to counter-match their proposals to win the contract. In the BAFO approach, all of the standard procurement procedures are followed but the original proponent is guaranteed access to the BAFO process, in which final negotiations for contract award are conducted.

Some countries also provide a mechanism for reimbursing the original proponent for their cost of developing the project, in the event that they do not win the contract. In South Africa, Chile, and Argentina the winning bidder reimburses such costs. In Indonesia and some provinces of India the Government provides such reimbursement, subject to certain terms and conditions.

We consider the direct reimbursement methodology to be problematic, because the costs that were incurred by the original proponent have to be audited to be reliable, and the final design
of the project often turns out to be somewhat different than the design originally proposed, so the value of the original project development work is diminished. Similarly, we consider the Swiss Challenge and BAFO approached to be excessively discouraging to other potential bidders. For Kenya, we believe a variation on the standard Bonus System would be appropriate.

Such “Modified Bonus System” would award 5-10% bonus points in scoring for the technical proposal, as a reward for innovation, and credit for “reasonable and necessary” development costs in the financial proposal. The proposal evaluation committee reserves the right to set the amount considered to be reasonable and necessary, thereby eliminating the need to audit costs represented by the original proponent. The financial proposal is scored on the basis of the total investment proposed, but a “credit” for development costs is deducted from the total investment that the prospective partner will have to actually disburse when the project is implemented.

In using the Modified Bonus System, winning third-party bidders have no obligation to pay the original proponent for its development costs because the proponent already received a benefit in the bidding process via the credit system, which enables them to propose a higher investment than they would otherwise have been willing (or able) to propose without the credit. If the proponent wins the bid, then the cost of the credit is covered by the entire project finance package, rather than becoming an individual burden to Government or the winning bidder. The Modified Bonus System also includes a feature termed “automatic short listing,” which means the original proponent is not obligated to submit an Application for Short-listing for the RFQ. In practice, any Bonus System assumes there is enough intellectual property value in the unsolicited proposals to warrant such reward. From what we have seen in Kenya, such value is rarely present, hence the need to get the competitive procurement system developed to the point at which unsolicited proposals no longer need to be accepted.

Public Procurement Oversight Authority (PPOA)

As discussed above in the section on DMD, the PPP Secretariat should have a consultative relationship with certain bodies within Treasury. This includes the PPOA, with which there should be an active, collaborative relationship. The PPOA has shown admirable initiative and foresight by having a consultancy prepare draft PPP Guidelines that are to be inserted into the Regulations for the Public Procurement & Disposal Act as a Schedule. Although PPP is not a procurement methodology (an issue that crops up from time to time) in all PPP transactions there is a procurement process (or tender phase), and that process must be subjected to the very capable oversight of the PPOAB, which will have the final “say” in all such matters.

For example, suppose the PPP Secretariat decides to use a limited competition tender for a new PPP project in an industry for which it is generally accepted there are only a few firms that are capable of implementing the project within the designated service delivery standards. When the project is recommended by the PPP Secretariat to its PPP Steering Committee, naturally the Committee members are going to note the limited competition procurement methodology, and will inquire as to whether PPOA has “signed off” on it. So even though the Secretariat has the right to go directly to its Steering Committee with a project recommendation, in practice they will need PPOA concurrence in order to obtain Steering Committee support.
Given that the project assessment tests of Affordability, Risk Allocation, and Value for Money are all natural investment management tests associated with a treasury function, in both the public sector and the private sector, one might conclude that the Unit should logically locate in the Office of the Investment Secretary. Although there is no doubt that DGIPE personnel have the sophistication and motivation to properly fulfill such a mandate, we are concerned about two factors: (a) the workload of DGIPE is already very high and is straining resources, so adding an additional area of responsibility might create a burden that would be hard to manage; and (b) a PPP Unit should have a mandate that is a bit broader than just investment narrowly defined, so setting it up as a separate Secretariat seems a better option.

However, all PPP projects will require investment of public funds, so it is essential that DGIPE play a role. We have accommodated this in our design by placing the Investment Secretary in a position of advising the PPP Secretariat regarding investment matters, and assisting it with its day-to-day operations (being physically housed within Treasury) as well as helping maintain its collaborative working relationships with other Treasury bodies.

Ministry of Planning & National Development (MPND)

The first step in PPP Secretariat assessment of a proposed PPP project will be to apply the Affordability test. How will PPP Secretariat personnel determine whether the proposed project is affordable? The first place they will look is the Budget. Within the Budget, there could be a “line item” that authorizes a certain level of expenditure for either this particular project or a class of project in which the proposed project logically fits. If there is not, the project has do be included in the next round of public investment planning, and that is where the Ministry of Finance and the Ministry of Planning & National Development have a key interface for the purposes of the PPP program. There needs to be a close and collaborative working relationship between the PPP Unit and the Planning Division of MPND so that potential PPP projects that have merit can find their way into the Medium Term Expenditure Framework, then into the national Budget. As described in the section above on Local Government, the MPND will also play a key role in enabling sub-national government bodies to develop new PPP projects.

Sector Regulators

Until the regulatory framework has been developed to the point that financially and politically independent economic regulators are fully operational and empowered, PPP projects are going to rely to some extent on “regulation by contract.” Because of this, we put a lot of material on PPP contract clauses, and appendix on PPP contract risks, into our First Interim Report. Within a regulation by contract system, there are four entities participating in the contract monitoring and enforcement process: (a) the public sector partner for the project; (b) the private sector partner for the project; (c) the sector regulator; and (d) the Contract Monitoring & Compliance functional group within the PPP Secretariat.

The day-to-day contract monitoring and enforcement activities are conducted by (a) and (b), who “keep an eye on each other” and use contract clauses relating to breaches and remedies for
ensuring that the other party stays in compliance. The entities referred to above as (c) and (d) play unique roles in a regulation by contract system. The sector regulator's focus is normally on pricing and the quantity and quality of service. The regulator is tasked with protecting all stakeholders to the project, which include the operating partners, the users of the service, and of course Government. The focus of the Monitoring and Compliance functional group within the PPP Secretariat is very different from that of the other three parties to the regulation by contract system. Their focus is on the activities that impact all of the factors taken into consideration by the PPP Unit when approving the project, i.e., activities that impact the Affordability, Risk Allocation, and Value for Money of the project. This focus is narrow, and is intended to be narrow so that the Secretariat is not expected to perform duties that are more appropriately within the purview of the other three parties.

Public Sector Project Sponsors

For the public sector, the term Project Sponsor is generally used to refer to the Government body that has proposed the PPP project. This means the Project Sponsor will generally be line ministry, local government, and Public Enterprise bodies. The relationship between the PPP Secretariat and the public sector Project Sponsor must be arm’s length because the PPP Secretariat is tasked with assessing the proposed project and making decisions regarding public investment. For this and other reasons, a PPP Secretariat is not directly involved in project development but rather limits its role to project appraisal thereby avoiding a potential conflict of interest. If the Project Sponsor has a PPP Node, it will be the Node that takes the lead in project development. There is a development role for the PPP Secretariat, but that is development of the PPP Framework, not the development of any particular PPP projects.

**Recommendation 8: PPP Secretariat Operational Procedures and Policies Need Definition and Development**

**Issues and Options**

The criteria for the establishment of the PPP Secretariat are set out in our analysis in the Second Interim Report. There are a series of operational considerations to ensure the PPP Secretariat remains focused to its designated role and efficient. The specific criteria established in this consultancy’s Terms of Reference¹ are:

- Ensure there is not another layer of bureaucracy, have streamlined administrative process, including small staffing numbers;
- The existing resources and institutional framework needs to be fully utilised, without duplication of functions, while respecting spheres of accountability;
- Any PPP Secretariat should act as a facilitator for PPP activity, with the institution capable of efficient implementation of PPP projects;

¹ Terms of References for the Establishment of PPP Framework Sub-Task 6
• The institution should be modelled on “outputs” rather than being process driven;
• Consideration should be given to an institution modelled on Project Management principles;
• Considerable use should be made of outsourced technical expertise at various stages of PPP preparation and implementation;
• Clear division of responsibility should be maintained between technical project feasibility and process regulation with respect to in-house and outsourced resources;
• Ensure fiscal accountability; and
• Appropriate measures for ensuring its independence from potential political, financial, and/or industrial capture.

A number of additional operational policies that we recommend should be adopted by the PPP Secretariat, include:

• The PPP Secretariat needs to address the existing PPP transaction gaps, once due consideration has been give to capacity building in the Sector Ministries responsible for promoting and sponsoring PPPs;
• The staffing of The PPP Secretariat should be demand-driven, based on deal-flow, and structured to support a more ad hoc ‘matrix project management’ approach rather than just fixed departmental static functions and structures.
• Specialist technical expertise, including legal, economic, investment banking, media communications etc., should be contracted externally according to requirements of particular PPP projects rather than build up permanent expensive internal capacity within PPP Secretariat or a PPP Node within the Sector Ministries, State Agencies and/or SOEs.

These three principles fit well with the goal of keeping the staffing levels small and flexible and that specialist or sector technical expertise can be contracted externally according to the needs of the possible larger scale PPP projects. This does not exclude the need for some basic in-house expertise to support projects and oversee standards as previously outlined, such as transaction management, financial and tendering personnel, in addition to project management and coordination needs, if the deal-flow demands require.

Below we indicate a number of additional sub-recommendations.

Sub-Recommendation 8.1: All ‘large’ capital investments in infrastructure must consider PPP options analysis before undertaking any new public investments and/or borrowings

The rationale for PPP is that it will support additional infrastructure development by leveraging financial resources in partnership with private sector investment. The aim is to accelerate public services to the consumers while improving the quality of life for Kenyans. This would require all Government institutions to analyze PPP options whenever possible as an alternative to placing additional financial burden on GOK borrowing capacity. Therefore, when proposing large-scale infrastructure projects, all public sector sponsors (including Ministries, public corporations, or other relevant public bodies) should include an appraisal of whether the project could be effectively and efficiently provided through a PPP, privatised or warrants direct public
funding. The definition of ‘large-scale’ financial threshold should be defined by the total budget for the PPP project, including private sector investment estimates. When this policy is implemented, it will have a profound effect on the ‘deal-flow’ of PPP projects.

Sub-Recommendation 8.2: The PPP Secretariat access to Government decision-making process should have final approval / veto power over all PPP projects

A centralised PPP decision-making process will have final say on PPP approvals/disapprovals, of all PPP project proposals. The PPP Secretariat is not to assume the responsibility of financial approvals or vetoes over projects itself. Rather, it will decide whether or not to recommend a particular project to its PPP Steering Committee. All final financial approvals will involve technical evaluation by the PPP Secretariat, supported by DGIE, DMD, PPOA, and MPND, then presentation to the PPP Steering Committee through the PS-Treasury in his capacity as Chairman of that Committee. Where appropriate, the Committee will make the final decision regarding the project, unless there is a requirement to obtain Cabinet approval.

The PPP Secretariat will enforce quality control and give support and guidance on the required criteria for financial approvals and project standards. The bulk of this work will be addressed through a PPP feasibility studies and the appointment of external expertise, as suggested below (and if required supported by a Project Development Fund (PDF) if the decision is made to establish it. This financial approval is additional to the need to undertake risk assessment of the contingent liabilities of the GOK associated with the PPP contract.

Sub-Recommendation 8.3: The PPP Secretariat should improve the quality of potential PPP projects by requiring clear standard procedures for ‘affordability and value for money and ensure the appropriate risk transfer’

This is in line with its project management and process management of transactions, through the PPP project feasibility procedures. This approach is different from the final PPP decision-making process, as suggested in above. The list and description of these required procedures is described below in the recommended outline for the PPP Policy & Procedures Manuals that will be prepared for the PPP Secretariat and PPP Nodes.

Sub-Recommendation 8.4: The PPP Secretariat will design implement PPP models, templates and standard operating procedures (SOPs)

This has already been accepted as a critical first step for the PPP Secretariat to perform.

Many of Kenya’s Sector Ministries and Public Enterprises are already engaged in or considering PPP project without the benefits of guidelines, operational standards, proper feasibility studies or PPP procurement output-led procedures. Within the PPP Policy & Procedures Manuals that will have to be prepared for the PPP Secretariat and PPP Nodes, it will be necessary to include Standard Operating Procedures and model documents for the procurement and contracting processes of PPP arrangements.
Sub-Recommendation 8.5: The PPP process should be decentralized as far as possible to the Sector Ministries’, State Agencies’ or SOEs’ own PPP Node

Many of the sector ministries, State Agencies, and Public Enterprises are already advanced in their development of PPP projects. The intent in setting up a PPP Secretariat is to support the transaction process, ensure consistency and quality of approach. The goal is to ensure the PPP Secretariat is small, non-bureaucratic in approach, with the aim is to decentralize as much as possible, allowing capacity to be build up in the within Sector Ministries, State Agencies or Public Enterprises’ own PPP Nodes once all the PPP criteria have been established.

Sub-Recommendation 8.6: The PPP Secretariat needs to be output focused rather than focused only on administration and monitoring.

The role of PPP ‘process management’ can be easily perceived as administrative and policing of standards and compliance with procedures. Therefore, it is important to ensure that the central PPP team tries to focus on delivery of institutional outputs. There are a number of factors, some of which are set out below, that are critical to ensure the PPP institution is output focused:

- Careful selection of PPP projects that meet initial selection criteria
- Procedures which are output-led and measurable
- Quick decision-making with timeline for project turnaround
- Small core PPP unit team with access to external specialist consultancy skills
- Staff appointed on performance contracts
- Regular reporting patterns and financial approvals sought
- Project matrix management structured for timely delivery across a range of projects rather than functional hierarchical civil/public service model
- Establish Action Plans with agreed timetables with stakeholders

PPP Secretariat guidelines or operational policy areas, which need to be clarified to support the day-to-day working, that is:

- As part of PPP planning, sponsors of PPP projects should be first ensure their inclusion in the MPND infrastructure plans, meeting the objectives of Vision 2030, ensuring there is no conflict in the relationship with the existing GOK/MOF protocols
- Classification of projects to enable fiscal approval procedural to set between sector ministries and Treasury, while incorporating existing budgetary approvals protocols
- Short-term service contract should not be classified as PPP projects. They should be treated as procurements and overseen by the PPOA and the implementing agency
- The sector ministries, in promoting and sponsoring a project, must manage the project team, but must include a representative of the PPP Secretariat at the concluding stages of PPP contract negotiations
- Sector Ministries, State Agencies and Public Enterprises need to spell out the general approval/decision-making structures
• The relationship between the PC and the PPP Secretariat in undertaking PPP projects is clarified, assuming the PC will address existing entities PPP proposals, once established, while following agreed PPP Secretariat regulations, guidelines, etc.
• Large ‘flagship’ or sensitive projects should have inter-departmental ‘Steering Committee’ reporting to the cabinet supported by their own Technical Project Team with guidance from the PPP Secretariat
• PDF for ‘second’ levels projects, especially those from local government, regional, and community projects.

Recommendation 9: The PPP Secretariat Must be Active in Fiscal Management & Public Investment Planning

Issues and Options

The primary purpose of the PPP Secretariat is assessing and mitigating risks, which means that its policies and procedures will focus on assessment, rather than on development. The assessment function is not only focused upon the internal aspects of each project, but more importantly is focused on the questions of whether undertaking the proposed project may create unacceptable contingent liabilities on the Treasury, whether the acceptance of direct and indirect liabilities associated with the proposed projects will be consistent with sound fiscal management practices, and whether the process of putting the project into the Medium Term Expenditure Framework and Budget is a process that reflects established principles of sound public investment planning.

The role of the PPP Secretariat in fiscal management and public investment planning, as part of the national Treasury, will focus on the following:

• Flag potential PPP fiscal risks in view of Kenya's public finance indicators;
• Employ safeguards to ensure effective financial control of PPPs, by clearly separating activities related to PPP promotion, technical oversight for PPPs, and financial control over PPPs;
• Performing a gateway function under the control of Ministry of Finance;
• Advise on legal options to limit PPP related-risks to the government (e.g., ceilings on exposure to PPPs—stocks and flows);
• Establish and enforce criteria and procedures for prioritizing investment projects and selecting PPPs;
• Determine whether donor support is likely to be involved in the PPP process, and, if so, what are the implications for fiscal risks and control;
• Recommend starting operations with small, manageable PPP projects, rather than "one or two large" ones) in order to build-capacity and limit fiscal risks.

The following are key components of the fiscal management policies:

• The PPP Unit's gateway function manages fiscal risks from PPPs. The proposal for a gateway process that is maintained by the Ministry of Finance has been standard advice the Fund has offered in a technical assistance context and is an essential device for the Ministry of Finance to maintain fiscal control. There is an urgent need for government/PPP
Secretariat approval e.g. at the contract negotiation and finalization stage. Accordingly, the PPP Secretariat will play an active role in the contract negotiations stage, ensuring that contract clauses are not introduced that could have an adverse impact on financial exposure to Government.

- Proposals for new PPPs will come from the Ministries in charge of delivering the relevant services, not the PPP Secretariat, whose main function is fiscal control. PPP Nodes within those Ministries will be responsible for ensuring that proposals meet certain minimum standards (technical control). This separation of different functions is essential for: (a) achieving incentive neutrality with regards to different procurement routes (i.e., whether to procure a project as a PPP or not, which should be decided on purely economic grounds); and (b) ensuring that there are no vested interests in a PPP that could influence its subsequent implementation decisions and assessments.

- The PPP Secretariat is tasked with anticipating fiscal risks from PPPs and seeking ways to limit them. In the detailed Operations Guidelines to be developed for the PPP Unit, there will be clearly defined decision criteria for performing this key task. In applying those criteria, PPP Secretariat officers will maintain a close focus on Kenya's public finance constraints and how they should influence assessments.

- The PPP Secretariat’s primary function is fiscal control. The assessment of contingent liabilities and fiscal risks will be done jointly by the PPP Secretariat and Debt Management Department (DMD) of the Ministry of Finance. The DMD does not have the authority to make final decisions regarding acceptance of contingent liabilities, nor does PPP Secretariat. Those decisions are made by the PS-Treasury subject to concurrence by the Minister for Finance. The PPP Secretariat will, however, make recommendations to the PS-Treasury as to which contingent liabilities should be accepted, as well as the amount of reserves that should be recorded to reflect those contingent liabilities. In preparing its recommendations, the PPP Secretariat will consult with the Debt Management Department, and when a project is proposed by the PPP Secretariat to its Steering Committee via the PS-Treasury acting in his capacity as Chairman of the Committee, there must be evidence of DMD consultation in the records pertaining to assessment of the PPP project being proposed.

**Recommendation 10: Establish a Timely Implementation Plan for the Establishment of the PPP Secretariat**

Table 7 below provides a recommended timetable for establishing the PPP Unit.
Table 7: Timeline for Establishment of the PPP Secretariat

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<td>Implement PPP stakeholder awareness building activities</td>
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Recommendation 11: Establish a Dedicated Source of Funds Available to Sector Ministries to Complete their Own PPP Project Analyses & Proposed Structures: The PPP Project Development Facility (PPP PDF)

Key Issues and Options
While infrastructure sector ministries, public agencies, and public enterprises in Kenya are clearly interested in many of the benefits that PPPs can offer, they do not consistently apply the established project development techniques of international PPP best practice. While having these sponsoring agencies perform or contract their own pre-feasibility studies may be advised, there may be a need to offer assistance in the provision of highly skilled independent consultants to perform feasibility studies. This would improve the quality of PPP deal flow.

PPP Feasibility analyses for medium-sized infrastructure projects may require from $100,000 to $300,000. Lacking these project preparation funds, many Sector Ministries may try to turn to private developers to conduct their own PPP feasibility studies and proposed risk structures. This puts the Line Ministry at the disadvantage of having to review a PPP project study and proposal clearly written in the interests of the private developer, it also pressures the Line Ministry to grant exclusivity to the developer and to limit the possibility for competition.

On the other hand, some sector ministries and public enterprises do engage skilled professional consultants, from internal budgetary resources, and the resulting reports are relatively good. In other cases, this process has been manipulated, according to the most recent report on public enterprises by the Auditor General’s Office, to give large value consulting contracts to business associates, friends, or even family members, the result of which is a poor quality report and loss of significant funds that could have been used to hire competent consultants.

The depth of study required to determine whether or not Kenya should establish a new Project Development Facility is not within the scope of this consultancy. If the lack of a PDF is viewed as a key reason for the relatively large volume of unsolicited proposals, and/or the misuse of internal consulting funds in sponsoring agencies, or if there are not sufficient internal funds in sponsoring agencies to hire qualified consultants to perform such studies, then there is a need for a PDF in Kenya. If the decision is made to create a PDF, the design and institutional relation
material in this report can be utilized. Funding for the PDF should include some Government funds, so that the Facility will not be excessively dependent on donor funding.

Because a PDF employs local consultants to the maximum extent possible, it might be possible to provide some of the funding for a PDF via a private sector development program. Kenya has a large and robust private sector, with many skilled workers who could do a good job preparing feasibility studies for PPP projects. Another source of potential funding would be the IFC and other project finance arms of multilateral and bilateral donors, because the PDF would be a way of generating high-quality deal flow of projects that they could then finance.

The figure below shows an illustrative PPP Secretariat and PDF structure, outlining the various institutional relationships and process flow. If the decision is made to establish a PDF, then a separate design exercise will be required because a PDF is a complicated mechanism, not simply a pool of money. A new legal entity has to be established, a separate bank account will be necessary, or a separate line item in the national budget, and professional fund management and accounting personnel will have to be hired to manage the funds entrusted to them, thereby conveying a fiduciary responsibility. Cost sharing arrangements will have to be worked out with project sponsors, and PPP procurement documents will have to be modified to insert the requirement that winning bidders must reimburse the PDF its project development costs.

**Figure 3: PPP Secretariat and PPP Project Development Facility Relationship**

The design of the PPP Project Development Facility makes funds clearly available to pay for this crucial feasibility stage of the PPP project lifecycle. To access the funds, sector Ministry and/or public enterprise and/or local government PPP Nodes must pass through the PPP Secretariat approval process up to the point of feasibility study. Then the PDF will consider an application for assistance. PDF management will make its own decision of whether or not to approve the
application, i.e. the PPP Secretariat does not make that decision. If the decision is positive, then
the Project Sponsor and the PDF-appointed Consultant will enter into a contract, which will be
overseen for consultant quality control by the PDF. Oversight of the day-to-day activities of the
Consultant will be performed by the Project Sponsor.

PDF Cost Sharing & Revolving Fund Dynamics

Assuming that a feasibility study for an average PPP project will cost on average US$300,000 a
Fund size of say US$9 million could support a portfolio of 30 of such-sized projects. With an
extra US$1 million for staffing and operational costs, total PDF investment is US$10 million.

This Fund’s longevity could be greatly enhanced if it operates on a revolving-fund basis. This
feature becomes available if winning bidders are required to reimburse the PDF for funds it has
expended on consulting services for preparation of feasibility studies. PDF capital resources
can be further leveraged by requiring sponsoring agencies to bear an agreed percentage of the
costs of procuring feasibility studies. A rough rule of thumb is a PDF will run out of money in
about 5 years if these features are not in place, and it will run out of money in about 10 years if
these features are in place. The reason why a Fund with the features in place eventually runs
out of money is some deals never reach closure, so there is no winning bidder to reimburse the
Fund for its project development costs.

Recommendation 12: Develop, Officially Adopt, and Distribute PPP Policy & Procedures
Manuals for the PPP Secretariat and PPP Nodes

Key Issues and Options

In order to ensure that the implementation of PPPs in Kenya delivers key goals like value for
money and that the conditions of affordability, competition, independence, transparency,
accountability, and other key priorities are met, PPP Policy & Procedures Manuals are needed
for the PPP Secretariat and the PPP Nodes. The project life cycle to be covered by such Manuals
is described in the figure below.

Figure 4: Phases of the PPP Project Lifecycle in Kenya

Kenya’s PPP Framework:
Phases of PPP Project Life Cycle

PHASE I: PPP Project Conceptualization & Initiation

PHASE II: PPP Feasibility Analyses & Proposed Risk Allocation Structure

PHASE III: PPP Tendering & Procurement

PHASE IV: Contract Signing & Project Financial Closure

PHASE V: Post-Award PPP Performance Monitoring
The overall process by which PPPs projects in Kenya advance from the very first initiation as a PPP concept all the way through to the completion of the contractual terms (often 20-30+ years), can be more easily understood according to five key Phases of the PPP Project Life-Cycle, as contained in the PPP Policy Statement.

The Manuals should describe the procedures for each of the clear stakeholders in the implementation of the PPPs in Kenya. Once the Manuals are developed and drafted by the PPP Secretariat’s consultants, they should be reviewed the PPP Steering Committee and also by key stakeholders in Government, especially the sector ministries and public enterprises. The Manuals should then be officially adopted by the Ministry of Finance as the implementing rules that PPP projects must comply with during each phase of their development. This measure will ensure that the Manuals are not simply a recommended guideline that Government ministries can choose to ignore if they wish, but instead are requirements. This will also enable the PPP Secretariat to give clear justification to any decisions to disapprove or reject PPPs that are submitted to it, when the project sponsor did not follow procedures for demonstrating key requirements like affordability, value for money, valuing and managing all fiscal risks, etc.

As depicted by in Figure 5 above, the Manual will describe each key procedure that needs to be performed by each stakeholder institution during each Phase of a PPP project’s development. Each Phase can be made of up of dozens of specific required procedures. For a more detailed outline of the PPP Policy & Procedures Manuals, please see the Appendices to this report. The sections below outline the phases of the project life cycle covered by the Manuals.
Phase I: PPP Project Conceptualization and Initiation
In the first Phase, PPP Nodes will conduct a systematic screening, using a model PPP screening checklist, on all of their planned, priority infrastructure projects to determine which ones might better delivered through PPP arrangements. For each project that passes this screening, the Line Ministry PPP Nodes will then prepare PPP Project Concept Papers for them. Based upon the information available for each project, which is likely to be incomplete and/or qualitative in nature, the PPP Project Concept Paper will seek to summarize the likely benefits and the requirements of a PPP. The purpose of the PPP Project Concept Paper is not to provide a complete analysis of a potential project’s feasibility, but instead to allow the P3CU and the PPP PDF Board to determine if the given project candidate exhibits the initial indications that it would likely make a strong candidate for a PPP after detailed analyses of its feasibility as a PPP, including a proposed risk allocation structure were proposed. Each PPP Node should be able to complete these Phase I procedures and reports without requiring outside PPP project consultants. Thus, the Phase I PPP Concept Paper should focus on deciding whether the PPP PDF’s limited resources should be invested in the further development of the project or not.

Phase II: PPP Feasibility Analyses & Proposed Risk Allocation Structure
Phase II focuses on completed systematic analyses of the potential project’s feasibility as a PPP. Phase II’s procedures would require PPP Nodes to be supported by experienced PPP project consultants to complete these required analyses. This include specifying the project’s important required output levels of service, identifying and consulting stakeholders, conducting demand analysis, technical feasibility analysis, financial feasibility analysis, economic feasibility analysis, as well as environmental, legal, and institutional feasibility analyses. Secondly, Phase II also requires the identification and analysis of all material risks to the PPP, and especially the important proposed risk allocation structure for the project as a PPP. The PPP Node submits these feasibility analyses and proposed PPP risk structure to the PPP Secretariat, which reviews them for completeness, quality, and especially to determine if the proposed PPP is still affordable and still offer better value for the public’s money. The PPP Secretariat then either approves or disapproves the project’s advancing to Phase III’s tendering & procurement. The PPP Secretariat also recommends to the PPP PDF Board whether or not further funds should be spent on supporting the Phase III’s tendering & procurement procedures.

Phase III: PPP Tendering & Procurement
Phase III also assumes that PPP Nodes will require the experience of PPP transaction advisors to prepare and manage the overall tender and to help ensure its reaches a successful conclusion. Key procedures under this phase include ensuring that all required pre-tendering reforms are completed (acquiring access to needed land, finalizing plans for the management of any labour-impacts, clarifying issues of public asset ownership or debts owed, etc.); drafting Requests for Qualifications, draft PPP contracts, evaluating bidder qualifications received, and drafting Final Tender Documents. The PPP Secretariat will review Final Tender Documents prior to their release to ensure quality and also to update appropriate affordability and value for money analyses in case of any material modifications to the project’s scope of risk structure. The Line Ministry then issues the Final Tender Documents and receives and evaluates both technical and financial bids. The award decision by the Line Ministry and the final version of the PPP contract must first be reviewed by the P3CU to ensure its appropriateness and fairness, and to reconfirm the project’s final affordability and value for money levels.
Phase IV: PPP Contract Signing & Project Financial Closure

Given the size and complexity of large, infrastructure-related PPPs, there can often be an important amount of technical details that must be agreed upon after the award as “Schedules” and attachments to the PPP contract. It is important, however, that such post-award discussions and negotiations not seek to change the fundamental risk allocation structure of the PPP contract. Post-award technical discussions and negotiations can take several weeks or even months to conduct, and it is important that managed smoothly and effectively. Phase IV provides guidance for how PPP Nodes should ensure this happens. Additionally, the long-term lenders to PPP projects, such as local & international commercial banks, and even the private sector arms of MDBs, need to see the final version of the PPP contract and its schedule before they can offer clear financing terms to the winning private investor. This process of negotiations between the winning private investors and their chosen lenders that occurs after the PPP contract signing can takes several months to complete (6 to 9 months is not uncommon for larger, PPP pilot transactions). Sometimes such negotiations fail, leaving the winning bidder unable to begin to construct or operate the new project, and exposing the Government to the risk of the project not happening at all. Although this process does not directly involve the Government, the Line Ministry must still be aware of the requirements of the project financial structuring process, available to provide clarifications if needed, and also capable of monitoring the winning bidder’s progress in reaching financial closure.

Phase V: Post-Award Performance Monitoring

While the process of advancing from Phase I through Phase IV may take 2-3 years for large PPP projects, the full contract term of the PPP often takes 20-30+ years. This Phase includes procedures for establishing Project Monitoring Committees, for monitoring progress during construction, monitoring progress during operations, managing periodic requests for adjustments in prices, mechanisms for resolving PPP contract disputes, as well as procedures to follow at the end of contract close-out and expiration stage.
Chapter 3. Conclusion

This consultancy has determined there is already a significant amount of PPP activity underway, there is a large and robust private sector expressing keen interest in participating in PPP projects, and there is substantial potential in Kenya for the use of PPP in accelerating development of infrastructure.

To more fully develop the Policy, Legal, and Institutional Framework for PPP in Kenya we have prepared a National PPP Policy Statement, a series of legislative initiatives, and a design for the establishment of a National PPP Steering Committee and PPP Secretariat. The Legislative Initiatives are summarized as follows:

Near Term:

Include within the current Finance Bill, either by amendment or insertion, minor amendments to the Public Procurement & Disposal Act and Government Contracts Act, and exempt all PPP arrangements from the capacity building levy.

Pass subsidiary legislation in the form of regulations under the Public Procurement & Disposal Act, Privatization Act, Government Contracts Act, State Corporations Act, and the Government Financial Management Act, to provide procedures for PPP Arrangements.

Long Term:

If Government deems it appropriate, enact a State Entities (PPP Arrangements) Bill that will fill gaps for PPP in legislation pertaining to State Corporations and Local Government Authorities.

The Institutional Framework design is summarized as follows:

- Establish a National PPP Steering Committee as a semi-autonomous body
- Establish a PPP Secretariat to serve as the PPP Steering Committee’s technical unit, and house it within the Ministry of Finance
- Staffing for the PPP Secretariat will be achieved by offering compensation packages that can compete with the private sector, either by having the personnel classification of PPP Secretariat personnel conform to that of financial service technical specialists in a public enterprise, or by secondment from the Privatization Commission
- The PPP Secretariat reports to the PS-Treasury in his capacity as Chairman of the PPP Steering Committee
• The Investment Secretary provides a support role to the PPP Secretariat, assisting it in operations and working relationships within Treasury, and providing guidance on all matters pertaining to investment of public funds
• The PPP Secretariat maintains consultative and collaborative relationships with Debt Management Department, Public Procurement Oversight Authority, and Ministry of Planning & National Development
• Final decisions regarding PPP projects are made by the PPP Steering Committee, but when the nature or size of the project requires it, Cabinet will make the decisions
• If the decision is made to establish a Project Development Facility, that PDF will be a separate body from the PPP Secretariat making its own decisions

The proposed timeline for implementation is provided below:

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Next Steps:

✓ Submit the National PPP Policy to Cabinet in a Policy Paper, while simultaneously inserting the designated legislative initiatives in the current Finance Bill
✓ Publish the National PPP Policy in the Kenyan Gazette, while simultaneously passing PPP Regulations under the Public Procurement & Disposal Act (as a new Schedule to existing Regulations), the Privatization Act, the Government Contracts Act, the State Corporations Act, and the Government Financial Management Act
✓ Establish the National PPP Steering Committee and its PPP Secretariat, announcing it through publishing in the Kenya Gazette
✓ Engage consultants to assist sector ministries, public enterprises, and local government authorities to establish PPP Nodes, and to prepare PPP Policy & Operations Manuals for the PPP Secretariat and PPP Nodes
✓ Obtain PPP Secretariat personnel classification that can compete with the private sector, either by giving them a classification equal to that of financial services specialists in the public enterprises, or by hiring them in the Privatization Commission and seconding the personnel hired to the PPP Secretariat
✓ Immediately process pending applications for PPP projects, from sector ministries, public enterprises, local governments, and private sector sponsors (unsolicited proposals) when the PPP Secretariat is formed, staffed, and funded.

Draft Policy Statement on Public-Private Partnerships for Kenya

Background

It is official Government policy to encourage the use of Public-Private Partnership (PPP) in the provision of public infrastructure and services.

PPP is consistent with Kenya’s strategic and long-term goals that have been articulated in the following plans, policies, and regulations:

- Vision 2030 plan to rapidly transform Kenya into a middle-income country
- The Roads 2000 Programme, which calls for the construction of some 1,063 km of new roads and the maintenance of over 4,469 km of existing roads
- The Water Act 2002, which has called for the systemic improvement of water services and new investments through commercialization and private sector participation schemes
- The Energy Sector’s Sessional Paper No. 4 of 2004 calling for more cost-effective, affordable, and better quality energy services.
- The Local Authority Service Delivery Action Plan (LASDAP) and the Local Government Integrated Financial Management System (LGIFMS) which call for strengthening local government infrastructure development
- The Housing Sector’s Sessional Paper No. 3 of 2004 on improving housing development in Kenya
- The Information and Communications Technology Sector’s new ICT policy on the road map for Kenya’s ICT growth and expansion
- The National Environmental Action Plan of 2003
- The Private Sector Development Strategy (PSDS)
- Sessional Paper No. 2 of 2005 on the development of Micro and Small Enterprises for Wealth and Employment Creation
- The goals of the Government’s Results-Based Management System of public sector performance contracts
**Definition of Public-Private Partnership**

A “public-private partnership” is a commercial joint venture, between a public institution and a private party, in which project risks are allocated amongst the parties based on which party is best equipped to manage each category of such risks, and in terms of which the private party:

- Performs an institutional function on behalf of the state; and/or
- Is allowed the use of state property; and
- Assumes substantial financial, technical, and operational risks in connection with the performance of the institutional function and/or use of state property; and
- Receives a benefit for performing the institutional function or from utilizing the state property, either by way of:
  - Consideration to be paid by the institution, which derives from a revenue fund; or
  - Where the institution is a national government business enterprise or a regional or local government business enterprise, from the revenues of such institution; or
  - Charges or fees to be collected by the private party from users or customers of a service provided to them; or
- A combination of such consideration and such charges or fees.

**Scope of Public-Private Partnerships**

A PPP is an arrangement between the public and private sectors (consistent with a broad range of possible partnership structures) with clear agreement on shared objectives for the delivery of public infrastructure and/or public services by the private sector that would otherwise have been provided through traditional public sector procurement.

Characteristics often associated with PPP arrangements include:

- Shared responsibility for the provision of the infrastructure or services with a significant level of risk being taken by the private sector, for example, in infrastructure projects, linking design and construction with one or all of the finance, operate and maintain elements;
- Long-term commitment by the public sector to the provision of quality public services to consumers through contractual arrangements with private sector operators; and
- Better value for money and optimal allocation of risk, for example, by exploiting private sector competencies (managerial, technical, financial and innovation) over the project’s lifetime and by promoting the cross-transfer of skills between the public and private partners.

The creation of an environment supporting the development of PPPs extends beyond the application of contract law to the development of consensus and understanding of the main objectives of PPP including, in particular, the need for quality public services.

Collaborative management styles and working practices should foster successful partnership in PPP projects. Partnership skills at project level are a critical element of the PPP agenda.
The core strength of PPPs is the scope they allow for dynamic interaction and cooperation between the public and private sectors, highlighting the complementarity of the public service ethos with innovation in the provision of public capital infrastructure and services. PPPs are an important part of the ongoing agenda for the modernization of public services.

Genuine partnership has a crucial role to play in helping to achieve the shared goals underpinning the PPP program and also provides the opportunity for all parties - public and private sectors - to re-evaluate shared areas of interest and develop new and innovative ways of working together in PPPs.

**Statement of Principles**

PPPs should yield value for money for the Ministry of Finance, which includes:

- Allocating risks to the party best able to control and manage them; and
- Maximizing the benefits of private sector efficiency, expertise, flexibility and innovation.

The adoption of a PPP approach should be determined by factors, including:

- The likelihood of it providing value for money, particularly as compared to conventional public capital procurement;
- Economic, social, and environmental factors;
- Long-term affordability in the light of overall budgetary sustainability, forward commitments in relation to public expenditure and the potential for returns on private sector investment;
- Willingness of the private sector to participate in the project (i.e. financial viability considerations); and
- The balance between economic and social benefits and costs (including the opportunity costs of the Ministry of Finance contribution required).

Private finance in PPPs should be additional to public finance, complementing the Ministry of Finance’s resources in funding investment in public infrastructure and public services. Introduction and development of PPPs should take place within the overall process and structures of social partnership and should be managed in an open and transparent manner. PPPs should be consistent best industry and business practices.

**Goals and Benefits**

Identification of the goals of PPP and the prospective benefits from individual projects provide more certainty, in particular, for those (e.g. local communities) whom PPP projects are expected to serve. These goals and benefits include the following:

- Speedy, efficient and cost-effective delivery of projects;
- Value for money for the taxpayer, through optimal risk transfer and risk management;
- Efficiencies from integrating design and construction of public infrastructure with financing, operation and maintenance/upgrading;
• Creation of added value through synergies between public authorities and private sector companies, in particular, through the integration and cross-transfer of public and private sector skills, knowledge and expertise;
• Alleviation of capacity constraints and bottlenecks in the economy through higher productivity of labour and capital resources in the delivery of projects;
• Competition and greater construction capacity (including the participation of overseas firms – especially in joint ventures and partnering arrangements);
• Accountability for the provision and delivery of quality public services through a performance incentive management/regulatory regime;
• Innovation and diversity in the provision of public services; and
• Effective utilization of state assets to the benefit of all users of public services.

The PPP Process

PPP issues should be reviewed through the structures and systems currently in place for managing the PPP program. It is essential to ensure a standardized approach consistent with this Framework to the development of the PPP program overall, while recognizing the need for sectoral flexibility to accommodate diversity at project level.

PPP Identification and Project Selection
The first step in determining the technical profile, operations, service delivery targets, and future income and costs of the project is to perform a demand analysis. All PPP infrastructure projects should be “demand driven,” meaning that the interest on the part of Government to promote the project should be driven by a commensurate desire on the part of consumers to use the services. Demand analysis, therefore, will require that surveys be taken. For those PPP projects that require the collection of user fees directly from consumers, it will be important to confirm through such demand analysis studies that the revenues paid by consumers will be sufficient to make the project financially viable. If not, then subsidy payments from the Government or other forms of public sector support will need to be considered.

PPP Project Evaluation and Feasibility Analysis
After completing the demand analysis to confirm that future users of the services want to have those services and are willing and able to pay the level of tariff necessary to attract private investment and increase the quantity and quality of service delivery, the next step is to perform Options Analysis and the Feasibility Study.

PPP Options Analysis
Examining PPP options means exploring the various ways that the desired services can be most efficiently and effectively provided. This is a complex and time-consuming process and one that is often passed over because of the complexity and time consumption. Options analysis requires staying focused on the targeted service delivery and examining all possible options for delivering those services, regardless of what projects might have already been developed or planned to a certain degree by the potential project sponsor. In performing options analysis, many factors have to be taken into consideration regarding how the potential project could impact other related forms of service delivery.
**PPP Feasibility Analysis**

Once the PPP options analysis has been done, the line ministry’s PPP Node should conduct a PPP feasibility study. Once user demand, willingness to pay, and affordability, and elimination of other options to the proposed project have been demonstrated as described above, the PPP feasibility study should be a detailed description of the project. In order to prepare this section, there will be a need to conduct some preliminary engineering, capital expenditure analysis, including the any requirements for new land acquisition, as well as analysis of projected revenues and operating costs.

**PPP Risk Allocation & Structuring**

While the traditional analyses of technical feasibility, economic feasibility, and of environmental impact as sufficient for traditional public projects to proceed to the tendering phase – these are not sufficient to tender a PPP project. In order to be viable, PPPs must carefully allocate all relevant risks to specific parties and must also determine if the project is still financially and commercially viable for the project’s given risk-allocation structure. Detailed risk identification and allocation matrices are very useful models for completing these tasks. This additional level of feasibility analysis is needed not only to ensure that the project’s proposed structure allows an acceptable level of return and coverage for the risks that private investors and lenders will be taking – it also clarifies the risks that the public sector is being asked to bear. Therefore, this additional level of PPP feasibility analysis should ensure that the Government can afford to make the contributions required by the project’s proposed risk structure.

Where the implementation of recommendations requires a high-level policy decision, they should be submitted through the relevant agency to the responsible Minister and, where appropriate, the Minister for Finance. The experience and expertise available across both in the public and private sectors and from the social partners should be utilized to advance the PPP process.

**Consultation with Stakeholders**

Stakeholders include employees and their trade unions, the public, the people who will use the assets and services provided, local communities, Secretariat groups and sectoral interest groups. In selecting, developing and implementing PPP projects, the economic, social and environmental concerns of those directly affected at local level should be taken into account along with the statutory rights and legitimate economic interests of stakeholders.

The PPP framework requires that Kenya’s stakeholders be consulted throughout the PPP project development process to ensure the PPPs address the key needs of all members of the Kenyan public. These requirements will be described and explained in detail in the framework’s implementing procedures, and will feature consultation requirements during the project selection analysis, structuring, and performance monitoring stages. Key groups featured in these stakeholder consultation requirements include:

- End users and consumers of public services in Kenya, especially low-income users and the poor
Labour organizations (described in more detail in the section below)
Kenyan businesses, local contractors, and small-scale Jua Kali entrepreneurs
Kenya Government ministries, public agencies and Local Governments
Community-Based Organizations, Environmental groups, and other Non-Governmental Organizations
Kenyan private investors, commercial banks & financial institutions
International private investors, banks, and financial institutions
Other relevant stakeholders for each individual PPP project

These procedures will establish the required minimum standards for consulting and communicating with these key PPP stakeholders to ensure transparency and sustainable public support for PPPs in Kenya.

Consultation with Labour

As one of the most important stakeholders affected by PPPs in Kenya, specific standards will be required to ensure fair and transparent analysis and communications of labour-related PPP issues. While many PPPs in Kenya will entail new, green-field projects, that will create new jobs in infrastructure construction and long-term operation and maintenance requirements, some PPPs will require the transfer of existing infrastructure networks, currently being operated by public agencies and their staff, to management by a private contractor. To ensure that any labour impacts from PPPs are managed transparently and fairly, this framework will require specific consultation and communications standards. These will include required standards for:

- Planning and completing a PPP labour impact analysis for each PPP project, similar to the requirements of the current Privatization Act of 2005
- Managing communications and consultations with labour groups on plans for managing the impacts of PPPs on labour

Existing structures and agreements should be used to ensure extensive consultation and open communication in respect of PPP projects. Public service employees should be informed at the earliest possible stage of proposals for the introduction of PPPs and of significant developments throughout the process. They should also have the opportunity to contribute positively to the development of projects, building on progress in the development of workplace partnerships under the PPF. The partnership approach should be maintained throughout the project’s lifetime. All parties to a PPP arrangement should have regard to appropriate industry norms in terms of pay and conditions and of prevailing industry-wide agreements including health and safety regulations.

Communications Strategy

The success of the PPP program requires widespread public support. A PPP communications and awareness strategy, led by the PPP Secretariat in the Ministry of Finance, will be directed at key stakeholders, officials of public service procuring agencies, employees in sectors where PPPs will be developed and the general public.
Information on progress in assessing and implementing the various PPP projects should be made available to all those interested in Kenya’s PPP program, using project trackers posted and updated regularly on the national PPP website.

## Implementation

### Structures

PPP projects under the PPP Framework are implemented by the relevant public authority, e.g., sector ministries, statutory bodies, public enterprises, and local government bodies. Implementation of PPP projects is coordinated by the national PPP Secretariat in the Ministry of Finance, which will distribute PPP Operations Guidelines Manuals for use by public authorities in developing PPP projects.

### Affordability

Two kinds of affordability are tested in the assessment of PPP projects: (1) affordability to consumers; and (2) affordability to Government. Affordability of a PPP to Kenya’s consumers will be assessed by a conducting consumer demand, affordability, and willingness-to-pay survey, which must be conducted by a public authority proposing a new PPP project. Affordability to Government will be assessed by determining whether the proposed PPP project is included in the budget, either as a specific project or as funds allocated for a category of project within which that proposed project appropriately fits. If funding for costs to be borne by Government is not already provided in the budget, then the proposed project will be introduced for consideration by the Ministry of National Planning, which will decide whether the project should be included in its sector plan. Once it is confirmed that the proposed project does fit within the sector plan, the Ministry of Finance will determine what level of public resources will be committed to the project. This will ensure that Government can afford its share of the costs of the proposed project.

### Risk Allocation

Much of the design, construction, service delivery, and financing risks are bundled together and transferred to the private sector, while Government focuses on managing the risks that it is best equipped to manage, i.e. political risks. In practice, the dividing line between political risks and commercial risks is not always so clear. Some kinds of risk may be too large or too “undiversifiable” or “uninsurable” for any one party to have to manage on its own, so those risks are shared between the parties. In cases where price and quantity are heavily influenced by government policies and regulations, such as taxes or planned improvements to competing transport facilities, demand risks are shared between both the public and private sectors. Other risks may or not be shared depending on the public policy environment, e.g., exchange rate risk.

### Value for Money

The concept of value for money is that the PPP projects to be selected will be those that will provide the highest quantity and quality of service provision for a given amount of public expenditure. In evaluating bids for PPP projects, the focus is different from traditional procurement, which is to select the bidder that can delivery the specified material or commodity at the lowest price. In PPP, the winning bidder should be the one that provides the highest quantity and quality of service delivery, given a particular level of public expenditure, not
necessarily the bidder with the lowest initial cost to Government, as would be the case in conventional procurement.

**Procurement**
The projects should be procured in an open and transparent fashion consistent with national and relevant international-standards procurement rules and with the need to ensure effective competition.

The tendering and procurement process for PPP is different from standard public procurement, and usually more complex. PPP procurement requires the Government to do only the basic design and engineering estimates, because the tender is for delivery of the outputs rather than delivery of the facilities. Private sector providers complete the design and engineering, indicating their planned approach in their proposals, and demonstrate how this approach will comply with the service delivery requirements. This infuses private sector innovation into the project design. In PPP contracting, there are often the terms: (a) Outputs; and (b) Service Delivery Standards.

Overall when implementing the tendering and procurement of PPPs, the policy calls for the following principles:

- **Fairness** – the procurement process must be fair to all parties, i.e. the rights of all parties must be protected at each stage of procurement, and then in contract management;
- **Transparency** – the procurement process must keep as much information as possible in the public domain, and as much information as practicable must be shared equally with all bidders, especially the methodology for selection;
- **Competition** – in order to avoid possible conflict of interest, and in order to ensure that the most qualified bidder is selected, the procurement process must provide competition sufficient to ensure that vested interests and/or corruption do not influence selection; and
- **Accountability** – decisions made by the parties must be open to review by stakeholders, and decision makers must be held accountable for their decisions.

**Contract Terms**
In PPP projects, a long-term partnership is created for the procurement of an asset and/or the delivery of a service to a specified quality level. The design of the PPP contract is crucial. As the pilot PPP program is rolled-out, a number of broad principles should guide the design of PPP contracts.

These include the following:

- Risks should be clearly identified and distributed appropriately between the parties to the contract;
- Innovation by the private sector in providing infrastructure and public services should be encouraged, to realize value for money over the life-cycle of the project; and
- The provisions governing the transfer of public capital infrastructure from a public authority to a private sector consortium (i.e. by means of lease or license) and its
reversion at expiry of the concession period should be clear and transparent at the outset and over the lifetime of the PPP project;

- The payment mechanism should provide a clear procedure for establishing the charge on public expenditure over time;
- Reduction in costs over the life span of the contract should be incentivized in order to bolster price-competitive quality public service provision;
- Adequate flexibility, where feasible, to encompass, with the agreement of the contract parties, new and innovative ways of upgrading the quality of services (in response to advances in technology and innovations in potential delivery mechanisms);
- Full disclosure of all relevant information relating to the conduct of the PPP over time should be encouraged in order to minimize the scope for costly information gaps arising between the public and private sector partners; and
- Regard for prevailing national and/or industry wide agreements on pay and conditions, including health and safety regulations.

**Output Specifications**

The output specifications should take account of the following general principles:

- The level of service quality and design should be related to the objective for the service and user requirements;
- Social and environmental sustainability and gender equality/disability considerations; and
- Any need for improvements in service standards over the lifetime of the contract required to comply with regulatory obligations, for example, relating to environmental, and public health standards.

**User Charges**

These charges, where they apply in PPP projects, can make a valuable contribution to enhanced service quality and efficient use of infrastructure or services consistent with the need to maintain environmental sustainability and to conserve scarce environmental resources (taking account of the “polluter pays principle”).

New financially viable freestanding PPP infrastructure projects will, where possible, be expected to generate a revenue stream from user charges sufficient to remunerate and redeem the private sector finance. Any Exchequer contribution should ensure that the level of charges is consistent with efficient use of the infrastructure. Mechanisms should be developed to reduce the negative impact of user charges on low-income groups.

**Post-Transaction PPP Contract Compliance & Performance Monitoring**

PPPs will only deliver the planned benefits in Kenya if each of the parties continues to perform, as required by the contract, for the entire term of the project. In the past it has been a challenge for the Government, which has not been institutionally set-up to monitor the actual performance of public infrastructure and services, to fulfil this important role of monitoring the performance of private PPP contractors. PPP contractors should only be paid if it has been properly verified that they have delivered all of the required services specified in the PPP contract. Therefore, a key requirement of this new PPP Policy is that the public sector sponsor of the project establishes clear procedures to monitor the contractor’s performance and to ensure
compliance through the designation of either a contract compliance office or the naming an appropriate regulatory body.

**Central Coordination of the PPP Process**

Central direction should continue to be provided to the PPP process by the institutional structures established by Government to manage the PPP program. This will ensure a consistent and co-ordinated approach and maintain a positive business climate for the private sector.

The PPP Secretariat in the Ministry of Finance, working together with the other sectoral PPP Secretariats and the social partners, should continue to give a high priority to:

- Delivery of the PPP program;
- Developing a standardized approach in terms of tendering procedures, model contracts and documentation, in step with progress in the pilot program;
- Developing PPP policy; and
- Resolving outstanding obstacles to the wider use of PPPs (including legal, taxation, financial and other issues).

This will ensure that:

- PPP becomes a standard element of Government procurement methods; and
- A stream of PPP projects is developed and a sustainable and dynamic PPP market is created in Kenya in the long term.
Appendix 2. Gazette Notice on Establishment of a National Public-Private Partnerships Steering Committee

MINISTRY OF FINANCE

ESTABLISHMENT OF A NATIONAL PUBLIC-PRIVATE PARTNERSHIPS STEERING COMMITTEE
(Draft)

IT IS notified for information of the general public that the Minister for Finance has established a Steering Committee under the Ministry of Finance known as the National Public Private Partnerships Steering Committee.

1. **Membership of the Steering Committee:**

The Steering Committee shall comprise the following persons –

Permanent Secretary, Ministry of Finance – (Chairman):

Members:

- Permanent Secretary, Ministry of Planning and National Development;
- Permanent Secretary/Secretary, Public Service Reform and Development Secretariat;
- Permanent Secretary, Ministry of State for Public Service;
- Permanent Secretary, Ministry of Local Government;
- Permanent Secretary, Ministry of Trade and Industry;
- Solicitor-General;
- Investment Secretary; and
- Chairman, State Corporations Advisory Committee.

2. **Functions of the Steering Committee:**

The functions of the Steering Committee shall be to –

a. Advise on national target setting and consensus building in the implementation of the Public Private Partnerships programme;
b. Strengthen the process of open and competitive identification of projects amenable to Public Private Partnership arrangements;

c. Co-ordinate the development of laws, amendments to existing laws, rules, regulations and guidelines for Public Private Partnerships;

d. Deliberate on and make recommendations on conflicts arising from policy and implementation of Public Private Partnerships;

e. Draw lessons learnt and best practices to improve Public Private Partnerships;

f. Advise on integrated information, education and communication strategy for Public Private Partnerships;

g. Provide overall monitoring and evaluation of Public Private Partnerships from the initiation stage to post completion stage;

h. Advise the Government on enabling institutional framework to facilitate achievement of results for Kenyans;

i. Explore opportunities for benchmarking to ensure continuous performance improvement of Public Private Partnerships;

3. **Powers of the Steering Committee:**

The Steering Committee shall have all the powers necessary for the proper discharge of its functions, and without prejudice to the generality of the foregoing, shall have power to:-

a. Regulate its meetings and its own procedures;

b. Co-opt members as it shall deem appropriate;

c. Extensively engage stakeholders.

4. **Technical Unit**

a. The Steering Committee shall be supported by a Technical Unit within the Treasury Department of the Ministry of Finance which shall comprise such experts whether foreign or local and staff as the Steering Committee shall determine.

b. The Technical Unit shall also serve as the Secretariat to the Steering Committee.

5. **Responsibilities of the Technical Unit**

The Technical Unit shall be responsible for inter alia the following: -
a. Reviewing/analyzing all proposals for Public Private Partnership projects whether unsolicited or emanating from line ministries and other government agencies based on affordability and value for money criteria.

b. Coordinating and developing the new Public Private Partnership framework.

c. Assisting line ministries and other government agencies in capacity building for Public Private Partnerships.

d. Developing a manual or manuals for standards and procedures for Public Private Partnerships for approval by the Steering Committee.

e. Developing regulations and guidelines for Public Private Partnerships for approval by the Steering Committee.

f. Developing model sector based Public Private Partnership agreements for approval by the Steering Committee.

g. Developing a communications strategy for the Public Private Partnership policy for approval by the Steering Committee.

h. Monitoring Public Private Partnership projects from start-up to post completion.

i. Assisting line ministries in identification of viable Public Private Partnership projects.

j. Identifying legal constraints on Public Private Partnerships and drafting proposed amendments to the law to overcome them.

6. **Joint Secretaries:**

The Joint Secretaries of the Steering Committee shall be ________

7. **Reporting:**

The Committee shall present its programme of work on ________ 2007 and deliver its first report to the Minister by ________ 2007.

AMOS KIMUNYA
Minister for Finance
Appendix 3. Recommended Legal Framework for PPP

Amendment to the Finance Bill:

1. Paragraph (d) of subsection 18(5) of the Public Procurement and Disposal Act 2005 is amended by inserting after “prescribed” the following phrase “but a public private partnership arrangement that is the subject of a contract signed in accordance with Section 7A of the Government Contracts Act shall not be subject to a capacity building levy”.

Schedule XXX to the Finance Bill

Consequential Amendments

Public Procurement and Disposal Act 2005

1. Section 3 of the Public Procurement and Disposal Act 2005 is amended by inserting after the definition of “public funds” the following definition:
   “public private partnership arrangement” means:
   a) an arrangement between a State Entity, either itself or in conjunction with any other person, including another State Entity, with a person (referred to in this context as a “partner”) for the performance of functions of the State Entity specified in the arrangement in relation to:
      i. the design and construction of an asset, together with the operation of services relating to it and the provision of finance, if required, for such design, construction and operation, or
      ii. the construction of an asset, together with the operation of services relating to it and the provision of finance, if required, for such construction and operation, or
      iii. the design and construction of an asset, together with the provision of finance for such design and construction, or
      iv. the provision of services relating to an asset for not less than 5 years and the provision of finance, if required, for such services,
   b) includes concessioning referred to in Section 92(2) where for the purposes of this definition “construction” includes building, refurbishment, maintenance, repair, improvement, demolition, extension and replacement, and “operation” includes management and maintenance;
2. Section 3 is amended by inserting before “the regulations” “State Entity means an authority listed in the Fifth Schedule which Schedule may from time to time be amended by an order made by the Minister”.

**Fifth Schedule to the Public Procurement and Asset Disposal Act 2005 to be inserted after the Fourth Schedule**

State Entity

i. Government or any department of the Government,
ii. The Permanent Secretary to the Treasury Incorporated,
iii. A state corporation within the meaning of the State Corporations Act.

**Government Contracts Act**

After Section 7 of the Government Contracts Act Section 7A is inserted:

7A (1) “A contract for a public private partnership arrangement, as defined in Section 3 of the Public Procurement and Disposal Act 2005, shall not bind the Government or any State Entity as defined in Section 3 of that Act in respect of any matter, unless the contract is signed or countersigned by the Permanent Secretary to the Treasury, or a person or persons specially authorised by him in writing in that behalf.

(2) The Minister responsible for matters relating to finance may make regulations for better carrying out the provisions of this Act and without prejudice to the foregoing, make regulations (a) prescribing the process, procedures and regulation generally of public private partnership arrangements including the approvals to be obtained, the actions to be taken and requirements to be satisfied before the Permanent Secretary to the Treasury may sign or countersign a contract for a public private partnership arrangement, (b) issuing directions and guidance to State entities in relation to financing public infrastructure projects including (a) the type of project, (b) the size of the project, (c) the stage of development of the project, and (d) any other relevant factors on which the Treasury’s advice shall be sought by a State entity as soon as is practicable in connection with a public infrastructure project.

(3) The Permanent Secretary to the Treasury may issue directions and guidelines regarding public private partnership arrangements.”

**The Permanent Secretary to the Treasury (Incorporation) Act CAP 101**

After Section 7 of The Permanent Secretary to the Treasury (Incorporation) Act Section 8 is to be inserted:

“8. The Minister with responsibility for finance may make regulations for the better carrying out the provisions of this Act and the functions of the corporation.”

**END OF SCHEDULE TO FINANCE BILL**

Note: The following subsidiary legislation is proposed as initiatives that can be taken outside of the current Finance Bill. There is no need to use the Finance Bill as a means of achieving quick
implementation, because the subsidiary legislation is all Regulations, for which authority is already conveyed to the respective Minister for enactment.
Subsidiary Legislation

Regulations to be made under Section 7A of the Government Contracts Act:

In exercise of the powers conferred by section 7A(2) of the Government Contracts Act, the Minister for Finance makes the following Regulations:

**Government Contracts Regulations 2007**

1. These Regulations may be cited as the Government Contracts (Public Private Partnership Arrangement) Regulations 2007 and shall come into force on —

2. In these Regulations “public infrastructure project” means a concept, plan, asset or activity that is or may be the subject of a public private partnership arrangement.

3. The Permanent Secretary to the Treasury shall not sign a contract for a public private partnership arrangement unless it is satisfied that the State Entity which is mainly connected with the public infrastructure project, has at all times and promptly:
   (i) brought to the attention of the Treasury all matters relating to the public infrastructure project as soon as practicable after the public infrastructure project has come to its notice;
   (ii) provided to the Treasury all records, facts, information, documentation and correspondence relating to the public infrastructure project and persons interested in the project whether these have been requested by the Treasury or not,
   (iii) complied with all directions, instructions, notices, circulars and requests from the Treasury.

4. A State Entity that is interested, or is requested by any person, to enter a public private partnership arrangement in connection with a public infrastructure project, shall bring to the attention of the Treasury all matters relating to a public private partnership arrangement as soon as practicable after the public infrastructure project has come to its notice.

5. Prior to initiating a process of identifying a partner for a public private partnership arrangement, the Permanent Secretary to the Treasury or person authorised to act on its behalf shall submit the tender documents relating to a proposed public private partnership arrangement to the Public Procurement Oversight Authority for written approval of a specially permitted procurement procedure in accordance with Section 92 of the Public Procurement and Disposal Act 2005.

**Regulations to be made under the Public Procurement and Disposal Act 2005**

In exercise of the powers conferred by section 140 of the Public Procurement and Disposal Act, 2005 the Minister for Finance makes the following Regulations

**Public Procurement and Disposal Regulations 2007**
These regulations may be cited as the Public Procurement and Disposal Regulations 2007 and shall come into operation on the --.

1. The Public Procurement and Disposal Regulations 2006 are amended as follows:

(a) in Regulation 2 the definition of public private partnership PPP is repealed;
(b) Regulation 3(a) is repealed;
(c) After Regulation 64(2)(b), 64(2)(c) is inserted “in considering the proposal and tender documents for approval the Authority shall satisfy itself that the proposal and tender documents accord with the objectives of the Public Procurement and Disposal Act but shall not consider the merits of the proposed public private partnership arrangement”.
(c) Regulation 64(4) is repealed;

Regulations to be made under the State Corporations Act

In exercise of the powers conferred by sections 7 and 30 of the State Corporations Act [Cap 446] the [President] makes the following Regulations.

State Corporations Regulations 2007

A State Corporation that is interested, or is requested by any person, to enter a public private partnership arrangement in connection with a project, shall as soon as practicable after the project has come to its notice, bring all matters relating to the project to the attention of the State Corporation’s Advisory Committee and the Minister for the time being assigned responsibility for the State Corporation

Regulations to be made under the Privatisation Act 2005

In exercise of the powers conferred by section 51 of the Privatisation Act 2005, the Minister makes the following Regulations.

Privatisation Regulations 2007

1. Where a method of privatisation under Section 25(b) is proposed which may expose the Government or a public entity to actual or potential liabilities, whether hidden, contingent, or otherwise, at the time of privatisation or subsequently, the Commission shall as soon as the potential exposure comes to its notice, bring the matter to the attention of the Minister so that the Government is fully aware of the exposure to liabilities.

State Entities (Public Private Partnership Arrangements) Bill

Statement of Objects and Reasons

While existing laws do not prohibit State Entities from entering public private partnership arrangements, as defined in Section 3 of the Public Procurement and Disposal Act 2005, there is a need to give certainty that State Entities have capacity to enter all the various forms of public private partnership arrangements. For example, some public private partnership arrangements
may involve the delegation of statutory powers to a partner (within the meaning of that term in Section 3 of the Public Procurement and Disposal Act 2005), or the forming of a company with a State Entity and a partner as members for the purposes of the public private partnership arrangement. While the need for certainty may arise in only a small number of instances, this Bill eliminates resort to piecemeal legislation, on a case by case basis, which could serve to delay or disrupt public private partnership arrangements.

The Bill contains sections relating to the public finances that require further discussion with the Ministry of Finance. They are inserted to indicate the range and of issues that are required to be addressed when embarking on the pursuit of public private partnership arrangements.

(Note that if this proposed legislation is introduced some time after the changes proposed to take place in the immediate future then amendments may be made to consolidate matters relating to public private partnership arrangements into one Act.)

Long Title

An Act To Make Further Provision In Relation To The Functions And Powers Of Certain State Entities, In Particular To Enable Them To Enter Into Public Private Partnership Arrangements, And To Provide For Related Matters

Short Title and Commencement

1(1) This Act may be cited as the State Entities (Public Private Partnership Arrangements) Act, 20-- (2) This Act shall come into operation.

Interpretation

2(1) In this Act, except where the context otherwise requires:
“appropriate Minister” means a Minister on whom functions stand conferred or who has general responsibility in respect of or in connection with the public private partnership arrangement concerned;
“asset” includes an existing asset or an asset to be provided under a public private partnership arrangement;
“company” means a company within the meaning of the Companies Act;
“construction” includes building, refurbishment, maintenance, repair, improvement, demolition, extension and replacement;
“direct agreement” has the meaning given to it by section 3(1)(c);
“functions” includes powers and duties, and a reference to the performance of functions includes, with respect to powers and duties, a reference to the exercise of the powers and the carrying out of the duties;
“local authority” means a [municipal council, city council or town council] for the purposes of the Local Government Act;
“Minister” means the Minister responsible for Finance;
“operation” includes management and maintenance;
“partner” has the meaning given to it by section 3(1);
“State entity” means an entity listed in Schedule 1 to this Act;
(2) In this Act (a) a reference to a section or Schedule is a reference to a section of, or a Schedule to, this Act unless it is indicated that reference to some other enactment is intended, and (b) a reference to a subsection or paragraph is a reference to the subsection or paragraph of the provision in which the reference occurs, unless it is indicated that reference to some other provision is intended.

(3) In this Act, a reference to any other enactment shall be construed as a reference to that enactment as amended, extended or adapted by or under any subsequent enactment.

Authority to enter Public Private Partnership Arrangement

3. (1) Without prejudice to the functions of a State entity under any other enactment, a State entity may, either itself or in conjunction with any other person (including another State entity) and with prior consent of the Minister and the appropriate Minister, in an agreement signed or countersigned by the Permanent Secretary to the Treasury (a) enter into a public private partnership arrangement as defined in the Public Procurement and Disposal Act 2005 with a person (referred to in this Act as a partner) for the performance of functions of the State Entity specified in the arrangement, (b) subject to subsection (4), arrange or provide for a payment to a partner, (c) enter, where appropriate, into an agreement (in this Act referred to as a “direct agreement”) with a person who has arranged or provided funding for the partner for the carrying out of the public private partnership arrangement, (d) transfer an interest, or part of an interest, of the State Entity in an asset or part of an asset, to the partner, to a nominee of the partner by transfer, assignment, conveyance, grant of lease or licence or otherwise, (e) take a transfer of an interest of the partner or a nominee of the partner, in an asset or part of an asset, by transfer, assignment, conveyance, grant or surrender of lease or licence or otherwise.

(2) Functions conferred on a State Entity by this section are in addition to and not in substitution for any other functions of the State entity.

(3) Subject to subsections (4) and (5) a State entity may, whether or not for consideration, transfer, convey or assign its interest in any real or personal property (including leaseholds) owned or held by such State entity to a company formed under subsection (6) for the purpose of enabling such a company to carry out its financing functions in connection with public investment projects.

(4) A State entity shall not convey, assign or transfer any such property to any such company unless the prior consent of the Minister and the appropriate Minister has been obtained.

(5) A State entity may with consent of the Minister attach such terms and conditions as it considers appropriate to any transfer, conveyance or assignment pursuant to subsection (2).

(6) A State Entity may, with the prior consent of the Minister for Finance and the appropriate Minister to which it reports and (a) either itself or in conjunction with any other person (including another State Entity) cause a company to be formed and registered, or (b) become a shareholder in an existing company, for the purposes of a public private partnership arrangement or of entering into such an arrangement.

(7) A public private partnership arrangement may include terms and conditions in relation to the performance by the partner concerned of the partner’s obligations under the arrangement as agreed by the State Entity.

(8) (a) Where a payment is arranged or provided for pursuant to section 3(1)(b) the Minister for Finance may, at any time until entry into the public private partnership arrangement by the State Entity, give directions to the appropriate Minister in relation to the aggregate value of exchequer moneys committed to such arrangements, as he considers necessary.
(b) The appropriate Minister shall have regard to any directions given by the Minister for Finance under this section.

4. (1) For so long as it continues in force, a public private partnership arrangement shall operate to confer on the partner concerned the functions of the State Entity specified in the arrangement, subject to any terms and conditions so specified.
   (2) A function conferred on a partner by a public private partnership arrangement
       (a) may be performed by the partner in the partner’s own name, subject to the general
           superintendence and control of the State Entity concerned, and
       (b) shall, notwithstanding such arrangement, continue to be vested in the State Entity concerned concurrently with the partner and may be performed by either or both of them.
   (3) The conferral of a function of a Minister on a partner by a public private partnership arrangement shall not affect the Minister’s responsibility to Parliament or as a member of the Government for the performance of the function.
   (4) In this section “functions”, in relation to a State Entity, includes functions of any other State Entity to be performed by it pursuant to an agreement or arrangement duly made by it with that other authority.

5. Where an agreement or arrangement was entered into on a date before the commencement of this Act, and that agreement or arrangement is or would have been a public private partnership arrangement or direct agreement if this Act had been in operation on such date, then the agreement or arrangement, as the case may be, shall have effect and be taken always to have had effect as if this Act was in operation when the arrangement or agreement was entered into.

6. (1) In relation to a company to be formed and registered, or a company that is formed and registered under section 3(2), the Minister for Finance may, either before, or at the time of entering into a public private partnership arrangement and, without prejudice to the requirements of the Companies Acts, give written directions to either or both (a) the State Entity concerned, and (b) where the company has been so formed and registered, the company, concerning the management, accountability, accounting and financial affairs of such a company and, in relation to such a company that is formed and registered, its participation in the relevant public private partnership arrangement.
   (2) In relation to a company that is formed and registered under section 3(2), the Minister for Finance may, without prejudice to the requirements of the Companies Acts, at any time after the company enters into a public private partnership arrangement, give directions to either or both (a) the State Entity concerned, and (b) the company, concerning matters of policy in relation to the public private partnership arrangement concerned or such arrangements generally.
   (3) A State Entity and a company shall comply with any directions given under this section.

7. (1) Where the Minister for Finance, following consultation with any appropriate Minister, is of the opinion that (a) a public entity not standing specified as a State entity in Schedule 1 ought, having regard to the purposes of this Act, to stand so specified, or (b) having regard to the amalgamation, dissolution or change of name of a State Entity, the State Entity ought to cease to be specified in the Schedule or to be so specified under a different name or description, he may, by order, amend the Schedule by adding the name of a person or body to it or by deleting the name of a person or body specified in it or by so adding and deleting, as the case may be.
(2) In this section “public entity” means (a) a person or body which at any time stood specified in the Schedule, (b) a board, authority or other body (other than a company) established by or under statute, (c) a company in which all the shares are held (i) by the Permanent Secretary to the Treasury or by or on behalf of a Minister, or (ii) by directors appointed by a Minister, or (d) a company in which all the shares are held by a board, authority or body referred to in paragraph (b) or by a company referred to in paragraph (c).

8. (1) The Minister may advance moneys from the Consolidated Fund or the growing produce thereof to a company formed under section 3(6) on such terms and conditions as he may determine. (2) Moneys advanced under subsection (1) may include moneys for the purpose of making an equity investment in such a company. (3) The aggregate of advances from the Consolidated Fund under subsection (1) that are outstanding at any time shall not exceed --

9. (1) The Minister may guarantee the due repayment by the State entity or any companies formed under section 3(6) of the principal of any moneys (including moneys in a currency other than the currency of the State) raised by the State entity or such companies, or the payment of interest on such moneys or both the repayment of the principal and the payment of the interest, and any such guarantee may include a guarantee of the payment by the State entity or such companies of commission and incidental expenses arising in connection with such moneys. The combined net aggregate of the principal of all moneys guaranteed by the Minister and outstanding (including the equivalent in the currency of the State of moneys raised in a currency other than the currency of the State) shall not exceed -- in total.

(2) The Minister shall, as soon as may be after the expiration of every financial year, lay before Parliament a statement setting out with respect to each guarantee under this section given during that year or given at any time before, and in force at, the commencement of that year (a) particulars of the guarantee, including the remaining life of the guarantee, (b) in case any payment has been made by the Minister under the guarantee before the end of that year, the amount of the payment and the amount (if any) repaid to the Minister on foot of the payment, and (c) the amount of moneys covered by the guarantee which was outstanding at the end of that year.

(3) Moneys paid by the Minister under a guarantee under this section shall be repaid to the Minister, with interest on it at such rate or rates as he or she appoints, by the State entity or any company referred to in subsection (1), as the case may be, within 2 years from the date of the advance of the moneys out of the Consolidated Fund.

(4) Where the whole or any part of moneys required by subsection (3) to be repaid to the Minister has not been paid in accordance with that subsection, the amount so remaining outstanding shall be repaid to the Consolidated Fund out of moneys provided by Parliament.

(5) Notwithstanding the provision under subsection (4) to repay the amount to the Consolidated Fund, the State entity or any company referred to in subsection (1), as the case may be, shall remain liable to the Minister in respect of that amount, and that amount, with interest on it at such rate or rates as the Minister appoints, shall be repaid to him or her by the State entity or any company referred to in subsection (1), as the case may be, at such times and in such instalments as the Minister appoints and, in default of such repayment and without prejudice to any other method of recovery, shall be recoverable as a simple contract debt in any court of competent jurisdiction.
(6) Moneys paid by the State entity or any company referred to in subsection (1), as the case may be, under subsection (3) or (5) shall be paid into or disposed of for the benefit of the Exchequer in such manner as the Minister thinks fit.

(7) In relation to guarantees given by the Minister under this section in respect of moneys in a currency other than the currency of the State (a) each of the references to principal, each of the references to interest and the reference to commission and incidental expenses in subsection (1) shall be taken as referring to the equivalent in the currency of the State of the actual principal, the actual interest and the actual commission and incidental expenses, respectively, such equivalent being calculated according to the cost in the currency of the State of the actual principal, the actual interest or the actual commission and incidental expenses, as may be appropriate, at the time the calculation is made, (b) the reference to moneys in subsection (2) shall be taken as referring to the equivalent in the currency of the State of the actual moneys, such equivalent being calculated according to the rate of exchange for that currency and the currency of the State at the time the calculation is made, and (c) each of the references to moneys in subsections (3) to (5) shall be taken as referring to the cost in the currency of the State of the actual moneys.

(8) Any payment by the Minister under this section shall be a charge on the Consolidated Fund or the growing produce thereof.
Appendix 4. Key Elements and Legal Issues in PPP Concession Agreements

1. Type of PPP agreement with Full Project Description:
   Examples: Design-Build-Operate-Maintain, Build Own Operate Transfer, Build Own Transfer, Pre-Development Agreement, Concession Agreement - Investor Financed/Tax Incentives, Other.

2. By what procurement process has PPP being sought?
   Competitive procurement
   Unsolicited proposal and negotiations
   Competitive procurement following unsolicited proposal
   Sole-source negotiations
   Other

3. Who are the contracting parties to the primary PPP agreement?
   What is the legal status of the private sector party (e.g. company, partnership, equity joint venture, joint venture agreement)?
   If a joint venture, is there joint and several liability?
   Are the obligations of the private sector party guaranteed by a third party (other than guarantor)?
   Does the Government contracting party have authority to enter agreement?

4. Is there a regulator and what is the regulatory regime?

5. Describe conditions applicable to the financing plan: types, sources, covenants of capital financing

6. Describe any public subsidy of revenues (e.g. shadow tolls, assumption of operation and maintenance costs).

7. What other major ancillary/supporting agreements are there?
   Are other agreements contemplated to be executed in the future (e.g., such agreements might include a design-build contract, a full or partial completion guarantee and/or financing agreements)?

8. What are the roles of the public and private entities for pre-financing tasks, such as project definition, preparation of environment protection documents, licensing applications, traffic and revenue studies, surveys, geotechnical investigations, easements and right-of-way acquisition and preliminary engineering, communications, public stakeholder involvement and consultation?

9. How is the private party to be compensated for pre-financing costs (e.g., current reimbursement, reimbursement from financing proceeds, development fee, return-on-equity contribution)?

10. How is the private party to be compensated for its equity and debt contributions with respect
11. How is the private party to be compensated for operation and maintenance services?
12. Is the Government or public sector party required to exercise its power of compulsory purchase to facilitate the project?
13. Does the Government or public sector party establish the design, construction, operation and maintenance standards with which the private party must comply?
14. Describe any payment due from the private party to the Government or public sector party for the grant of rights and the payment terms.
15. What is the mechanism by which user fees, if any, are established and adjusted? Describe any limitations on user fees, exempt parties etc.
16. Describe any revenue recovery between the public and private entities.
17. Sponsor’s rate of return/minimum revenue earning
18. What is the duration of the agreement and what are the options to extend this timeframe (if applicable) or the process that will govern renewal or new competition?
19. What are the major performance milestones that will be required of the parties, including the Government or public sector party and the private party?
20. If applicable, describe the private party’s rights and obligations to make capital investment, provide future project capacity improvements, extras, or expansions.
21. Who is responsible for the operation and maintenance of the completed facility?
22. What about services to be provided what operating and service standards, how measured and monitored and what penalties for non-performance in differing circumstances depending on causes?
23. Definitions of force majeure events and what about termination in event of long-standing force majeure events that cannot be ameliorated?
24. Describe any provisions relative to competitive transportation facilities (include a description of what constitute competitive facilities, exceptions, and measure of damages).
25. Is the private party required to reimburse the Government or public sector party for services? For design review? Licensing? Operation and maintenance? Monitoring?
26. Will Government assist in obtaining licenses/permits resolving regulatory issues prior to commencement of the project?
27. If applicable, what is the reasonable/maximum return or rate of return on investment authorised for the developer/operator to earn, the formula by which such rate of return will be calculated and the distribution of project revenues?
28. What are events of default on the part of concessionaire (developer/operator) defaults, and what are the major remedies available to the public owner? Examples may include: Breach of the agreement or any ancillary agreements, including failure to meet milestones; Bankruptcy; Revocation of parent guarantee; Misrepresentation or fraud; and Failure to pay claims. Following a default event, Government or public sector party may terminate the agreement or a portion of it and may be entitled to damages.
29. What other rights does the Government or public sector party have to terminate the agreement (e.g., failure to meet milestones, termination for convenience)? If the agreement is terminated for convenience, what compensation is paid to the private party?
30. What events constitute Government or public sector party defaults, and what are the remedies available to the developer/operator? Examples might include: developer has the right to stop work if Government or public sector
party fails to make a payment when due. Developer may terminate after say 180 days of non-payment. Developer is entitled to rights under law in the event of a material breach of the agreement by Government or public sector party. Damages recoverable due to Government or public sector party default may not exceed the amount payable under a termination for convenience by Government or public sector party.

31. What are the lender's rights and remedies with respect to private party defaults?
Does the agreement provide for lender's rights and remedies e.g. step in rights?

32. Are there any credit enhancement measures/tax incentives/grants available?

33. What indemnification obligations do each of the parties have?
Example: Developer must indemnify Government or public sector party against third-party claims due to the Developer's acts and omissions.

34. What are the obligations of the developer/operator to maintain records, to allow inspection and audit and to provide regular reports to the public owner?
Developer must retain records for 5 years after expiration or termination of the agreement. Developer must allow inspection and audit. What obligation does the Government or public sector party have to maintain the confidentiality of specified information?

35. What are the conditions under which the private party may assign its rights under the PPP agreement and/or its rights to the facility? What about change of control of the private party?
Example: Assignment requires Government or public sector party's prior approval. Does the PPP agreement contemplate a subsequent assignment of the private party's rights to another entity, such as a non-profit corporation to be formed for the purpose of financing the project? Can it make an assignment for security?
Can it transfer its rights and obligations to an affiliate or unrelated third party?
Example: Yes to an affiliate, with Government or public sector party's prior approval in its sole discretion and on a facility-by-facility basis. What are the conditions, if any, to obtain the consent of the Government party?

36. What dispute resolution mechanisms?

37. Provision for renegotiation to permit flexibility to adjust without undermining agreement

38. Describe any provisions limiting liability or waiving consequential damages.
Example: The comprehensive development agreement includes a limitation on liability of X plus any caps set forth in ancillary agreements. The cap does not include insurance proceeds, indemnities or losses due to fraud/gross negligence/intentional misconduct/illegal activities. The cap does not apply to loan agreements that may reached.
Example: The comprehensive development agreement includes a mutual waiver of consequential damages. The waiver does not apply to insurance proceeds, indemnities, losses due to fraud/gross negligence/intentional misconduct/illegal activities, liquidated damages or loan agreements.

39. Compensation on termination in varying circumstances
Compensation for improvements not recovered during term of agreement

40. What about taxation matters? Income/corporation tax, stamp duty or transfer taxes on property/lease/concession, VAT/indirect taxes on construction/plant and machinery, import duties and other taxes on imported goods for the project, taxation of international staff (if any)?
Appendix 5. Current PPP Project Opportunities

Over the course of this consultancy, the IP3 team has met with numerous officials in Government agencies at the national and sub-national levels. During these meetings, discussions regarding how the PPP Framework should be developed were conducted. Information was also obtained regarding PPP projects already underway or in the process of being developed. The information provided below is not intended to be an exhaustive list of every potential PPP project in Kenya, but rather to provide some information on the more important projects, for the purpose of estimating how much financial and human resources should be mobilized to enable processing of the current “deal flow” of PPP projects.

Transport Sector

Nairobi Urban Toll Road

The goal of this project is to improve traffic efficiency along the NC through removal of the main remaining bottlenecks by enabling private investment within a toll road concession along the most congested urban sections of the Uhuru Highway. The concession consists of road sections along the NC near Nairobi and a bypass alternative to a tolled urban stretch. Sections are being rehabilitated upgraded under the NCTIP. Works on both sections comprise the rehabilitation of the existing lane single carriageways while Section will also be upgraded to a lane dual carriageway. Feasibility Studies were conducted by an internationally recruited Consultant and confirmed the project's commercial viability. Given the assumed traffic levels calculations show that the estimated project costs can be recovered at acceptable toll rates. Total project cost is estimated at KSh19 billion.

Additional costs to be covered by the concessionaire over the life of the year concession will include future road related improvements periodic and routine maintenance construction costs of toll facilities as well as their operations and maintenance. The Concessionaire will also be required to develop roadside facilities e g parking areas utilities infrastructure bus and truck stops etc at key locations This includes social amenities like off road booths for sale of local produce and products bicycle paths pedestrian sidewalks and other means to enhance safety and benefit road users. An IDA PRG is being proposed in support of the Concession, in the amount of US$40 million. A consortium of A-Way, Strabag, and IPS was selected from 3 short-listed firms, but amidst allegations of impropriety IPS has emerged as the potential winner after its consortium members dropped out of the competition.
The project is part of the Northern Corridor Transport Improvement Project (NCTIP) and the Eastern African Trade and Transport Facilitation Project (EATTFP), which are expected to cover the Northern Corridor spanning from Mombasa through Nairobi to Uganda, Rwanda, Burundi and the Democratic Republic of Congo. The main objective of the project is to improve traffic efficiency along the Northern Corridor through removal of the main remaining bottlenecks by enabling private investment within a toll-road concession along the most congested urban section of the Uhuru Highway.

**Lamu Port Development Project**

This multi-modal transport project proposes to develop port facilities at Lamu, and establish ground transport links from the port to Nairobi and up to Southern Sudan. The total estimated project cost is US$15-20 billion, if all components are included such as an oil refinery, container handling facility, rail links, and various processing, assembling, and distributing facilities.

Lamu stands out as Kenya's best option for a second deep-sea port. Lamu has higher availability of both land and water surface area that can be deployed for port operations compared to Mombasa and other ports already established along the Eastern African seaboard. The higher land surface area available is attributable to the incidence of sparser human populations and human developments around the Manda Bay area and the Lamu mainland. Lamu is also gifted with deep waters that would make it ideal for serving large ships, including Panamax ships and crude oil supertankers.

The Al-Bader International Development Company, a Kuwaiti consortium has presented an unsolicited proposal for which the acronym is ROOLA, standing for Railway, Roads, Oil Pipelines, Oil Refinery, Optical Fiber, and Lamu Port. The proposed BOOT arrangements are for Lamu Port, Railway, Road Network, Fiber Optic Cable, Oil Pipeline, Oil Refinery, and Airports at Lamu and Junction Town. The proposed non-BOOT arrangements are for Resort Cities, Free Trade Zones, Cement Factories, and Steel Works. The BOOT projects are proposed to be concessions, while the non-BOOT projects are to be co-owned by the GOK and the Al-Bader consortium. Total private investment $15-20 billion.

The PPP design involves the GOK providing land, rights-of-way, and exclusivity for the provision of transport services over the proposed transport network, in exchange for a substantial investment and the sourcing of debt financing by a Kuwaiti consortium. Although the Ministry of Transportation has held negotiations with the consortium, which proposed the project via an unsolicited proposal, and appears to have executed a Memorandum of Understanding with the group, our analysis of the proposal is that: (a) it requires too much exclusivity; and (b) the due diligence performed by GOK on the group is far from sufficient for a project of this magnitude. There might be, however, opportunities to work with the group for development of PPP projects in the targeted region, with more limited exclusivity.

**Free Port Facility and New Container Handling Facility at Mombasa**

The Mombasa Port is congested and in need of expansion. There are containers stacked up all over the port, indicating such congestion, though this is partly caused by limited capacity in the railway and the poor condition of road alternatives to carry freight to Nairobi. There is an area
adjacent to the existing port that would be ideal for a new container handling facility. Discussions are underway to create such a facility, and to create a free port by obtaining free trade zone status. A PPP study has been performed for the Kenya Ports Authority.

While Kenya Ports Authority ponders the free port opportunity, a steady stream of prospective partners continues to approach them with PPP proposals to develop the new facility. One example is Portek International Limited, a Singapore-based ports operator, which in November 2006 submitted an unsolicited proposal for “Interim Container Terminal Capacity Expansion in Mombasa” arrangement, using the PPP methodology. The proposal includes a commitment from Portek’s Chairman Larry Lam to invest up to US$34 million immediately. KPA indicates its support of PPP arrangements, and cites existing PPP arrangements such as the LPG handling facility, but little progress has been made on this opportunity to date for this potential US$15 million PPP transaction.

A private consortium operating under the name of The Taj Group has submitted multiple unsolicited proposals to build, operate, and transfer a new container facility, as well as to reclaim land from the nearby Makupa Creek and build cargo handling, vehicle handling berth, storage, workshops, and other services such as environmental cleanup for the Mombasa Port. This proposal builds on their existing concession (granted in 1989; updated in 2002 and 2005) for a vehicle handling facility at Mbaraki and offers a new multi-story parking facility, a tunnel from the port, and a workshop for conversion of local cars to access the export market. They have also proposed a new assembly and manufacture facility for Makupa, along with a rail terminal, power substation, and container terminal. A third site would include another container facility, but would need a bridge and causeway plus railway terminal.

The Permanent Secretary of Ministry of Transportation organized a Committee to study the proposal, and subsequently issued a letter informing the Group that the Committee had authorized them to proceed and build the bridge required for access to the new facility. A waste oil processing facility to keep the water in Mombasa port clean per international standards, was included. A few days later, the letter was withdrawn. Rumors are labor resistance to PPP in the ports brought pressure on the Minister to quash the deal. This potential US$25 million transaction is presently being held up by lack of an Environmental Impact Assessment. Taj management has been advised that the owner must apply for EIA, and that because Taj is not yet the owner the EIA cannot be processed. The Taj Group also sponsored a Plantation PPP with potential US$300 million private investment, in which the GOK was the landowner, but according to Taj management, the deal was “hijacked” by another private investor group (with political connections) and now the project is stalled by disputes.

A new port about 400 km north of Mombasa has been proposed as a PPP arrangement, and JICA has commissioned some studies, which have created an interest on the part of JBIC but progress seems to have been stalled on this potential PPP arrangement. Other KPA arrangements have progressed, such as the LPG storage facility, and the leasing of land to Gulfstream, along with plans for dredging and land reclamation including lease arrangements with private firms for palm oil storage and marketing.

Private Sector Management and Service Delivery for Kenyan Airports
The Kenya Airports Authority (KAA) has been active in PPP arrangements for aircraft servicing, food service, aircraft repairs and maintenance, facilities management, parking, and many other areas. They have unsolicited proposals from private firms proposing to build, operate, and transfer a new hotel for Nairobi Airport, and a continuing flow of similar interest from private firms to provide several of the various areas of services made available at the airport. KAA management has indicated to the IP3 consultancy that they would like to proceed with many of these proposed PPP projects, but are unable to do so until the PPP Framework is developed and related procurement procedures are clarified.

Management of KAA itself appears to be a possibility, especially in view of Government’s current support for performance-based contracting, and the Management Contract precedent established by the Kenya Power & Light Company. If such private sector management could be contracted, and based on the Auditor General’s report on KAA for the past few years there certainly appears to be a need for such a change, then there should be multiple attractive PPP project opportunities in Kenya’s airports. A number of PPP initiatives are being considered, including a hotel and convention center for Nairobi, and a Dubai Flower Center.

The Nairobi and Mombasa airports are not the only ones in which a steady flow of PPP opportunities exists. Passenger and freight traffic between Kisumu and Eldoret is increasing steadily and is creating multiple PPP opportunities in airport services. Kisumu relies heavily on fresh produce from Eldoret and Kitale. As Kenya’s third largest international airport, Eldoret is a key facility for imported cargo, and now offers new warehouses and cold storage facilities that bring its capacity to 200 tons, up from 80 tons four years ago. The airport covers its own costs due to increased cargo volume. Regular users of the airport include Egypt Cargo and Singapore Cargo.

Kenya Airports Authority has actively promoted private provision of airport services, and has given incentives such as free parking for airplanes and a 25% reduction in landing fees to increase traffic volume in selected airports. With a Master Plan that encourages private sector service provision, along with a regional customs integration plan that would greatly expedite traffic flow, opportunities for PPP transactions in Kenya’s airports will be consistently available in good supply. A PPP study has been prepared for KAA by Stewart Scott, mapping out a number of potential PPP opportunities.

**Private Sector Provision of Air Transport Services**

The privatization of Kenya Airways has improved the quality and reliability of air transport services in Kenya, partly by making Kenya Airways more responsive to consumer demand, and partly by bringing increased competition to the market. A recent entrant into the Kenyan air transport market is Fly 540, which focuses on the local business market and is the only passenger airline providing service to Eldoret, which provides a vital link between the North Rift and the lakeside city of Kisumu.

The privatization of Kenya Airways and emergence of multiple private carriers such as Jetlink Express, Delta Connection, and Fly 540 reflect a consistent policy of deregulation of the industry and opening of the industry to private sector service provision. Airports services and air
transport services will make a continuing flow of opportunities available for PPP arrangements in the years to come.

**Telecommunications**

**Cellular, Wireless & Internet Services**

The telecommunications sector continues to offer significant opportunities for private sector service provision. The partial privatization of the Telkom Kenya reflects Government commitment to PSP and PPP. Wireless operators such as Safaricom, which is doing an IPO, and a the new entry of Econet into the cellular market, making a total of four licensed providers, reflect a robust market in which there is healthy competition. Internet service providers, such as SwiftGlobal and others, are experiencing the benefits of high demand and relatively low price sensitivity among customers. Telkom and others such as Pipote Wireless, offer wireless local loop solutions that deliver not only dial tone but a host of value added services such as wireless broadband internet based on either radio or microwave links.

**Fiber Optic Cable PPP Project**

One of the most significant PPP opportunities in the telecommunications sector is the tender for the construction of an undersea fiber optic cable, for which bidders are likely to include Alcatel, Tyco Telecommunications, Fujitsa Corporation, NEC Corporation, and Huawei Technologies of China. The East Africa Marine System (TEAMS) is a joint venture between the Governments of Kenya and the United Arab Emirates. The US$110 million project will be operated by a Special Purpose Vehicle, owned 40% by Telkom Kenya Limited, 20% by the UAE phone company Etislat, and the remaining 40 percent is reserved for private investors. Standard Chartered Bank is the lead arranger for sale of those shares in the SPV. The GOK has appropriated KSh1 billion for its participation in the venture.

**Energy Sector**

The Kenyan energy sector is going through restructuring and privatization. The unbundling of power generation, transmission, and distribution is creating multiple opportunities for private sector service provision. While PPP arrangements for transmission and distribution are relatively new, there has been considerable PPP activity in power generation, especially for renewable energy technologies. A steam turbine facility was tendered, for which the winner was Mitsubishi, but the project has been delayed due to cost escalations and resulting request for comfort letter by the project’s financing consortium. The petroleum refinery at Mombasa is in need of rehabilitation, as presently experienced by consumers throughout Kenya trying to by LPG containers for cooking, but often unable to do so because of the shortage caused by limited output of this refinery. This PPP arrangement is 50/50 owned by the GOK and Chevron/BP private investment, which wants to sell its shares but the Ministry of Energy does not want the sale because there is no assurance that buyers would rehabilitate the facility. Because of the petroleum price subsidies, the economics of the situation are such that it would be more profitable to replace the facility with a container handling facility, rather than rehabilitate the refinery.
Renewable Energy Power Generation

A 30-megawatt PPP wind-power project was launched in 2005 by KenGen with US$49 million in financing from the Danish International Development Agency and the African Development Bank. Another new PPP renewable energy generation plant was established in Olkaria, to tap geothermal power with three 15 megawatt generators. The National Power Development Plan envisions an additional 423 megawatts of generation capacity by the end of 2008. KenGen is to install 278 megawatts, and Independent Power Producers (IPPs) are to install 115 megawatts. Electricity demand is expected to grow 14% by the end of 2008, so there will be plenty of opportunities to utilize PPP arrangements to meet this escalating consumer demand. The P.S. Energy advised the IP3 team that one constraint to IPP projects is the high cost of outputs, caused by the relatively high cost of thermal energy and the expectation of capital recovery within a relatively short period of 5 years.

New Opportunities for PPP Power Generation

New KenGen Plants
- 60 MW hydro plant on Sondu River (July 2007)
- 10 MW Additional hydro capacity at Tana Power Station (July 2007)
- 60 MW combined cycle gas turbine plant at Kipevu (July 2007)
- 35 MW additional geothermal plant at Olkaria (April 2008)
- 20 MW hydro additional capacity at Kiambere (July 2008)
- 20 MW additional hydro capacity at Kindaruma (July 2008)

New KenGen/EcoGen Plants
- 30 MW wind power generation plant (July 2007)

New Independent Power Producer Plants
- 80 MW medium speed diesel plant in Nairobi (September 2007)
- 35 MW geothermal plant at Olkaria (April 2008)

Nine of the plants with a combined capacity of 273 MW are at various stages of implementation, while the Government has given KenGen authority to procure a 70 MW gas turbine to be installed by August 2006 and KPLC has been authorized to invite competitive tenders from IPPs for an 80 MW medium speed diesel plant to be completed by September 2007. A project to interconnect the Kenya and Tanzania power grids is at an advanced stage of preparation with possible Dutch funding. The project has been prioritized in the East African Power Master Plan Study and it involves construction of a 330 kV transmission line between Arusha and Nairobi. Electrical power trade between Kenya and Tanzania is expected by 2009. The price and demand stabilization features of this regional grid arrangement will make private investment in the energy sector more attractive, and will facilitate PPP arrangements.

Kenya-Uganda Oil Pipeline

The Governments of Kenya and Uganda plan to extend the existing Mombasa – Eldoret oil pipeline to Kampala. The governments of Kenya and Uganda signed a Memorandum of Understanding (MOU) in 1995, which established a Joint Coordinating Commission (JCC) to coordinate the extension project. The project comprises construction of a pipeline as an extension to the existing pipeline to take white products into Uganda to serve markets in
Uganda and beyond. A Feasibility study, funded by the European Investment Bank (EIB) was undertaken by an international consultant M/S Penspen who submitted a report in May 1999. A complementary study was undertaken in 2001 to update the earlier study. The two studies found the project technically feasible and also financially and economically viable. The project entails installation of an 8-inch diameter, 320 km long pipeline from Eldoret to Kampala with an annual capacity of approximately 1,200,000m³.

The project is being promoted as a public-private partnership (PPP) with the private investment partner playing a leading role. The two governments shall own 24.5% each of the equity based capital of the project and the private sector shall be the majority shareholder owning at least 51% of the equity. The Libyan firm Tamoil has expressed interest in this project, along with the LPG facility at Mombasa.

**Water, Sanitation & Irrigation**

In the Ministry of Water Resources Sessional Paper No. 1 of 1999 entitled “National Policy on Water Resources Management and Development” paragraph 4.1.3 states “The role of Government in the water sector will be redefined with emphasis on regulatory and enabling functions as opposed to direct service provision.” In paragraph 4.1.4 the Policy affirms that “the Government will support private sector participation and community management of services backed by measures to strengthen local institutions in implementing and sustaining water and sanitation programs.”

**WSP and MWI Initiatives for PPP Service Provision**

The World Bank’s Water & Sanitation Program (WSP) has made some progress in steering reforms in the sector. It has established several autonomous water service institutions, along with Water Services Trust Fund, a semi-autonomous body designed to ensure that revenues generated by the sector are then re-invested for development of the sector. The Ministry of Water & Irrigation (MWI) has also made impressive progress in making the sector more attractive to private investment. A pilot project has achieved the corporatization of 7 municipal water utilities, and the Water Act 2003 separated water activities from general municipal activities, leading the way to future PPP arrangements. The Water Regulators have given Water Service Boards authority to contract with private sector service providers.

Most of the progress in PSP/PPP for the sector has been on the part of Small and Medium Private Providers (SMPPs) and the projects have been mostly under US$ 2 million in size, generally financed from commercial sources on 5-year terms. There is talk about trying a pooled water utility bond flotation along the lines of what was done successfully in Tamil Nadu, India. Many of the water PPP deals involve a private entrepreneur getting an extraction permit from the Water Resource Management Authority, processing what is usually surface water, and then supplying it to communities in which piped water is unavailable or limited in availability.

The ability and willingness of consumers to pay the high prices of trucked water suggests opportunity for the private provision of small to medium scale water treatment and distribution PPP projects. The constraints are lack of capacity in water utilities and local government bodies.
to contract with private sector providers, and a history of subsidizing water tariffs. Some progress has been made via a PPIAF study for privatization of Nairobi Water, and a pilot project has been mobilized for the coastal region. Water Board bonds are being considered and related capital markets studies have been engaged.

For irrigation PPP projects, Kenya Private Sector Alliance has proposed a number of projects in which new dams would be constructed, and water accumulated behind the dams would be used for irrigation. The scheme includes installing turbines in the dams, generating electricity to drive the pumps to be used for irrigation, and selling excess capacity into the national grid. The IP3 consultants were advised these projects would be able to proceed once the PPP Framework is in place.

**Privatization of Nairobi Water & Sewerage**

Progress has been made in privatizing the provision of water and sewerage services in Nairobi. The water utility has been corporatized, and a special trust has been established, both of which will enable the revenues obtained from such services to be invested back into the sector. There are PPP contracts being considered for private sector maintenance and repair of distribution systems, and for collection of accounts receivable. Given Kenya’s well-developed private sector, PPP opportunities in these areas are likely to grow in the near-to-medium term.

**Private Sector Provision of Water & Sewerage Services in Kisumu**

Since 2002, progress has been made in assisting the GOK and the Municipality of Kisumu to make available opportunities for private providers of water and sanitation services. PPP arrangements have been made for small-scale water treatment and distribution, repairs and maintenance of distribution systems, and formation of community networks to invest in capital improvements. Additional projects will continue to become available for prospective PPP partners.

**Private Sector Provision of Water & Sewerage Services in Mombasa**

There has been considerable technical assistance, and private sector interest, in the provision of water and sanitation services for Mombasa and the coastal region. The economic and demographic profiles, and the geographic profile, suggest potential for a Dolphin Coast type transaction in this area. There is, however, a capacity constraint in the water utility and local government bodies, so bringing a private operator in to add processing and distribution capacity will require some capacity building assistance.

**Micro-Finance for Small Water Supply Projects**

As discussed in the section above on Nairobi water and sanitation services, most participation by the private sector in the water and sanitation sector is small or medium scale. In order to facilitate these kinds of PPP activities, progress has been made over the past 3 years in creating pilot projects to show lenders that water projects can be reliable borrowers. The goal is for domestic lenders to become more aware of this market niche and start offering tailored project
financing products to private companies attempting to penetrate or further develop this market for their services.

**Local Authority Sanitation PPP Projects**

There are a multitude of PPP opportunities at the local authority level in Kenya. There has been some progress with smaller PPP projects, such as Nairobi City Council’s Geographical Information System, Beautification (tree planting), street lighting (Adopt-A-Light), and environmental projects dealing with solid waste disposal. However, PPP initiatives continue to be frustrated by lack of capacity within the city councils to understand how to structure and implement PPP projects, conflicts between legislation and city bylaws regarding private sector service provision, and alleged corruption.

**PPP for Solid Waste Disposal / Methane Gas / Energy Generation**

One of the most attractive areas for PPP potential at the local authority level is solid waste collection and disposal. Nairobi has a population of slightly over 2 million people and is growing at 6.5 per cent per year. Poor Solid Waste Management (SWM) services in the city has remained a matter of concern to Nairobi residents as the city grows in size. It is estimated that the residents of Nairobi generate about 1500 tons of garbage per day. However, Nairobi City Council (NCC) can only handle 200 tons of garbage per day. This sorry state of waste management in Nairobi is manifested by huge garbage dumps in the city and the unsanitary conditions of the landfill site at Dandora, which is the only legal dumpsite in the City. However, a recent study by Japanese International Co-operation Agency, JICA (August, 1998) recommends a contingency plan to close down the present site and establish a sanitized one about 30 kms from the city enter at Ruai.

One of the more important PPP initiatives undertaken by Nairobi City Council was the **Fingal Landfill Project with Veolia Waste Solutions & Technologies**, which invested a considerable amount of time and expense in performing design and feasibility analysis for a major project in which solid waste was to be collected in Nairobi city and buried in a landfill from which methane gas would be derived for the generation of electricity. The engineering studies indicated that will Veolia technology a medium-size landfill would generate about 6 megawatts of electricity, enough to provide lighting to 10,000 homes. Citing legal constraints to its ability to contract with the private sector for long-term service delivery, the NCC pulled out of contract negotiations for this concession. There were allegations of monopoly control of solid waste collection by companies owned by City Council members but the legal issue was not the Local Government Act, which specifically authorized City Councils to contract with the private sector for provision of services for which the City Council was responsible. The legal issue was that the internal bylaws of the City Council were not consistent with the Local Government Act.

**Need for Internal By-Laws Changes in City Councils**

In order for PPP activity to be undertaken, there is need to amend the City Council By-Laws in order to allow producers of waste, or users of waste management services, to pay for the services rendered. Above all, By-Laws should be explicit on the ownership of waste and assign responsibility. The By-Laws should allow the council to manage competition and/ or restrict
market place to facilitate for critical mass of clients for service providers. Ultimately, it is necessary that such legal framework have inbuilt flexibility. The revised By-Laws would include clauses for technical business evaluation such as zone population, waste characteristics, collection methods, transfer facilities and disposal technology. In these evaluations, promotion of waste minimization, re-use, reduction and recycling shall be given priority consideration. Among the questions that shall be assessed and their implications clearly understood are: What are the legal boundary conditions for a technical solid waste management approach adopted? How effective is the districting/zoning of the municipality? What is the social mix of the zone? How does subsidy to low-income families become factored into pricing?

The revised City By-Laws would allow the Councils to regulate and supervise the private sector service provider. In doing so, the council would have powers to terminate the private sector services if its activities posed threats to humans and the environment. The new provisions would give private sector service providers an opportunity to invest and allow recovery of investment with profit in a reasonable service contract/franchise period. Questions relating to who sets the tariff, how it is assessed, collected and allocated to payment of the private sector operator would be clarified.

The initiatives described above need to be taken by the City Councils, to harmonize their internal By-Laws with the national PPP Legal Framework developed by the IP3 consultancy. Once that is done, there should be multiple attractive PPP opportunities in solid waste management for municipalities. For now, there are PPP arrangements already underway, in ambulance services, garbage collection, billboards, street lighting, rehabilitation, and tree planting. The Commissioner of Police has authority to make arrangements with private sector providers of security services. An MOU has been signed with Jacarozzi for recycling, but implementation of this PPP arrangement appears to have stalled, perhaps over legal ambiguities that also continue to impair the Adopt-A-Light PPP arrangement.

**Housing Sector**

Private sector participation and PPP are to play a significant role in provision of housing as indicated in the National Housing Policy Draft. It is estimated that up to 80% of the middle income housing will be produced through private investors either individually or jointly between local and foreign investors. It is in this spirit that the Overseas Private Investment Corporation (OPIC) has signed two Memoranda of Understanding with the GOK through the Ministry of Roads, Public Works, and Housing. The memoranda are expressions of mutual interest to support viable joint investment proposals by U.S and Kenyan companies to develop housing via the PPP methodology.

The GOK has initiated a number of measures with UN-HABITAT to develop housing using public, private, and community partnerships. Government has prepared the Kenya Slum Upgrading Strategy as well as a complementary Financing Strategy. The strategy envisages the improvement of the housing situation for approximately 5.4 million people living and working in unplanned settlements in urban centers throughout the country. The total cost of these potential PPP projects is estimated at more than twelve billion U.S. dollars over a period of 13 years.
The GOK has established the Kenya Slum Upgrading, Low Cost Housing and Infrastructure Fund. The Fund will pool resources from the Government and other development partners, the private sector, and beneficiary communities in financing the long-term housing strategy. In the last two financial years, the GOK has allocated about US$7 million annually towards implementation of this program. It intends to double that amount in the coming financial year. Work on the construction of 600 housing units is underway at the Kibera decanting site, using the PPP methodology, and work is underway for PPP projects carrying out water and sanitation interventions at Soweto village in Nairobi, as well as in Mombasa and Kisumu. A similar project will be implemented in Mavoko.

The Ministry of Roads, Public Works & Housing has a continuing series of initiatives for development of housing along the lines of the related UN-HABITAT initiatives. Private firms and local authorities do joint venture projects for development of low-income housing.

The Kenya Slum Upgrading Strategy spells out measures that require to be undertaken to prevent the development of new slums even as the GOK upgrades existing ones. Such preventive measures include strengthening the management and planning capacity of Local Authorities, supply of sufficient quantities of housing for low income households in line with the rate of urbanization, provision of urban housing infrastructure, and improved security of tenure. Other measures to check the spread of slums include urban planning in squatter settlements, urban re-development initiatives and urban land banking to cater for the future development of low-income housing. The envisaged measures are outlined in the Draft Sessional Paper on National Land Policy that Government intends to table during the current Session of Parliament.

**Health & Education**

**A. Health**

**AIDS Vaccine Distribution**

The Ministry of Health is conducting pilot programs in which AIDS vaccines are given to private firms for distribution to patients throughout the country. The program contracts with private firms that will distribute HIV test kits, Anti-Retroviral (ARV) inoculations, Sexually Transmitted Diseases (STD) drugs, condoms, blood safety commodities, and other supplies.

An example of a private sector partner in the program is Phillips Pharmaceuticals. Their warehouses in Nairobi house stock large quantities of Anti-Retroviral (ARV) drugs, along with other drugs that they distribute for major European and American pharmaceutical companies. Although the company makes no profit on the distribution of ARVs, it has contributed to the implementation of the “Accelerating Access Initiative”, an agreement signed in May 2000 by UNAIDS, WHO, the UN Population Fund and five multinational pharmaceutical companies to lower the cost of triple therapy treatment in developing countries from approximately $800 per month to between $40 and $60.

Phillips Pharmaceuticals charges a minimal handling fee of 5 per cent on the ARVs. Some private hospitals also agreed to reduce their mark-up to only 5 per cent in order to make ARVs
more accessible to Kenyan patients. This decision has since been taken up by others in the HIV drug supply chain such as Mission for Essential Drugs and Supplies (MEDS), a faith-based private distribution network that provides ARVs to mission hospitals in remote areas throughout Kenya. International donor HIV programs as well as government HIV initiatives depend on this private distribution network in place.

This ARV distribution system made up of a partnership between private, public and mission sectors in Kenya, patients in more than 100 HIV treatment centers in both urban and rural areas across the country now have access to HIV treatment and care. When Phillips began its not-for-profit ARV project, only 300 patients benefited from the drugs due to lack of financial resources, but now Access Initiative ARV prices, low handling fees, the efficient private distribution network in place, and financial support from international donors including the President’s Emergency Plan for Aids Relief of the U.S. government (PEPFAR) are enabling up to 20,000 HIV positive patients to benefit from treatment.

Today, MSD (whose ARVs are distributed by Phillips Pharmaceuticals Ltd.) through its partnership with The Kenya HIV/AIDS Private Sector Business Council and the Global Fund, Phillips, a distributor of Merck Sharp & Dohme (MSD)’s HIV drugs, continues to play a key role in initiating and organizing HIV management and care training programs and workshops on the latest developments. For these initiatives it has developed a training curriculum that has since been incorporated into the training materials of other entities.

**PPP Arrangements for Hospitals and Clinics**

Kenya lags behind many African countries in the development of a public-private partnership program for hospitals and clinics. There has been some outsourcing to the private sector in major hospitals such as the Kenyatta National Hospital and the Moi Teaching and Referral Hospital, where radiotherapy, CAT, MRI, and other treatments requiring use of expensive equipment are outsourced to specialized private sector service providers. There are also national PPP programs for prevention and treatment of tuberculosis, including an ongoing program by the International Medical Corps (IMC) and other NGOs targeting high-risk areas such as the Kiberia slums.

In the absence of a clear PPP framework for the medical sector, the private sector has established many treatment facilities on its own, rather than providing such services in partnership with Government owned health care facilities. This has resulted in a good supply of high-quality facilities, owned and operated by private physicians, for which access to care is quite good for those who can afford to pay, while access to good-quality medical care for those who cannot afford to pay continues to deteriorate.

**B. Education**

Government’s Education Sector Report 2006 paragraph 4.1 entitled “Proposed Strategies for Resource Mobilization” states that “there will (also) be a need for increased participation by the private sector in the provision and expansion of education, particularly at the secondary, TIVET, and university levels.” It goes on to say “Encouraging investment from the private sector will be crucial for sustained sector expansion and will require a new policy framework
within which to promote and regulate private investment, private school registration, as well as assurance and supervision.” This policy framework is to focus on “removing the constraints of private participation in education, for example, in the areas of school financing and land acquisition, by giving incentives designed to make private education more attractive to investors.” Among the initiatives to be undertaken are “Consideration of the Build Operate and Transfer (BOT) strategy where the private sector constructs facilities, operates and later on transfers to the public sector for ownership; Outsourcing of public owned facilities for private sector operators; and Enhancing tax exemptions and waivers, among other incentives for entrepreneurs and organizations willing to invest in the education sector.”

**Information and Communication Technology (ICT) PPP Program**

The Kenya ICT Trust Fund mobilizes and provides on Information and Communication Technology resources to facilitate Education and Training through Integration and Innovation. It facilitates Public Private Partnerships to provide ICT resources to Kenyan public schools, and community resource and learning centers. The specific objectives of the ICT PPP Program are:

1. To source and mobilize resources either in cash or in kind for the purchase of equipment necessary for improving the delivery of information and communications technology services within the Republic of Kenya;
2. To found, manage and facilitate comprehensive study and research in information and communications technology;
3. To establish and manage an information sharing system in collaboration with other organizations involved in the field of information and communications technology
4. To promote the widest possible universal access across the Republic of Kenya to equipment (Hardware and software) essential to the administration of information and communication technology studies;
5. To provide technical (including equipments), scientific and financial assistance to educational institutions in the Republic of Kenya for the promotion of information and communication technology studies;
6. To assist with the promotion of computer literacy among the Kenyan population in general
7. To recruit members, whether individuals or bodies corporate and thereby create a network of forging partnerships among stakeholders in information and communications technology;
8. To provide training to individuals by way of conferences, seminars, workshops and such related modes to achieve the sustainability of the Trust; and
9. To do all such acts as may be necessary or incidental to the achievement of the aim of the Trust.

The Trust has distributed 3,000 Microsoft licenses for donated education software, and has distributed 362 computers to 27 schools and community learning centers. It has conducted capacity building for over 800 teachers, and provided Internet connectivity to all recipients of assistance.

In preparing this material on financial security packages for the energy sector, we selected an oil/gas pipeline as the targeted sub-sector PPP transaction because the most important and immediate potential PPP transaction in Kenya in the energy sector, at the present time, is the Kenya-to-Uganda Oil Pipeline. We had previously considered using Independent Power Producer projects as the targeted transactions, but since then the pipeline transaction has moved forward significantly, and presents some substantial contingent liability risks for Treasury. There is, therefore, an immediate need for Treasury to have this case study and financial security package information for an oil pipeline PPP transaction.

Our approach to the material in this section is:

- Present a case study of an oil pipeline transaction in which we participated as advisors, and which has many similarities to the Kenya-Uganda Oil Pipeline case;
- Describe the financial security arrangements made for the Chad-Cameroon Oil Pipeline (the case study) and explain how such arrangements related to the Kenya-Uganda Oil Pipeline; and
- Present an international best practice example of a gas/oil pipeline policy governing the use of financial security arrangements in PPP contracting.

I. Case Study - Chad-Cameroon Oil Pipeline

Project Description

The project involved: (a) the development of Chad's Doba oil fields, including drilling of about 300 wells and construction of associated facilities and infrastructure; and (b) (i) the construction of a pipeline, 760 mm (30 inch) in diameter and 1,070 km in length, from the Doba oil fields to Cameroon's Atlantic coast at Kribi (buried to about 1 m of depth), three related pumping stations, and ancillary facilities and infrastructure improvements, and (ii) the installation of an off-shore floating storage and offloading vessel and related facilities, and an 11 km submarine pipeline from the Atlantic coastline to the vessel.

Component (a) constituted the "Field System" and (b) the "Export System." Private Sponsors financed the Field System entirely from their corporate resources. Two joint-venture companies, TOTCO, in Chad, and COTCO, in Cameroon, were established between the Private Sponsors and the two Governments to own and operate, respectively, the Chad and Cameroon portions of the Export System. External financing, including from the Bank and IFC, was provided for the purpose of partially funding the cost of the Export System, estimated at US$ 2,202.5 million (including financing costs).
The financial plan for the Export System, based on a debt-to-equity ratio of 64:36, was structured to provide political risk mitigation for the purpose of maximizing financing from commercial banks and project bonds. This was achieved through government equity participation in the pipeline companies and related Bank financing, and limited recourse project debt financing from IFC, US EXIM and COFACE, as well as Bank involvement. The IFC A loan, representing about 7 percent of the total debt, mobilized US$ 300 million in commercial bank lending under the B loan umbrella and plays, together with Bank financing, a key role in mobilizing up to US$ 400 million in project bonds. US EXIM and COFACE provided US$ 600 million of further debt to complete the debt-financing requirement.

The total estimated cost of the project is US$ 3.72 billion, of which about US$ 2.20 billion is for the Export System. This included the initial required funding of the Debt Service Reserve Accounts (DSRA), which were financed through the downstream investments estimated to be US$ 177 million. Physical and price contingencies ranging from about 5 percent to 10 percent, depending on the item, were included in the project cost.

The project cost was based on 5-year development plans for the upstream and downstream components of the project, which were prepared by Exxon-affiliated technical staff. Costs were reviewed by Stone & Webster, an independent engineering firm contracted on behalf of IFC and the Senior Lenders, and were found to be satisfactory. The average cost of the pipeline amounted to about US$ 850 per metric ton, and the average unit cost for its installation was estimated at about US$ 238 per meter; both measures were considered by Stone & Webster to compare favorably with project costs of similar magnitude undertaken in other countries. Using the Private Sponsors' proved plus probable reserves case, overall finding and development cost of total produced oil was estimated at about US$ 5.2/barrel. Based on published reports, this was in line with the 5-year worldwide average (estimated at about US$ 5.3/barrel) cost of finding and developing reserves by large integrated oil companies.

In addition to the components mentioned in the table above, there were: (a) project preparation costs for the two Governments; and (b) complementary activities regarding (i) the development and implementation of environmental and social mitigation plans for the project; and (ii) the development of Chad’s revenue management program.

**Bond Issue and Shareholder Financing**

At the request of GoT and GoC, COTCO and TOTCO issued bonds on the international capital markets of about US$ 400 million in total. These bonds were pari passu with the other senior loans made to the pipeline companies, namely by IFC and under the coverage provided by the export credit agencies. The bonds met the US$ 400 million target. The bond issue provided two main benefits for the two countries. First, it reduced the need for equity financing from the two Governments, by generating more debt financing. This meant the Governments' objectives of maintaining their percentage shareholdings in COTCO closer to the levels they had originally targeted (namely 15 percent for Cameroon and 5 percent for Chad), while also generating more equity per dollar invested (and, ultimately, per dollar borrowed from IBRD/EIB). Second, was a vehicle to provide for formal recognition by and official ratings from international capital markets and rating agencies, and would support efforts to attract foreign investment.
Risk Allocation & Financial Security Arrangements

All PPP projects undergo testing for (a) affordability; (b) risk allocation; and (c) value for money. It is in the (c) risk allocation phase of project assessment that the financial security arrangements need to be formulated. The Risk Analysis summary provided above in the case study shows the assessment by the PPP project team of the various categories of risks that need to be allocated among the parties to the PPP agreement based on the capacity of each party to manage that category of risk.

In the risk allocation process, when a party is allocated a certain risk, it responds with its plan for the management of that risk. This is the process that generates the financial security package.

The key elements of risk allocation and financial security arrangements for the Chad-Cameroon Oil Pipeline case were as follows:

**Pre-Completion Security Arrangements**

The security package for the IFC loans to TOTCO and COTCO includes a pre-completion guarantee against commercial risks to be provided by creditworthy affiliates of the Private Sponsors.

**Project Completion Security Arrangements**

Project Completion was achieved upon the satisfaction of certain physical completion, reserves adequacy and financial tests.

**Post-Completion Loan Security Arrangements**

The IBRD loan to Chad, an IDA-only country, was provided under the traditional elements of the enclave loan structure. Under this structure, IBRD loans were supported, in addition to the sovereign repayment obligations, by various support arrangements designed to enable IBRD to look directly to the project revenues for repayment, together, in certain cases, with other guarantees. The project is expected to generate for Chad annual revenues far in excess (by a factor of greater than four) of the annual debt service payments due the Bank under the loan. The proposed IBRD loan would benefit from the following support arrangements:

The IBRD loan benefited from commercial risk pre-completion guarantees covering principal (used to finance Chad's equity investments in COTCO and TOTCO) and interest due under the IBRD loan. These guarantees were provided by creditworthy Exxon/Petronas/Chevron companies, on a several basis (i.e., each oil company guarantor would be responsible for obligations under its guarantee, but not for the obligations of the other companies under their respective guarantees).

The IBRD loan would be repaid directly from an off-shore escrow account, specifically established to receive all royalties, taxes and dividends payable to Chad in connection with the
project. An offshore Chad debt service reserve account would also be established to support debt service payments due to IBRD; this reserve account would hold at all times an amount equal to 18 months of debt service payments due to IBRD under the Chad loan. The reserve would be funded from Chad’s royalties, taxes and dividends generated during the first 12 months of project operations.

In the event of interruption of project operations, Chad’s revenues would remain in the escrow account until project operations resume (i.e., a moratorium on disbursements to Chad from the offshore escrow account). Chad has chosen the floating rate dollar-based single currency IBRD loan product (US dollars matches the currency of project revenues). The loan would have a five-year grace period, an eight-year repayment period, with level repayment of principal. The total loan amount of US$ 39.5 million would include US$ 3.5 million in unallocated funds, which would allow Chad to maintain its equity stake in COTCO and TOTCO if there is a call for an additional 10 percent equity infusion requirement because of cost overruns or only partial success of the COTCO/TOTCO bond offering.

The IBRD loan to Cameroon, an IDA-only country, was supported by various additional arrangements. Like the loan to Chad, it would benefit from pre-completion commercial risk guarantees provided, on a several basis (i.e., separately), by creditworthy Exxon/Petronas/Chevron companies. However, in lieu of an escrow account/debt service reserve support structure, the Bank charged Cameroon a premium. This premium structure was better adapted to Cameroon’s current commercial debt situation than the escrow account/reserve approach given, inter alia, the Government’s outstanding commercial debt and the inter-creditor contractual obligations that characterize some of these loans.

The premium for Cameroon was set at 10 percent of the loan amount (i.e., US$ 5.34 million of the loan total of US$ 53.4 million). Like other loan charges, this amount has been capitalized into the total loan amount and would be drawn down in relative proportion to other disbursements under the loan.

Cameroon selected the fixed spread loan, denominated in dollars (which matches the currency of project revenues); with a five-year grace period, followed by a ten-year repayment period, with level repayment of principal. Cameroon capped its equity infusion at the US$ 70 million provided by IBRD and EIB, so the IBRD loan did not include any unallocated provision.

The security package for the IFC loans to TOTCO and COTCO included a pre-completion guarantee against commercial risks to be provided by creditworthy affiliates of the Private Sponsors. Post completion, the IFC loans were secured by the assets and revenues of TOTCO and COTCO and other suitable support arrangements were furnished by the Private Sponsors and their affiliates.

The European Investment Bank (EIB) provided financing to GoC (about US$ 30 million equivalent) and GoT (about US$ 17 million equivalent) to finance the Governments' respective equity investments in the pipeline companies. EIB loans provided with a maturity of 15 years, including 5 years' grace, and an interest rate of 3 percent per annum. EIB also provided additional non-concessional financing directly to the Private Sponsors. The Bank coordinated its activities with EIB, as well as with the IFC/ Senior Lenders group, and entered into a
memorandum of understanding setting out principles for coordination, cooperation and concerted action between the Bank and EIB, and with IFC, US EXIM, COFACE and the other Senior Lenders.

**Oil Market Price Security Arrangements**

The project generates substantial revenues to the participating governments. If the price of oil drops, Chad revenues will be adversely impacted because they are a function of market-based oil price calculations, but Cameroon revenues will be essentially unaffected since primarily based on volume shipped, not price.

For Private Sponsors, risk of substantial long-term depressed price projections may delay or stall decisions to invest. During operations, revenues will be sufficient to cover ongoing Private Sponsor costs, particularly given large up-front financial commitment.

For the Senior Lenders (including IFC) the sensitivity analysis shows that, using the proved reserves case and World Bank oil price forecasts, the project could withstand a 32% drop in prices and still be able to service its debt.

**Cost Overruns Security Arrangement**

Although cost overruns are foreseeable, they should be manageable given Private Sponsors' financial investment in project and resources to finance overruns. Cost estimates independently certified.

**Breach of Contract Security Arrangements**

Breach of Contract is covered by Government and Private Sponsor Contractual Stability Commitments, and risk of breach is mitigated by continuing financial benefits (both direct and indirect). Protection from unanticipated disputes is mitigated by extensive government evaluations prior to execution of the agreements, and the Chad negotiators were assisted by external advisors. Bank Group participation in the financing scheme enabled all participants to understand their rights and obligations.

Contractual stability risks are more pronounced over the long-term, for example relative changes in pricing for oil sales, transportation and other costs. These risks are mitigated by sound project implementation over the medium term to provide supportive context for any potential adjustments.

Breach of Contract risk was also mitigated by revenue management plan in Chad, Government equity in COTCO and TOTCO, significant engagement of Bank Group and EIB. World Bank and Senior Lenders mitigated Breach of Contract risk via direct agreements with Governments.

**Technology Risk Security Arrangements**
The technology was well proven, and the extensive experience of Private Sponsors mitigated any risk of technology not achieving targeted results. Creditworthy Private Sponsor companies provided pre-completion guarantees, enabling financial security for that phase of the project.

**Operator Risk Security Arrangements**

Esso Chad (Exxon) had considerable experience in operating pipelines, and is the project operator.

**Environmental Risk Security Arrangements**

Environmental Assessments addressed potential risks. Primary responsibility for environmental damage was allocated to the private sector operator, under Government and Bank Group supervision. **This is a key factor for consideration by Treasury for the Kenya-Uganda Pipeline.**

**Social Impact Security Arrangement**

Compensation/Resettlement plans, financing to address induced impacts on producing region under IDA capacity building operation, and regional development planning process. Responsibility shared between Governments and private sector operators under Bank Group supervision.

**Financial Returns Security Arrangement**

Projected financial results are adequate for the equity holders and Senior Lenders.

**Revenue Security Arrangement**

Private Sponsors' oil-trading affiliates committed to lift oil under "take and pay" off-take Agreements.

**Debt & Equity Security Arrangement**

Quality of Private Sponsors, Bank Group involvement, offshore nature of the financing, minimum subscription requirement to both B and ECA-supported loans, and possible underwriting of part of or the entire B loan.

**Currency Risk Security Arrangement**

Revenues and debt service obligations are defined in U.S. Dollars.

**Security Arrangement by Insurance**

TOTCO, COTCO, the Upstream Operator (Esso Chad) and the other members of the Upstream Consortium subscribed to a number of insurance coverages, which were placed in the international markets to cover the overall project construction and operational phases. The overall insurance program, which was reviewed by an independent insurance consultant on
behalf of the Senior Lenders and substantially agreed upon with TOTCO, COTCO and the Upstream Consortium members, was considered adequate.

**Financial Security by Auditing and Financial Reporting**

TOTCO, COTCO, the Upstream Operator (Esso Chad) and the other members of the Upstream Consortium: (a) establish and maintain, to the satisfaction of the World Bank Group, adequate accounts and records, including separate accounts and records for the Project; (b) engage independent auditors acceptable to the Bank Group to audit their accounts, including the Project accounts and financial statements, in accordance with internationally acceptable accounting principles and in such detail as the Bank Group may request; and (c) undertake audits annually and submit an audit report to the Bank Group within six months after the end of each fiscal year.

The Bank also receives: (a) annual audits of the Petroleum Revenue Account and Petroleum Future-Generations Investment Account, established by GoT; and (b) annual audits of the separate off-shore accounts established to support IBRD and the Senior Lender loans, including the account established to receive Chad's royalty and other receipts.

In addition, TOTCO and COTCO maintain offshore dollar-denominated escrow accounts to receive equity and debt funding (i.e., during construction), as well as revenues (during operations), as well as offshore Debt Service reserve accounts securing the Senior Lenders holding six-months' principal and interest due to these lenders. Each of the Upstream Consortium members also maintains an offshore dollar-denominated escrow account to receive proceeds from the sale of its oil from the three fields (excluding Chad royalty), and from which its share of the tariff payments due to COTCO and TOTCO will be made. All escrow accounts of TOTCO, COTCO and the Upstream Consortium members is operated in accordance with the IFC/Senior Lenders' semi-annual budgetary controls for both the Project's construction and operational phases. These budgets are also used by the Senior Lenders (including IFC) to produce independent financial projections to monitor reserves adequacy and minimum debt coverage ratios requirements. Chad royalties and other revenues are paid into the offshore escrow account established to secure the IBRD and EIB loans; the balance is then distributed to Chad to be applied in accordance with a revenue management program.

**Financial Security by Monitoring & Compliance**

TOTCO, COTCO, the Upstream Operator - namely, the agencies implementing the project - submits quarterly reports to the Bank Group, covering, inter alia, progress on physical implementation, procurement, financial commitments and other elements of project progress, and the other members of the Upstream Consortium submit summary reports quarterly.

TOTCO, COTCO, the Upstream Operator submits quarterly monitoring reports on implementation of the environmental management plan (to be made available by the Bank Group to the public). GoT and GoC submit annual reports regarding project progress in connection with the annual reviews to be carried out with the Bank, and quarterly reports regarding implementation of the EMP. Representatives of TOTCO, COTCO, the Upstream Operator, GoT and GoC, and the Bank meet annually to review progress in project
implementation and a mid-term review took place two years after loan effectiveness. The Governments submitted to the Bank, with assistance of COTCO, TOTCO and the Upstream Operator, a Project Implementation Completion Report within six months after loan closing.

The Bank Group, together with the other lenders, also employed an external compliance monitor group to assist it in monitoring implementation of the environmental management plan. The external compliance-monitoring group included a spectrum of skills, such as social development/consultation expertise, ecological/natural resource specialization, experience in the implementation of pipelines/other linear developments, and strong knowledge of the oil industry. The external compliance monitor group conducts periodic site visits (quarterly during the construction period and annually thereafter), and reviews the monitoring reports prepared by the private operators and the Governments, and liaises with local groups in-country as appropriate. The Bank Group has periodic meetings with local NGOs to assess progress in implementation of the project, including the environmental management and resettlement/compensation plans.

Quarterly progress reports and proved reserves estimates are submitted by COTCO/TOTCO and/or by the Upstream Consortium members to the Senior Lenders (including IFC), with a copy to the Bank. These are reviewed by independent technical consultants, who have the right to make site inspections on behalf of the Senior Lenders, and independent petroleum engineering consultants. An independent insurance consultant review annuallys the project insurance on behalf of the Senior Lenders to ensure adequate coverage is maintained.

III. Financial Security Package Contract Model

The document below is an international best practice example of the appropriate financial security contract for a gas/oil pipeline PPP transaction, from the Energy Regulator in Republic of Ireland.

1. COMPLIANCE PROVISIONS

Approved Credit Rating

If and for so long as the long term unguaranteed and unsubordinated debt of a Counterparty is rated BBB or higher by S&P and/or BBB or higher by Fitch and/or Baa2 or higher by Moody's (each an “Approved Credit Rating”), then such Approved Credit Rating shall exempt the Counterparty from the requirement to provide Security Cover. The Transporter will notify each Counterparty of the aggregate Financial Security Amount for which it is liable further to Section 5. The Transporter will also be entitled to recover all costs reasonably incurred in order to recover such monies.

A Counterparty shall provide the Transporter with such information as the Transporter may reasonably require in order to satisfy itself that the Counterparty has an Approved Credit Rating. Such information may include the Counterparty’s company registration number, details of its jurisdiction of incorporation, certified copies of letters from any relevant credit rating
agency and any other information that the Transporter may reasonably require in order to carry out an independent verification of any claim to have an Approved Credit Rating.

If a Counterparty has an Approved Credit Rating and such credit rating is subsequently downgraded to less than the Approved Credit Rating or withdrawn, the Counterparty must immediately notify the Transporter of any such downgrade or withdrawal, including giving details of its revised credit rating (if any) and certified copies of any correspondence with any relevant credit rating agency. If a Counterparty ceases to have at least an Approved Credit Rating, then such Counterparty must, by 5pm on the tenth (10th) Business Days of it so ceasing, provide Security Cover in accordance with this Package in respect of the Financial Security Amount. The Counterparty may request the Transporter to provide an updated calculation of the aggregate Financial Security Amount for which the Counterparty must provide to the Transporter pursuant to this Financial Security Package.

Security Cover

While a Counterparty has less than an Approved Credit Rating or no credit rating, the Counterparty must provide for the benefit of the Transporter and maintain Security Cover in respect of the Financial Security Amount in one or more of the following forms.

Letter of Credit

an irrevocable standby letter of credit in or substantially in the form attached at Appendix 1, or in such other form as may be acceptable to the Transporter (a “Letter of Credit”) issued for the account of the Counterparty in favour of the Transporter which Letter of Credit shall allow for partial drawings, if necessary, and shall provide for payment to the Transporter forthwith on demand and shall be issued either by:

(a) a Bank with long-term unguaranteed unsubordinated debt rated at least AA by S&P and/or AA2 by Moodys and/or AA by Fitch, or

(b) a subsidiary of a Bank which has total balance sheet assets of not less than €1,000 million (or equivalent in other currencies) and the long-term unguaranteed unsubordinated debt that is rated at least A by S&P or A2 by Moodys or A by Fitch.

For the purposes of this Financial Security Package, a “Bank” means the holder of a licence under Section 9 of the Central Bank Act 1971 (as amended) or the holder of an authorisation under EU Directive No. 2000/12/EC of 20 March 2000; or

Charged Account

a “Charged Account” means an interest bearing deposit account with a Bank that satisfies the criteria outlined in Section 3.2.1 (a) or (b) to which money has been credited and which account is charged by way of Account Charge for any amount becoming due to the Transporter and from which funds may be released to the Transporter on Demand to discharge sums due and payable from time to time to the Transporter pursuant to an Agreement and/or the Code (a
pro-forma Account Charge which is acceptable to the Transporter has been attached as Appendix 2; or

Cash Deposit Option

a cash deposit in an interest bearing deposit account specified by the Transporter where interest on the amount deposited will accrue for the benefit of the Counterparty at market related rates of interest after deduction for any tax or bank charges. The money standing to the credit of such an account (a “Cash Deposit”) is to be held by way of Security Cover pursuant to an agreement (a “Deposit Agreement”) that will allow sums due and payable from time to time by the Counterparty pursuant to an Agreement and/or the Code to be released to the Transporter on demand (a pro-forma Deposit Agreement that is acceptable to the Transporter has been attached as Appendix 3); or

Qualifying Guarantee

a guarantee for the payment of all monies due to the Transporter under the Agreement and/or the Code and all costs reasonably incurred in order to recover such monies in accordance with the guarantee, which guarantee shall be in or substantially in the form attached at Appendix 4, or in such other form as may be acceptable to the Transporter (a “Qualifying Guarantee”) and which is issued in favour of the Transporter by an entity with an Approved Credit Rating; or

Other

such other form of security as is acceptable to the Transporter and approved by the Commission.

Approval Process

Counterparties and the Transporter shall adhere to the following procedure in tendering and approving proposed Security Cover.

Letter of Credit Option

Where a Counterparty proposes to provide a Letter of Credit as Security Cover, the Counterparty shall provide the proposed form of Letter of Credit to the Transporter in advance of issue and the Transporter will review the proposed form of Letter of Credit and verify that such Letter of Credit will be issued by an entity which meets one of the criteria specified in Section 3.2.1(a) or (b). If the Transporter is satisfied with the proposed form of Letter of Credit and has so verified the issuer thereof, the Transporter shall approve the proposed form of Letter of Credit and shall confirm such approval to the Counterparty.

The Counterparty shall thereupon immediately arrange for the issue of the Letter of Credit.

A Letter of Credit shall be deemed to be received by the Transporter on the date that the original signed copy of Letter of Credit is received by the Transporter from an issuer which
meets one of the criteria specified in Section 3.2.1(a) or (b), in a form previously approved by the Transporter.

Charged Account

Where the Counterparty proposes to provide a Charged Account with Account Charge the Counterparty shall provide to the Transporter the proposed form of Account Charge together with details of the Charged Account which shall be with a Bank or other entity which satisfies the criteria in Section 3.2.1. If the Transporter is satisfied with the proposed form of Account Charge and Charged Account (including form of bank mandates in respect of such Charged Account) the Transporter shall approve the proposed form of Account Charge and Charged Account and shall confirm such approval to the Counterparty. The Counterparty shall deliver to the Transporter two (2) signed original hard copies of the Account Charge (including two (2) signed original hard copies of the forms of notice and acknowledgement and acknowledgement to BGE referred to therein) copies of the relevant mandates in respect of the Charged Account and evidence of the amount credited to such Charged Account) and if so required sign the Account Charge.

A Counterparty shall be deemed to have provided Security Cover by way of Charged Account on the date of receipt by the Transporter of the duly executed Account Charge (in a form as previously approved by the Transporter) together with the original forms of notice and acknowledgement and acknowledgement referred to therein, and evidence of deposit of moneys to the Charged Account in accordance with such Account Charge.

Cash Deposit Option

Where a Counterparty proposes to provide a Cash Deposit as Security Cover the Counterparty shall provide to the Transporter the proposed Deposit Agreement together with details of the proposed Cash Deposit together with confirmation of the amount to be lodged or lodged to the Cash Deposit. The Transporter shall review the Deposit Agreement and the Cash Deposit and if the Transporter is satisfied with the proposed Cash Deposit and Deposit Agreement the Transporter shall approve the proposed form of Deposit Agreement and Cash Deposit and shall confirm such approval to the Counterparty.

The Counterparty will be deemed to have provided a Cash Deposit by way of Security Cover on the later of:

(a) the date that the sum of money deposited to an acceptable account as a Cash Deposit, when aggregated with all other Security Cover that that Counterparty is providing, is at least equal to such Counterparty’s then applicable Financial Security Amount; and

(b) the date of delivery of the executed Deposit Agreement to the Transporter in the form as previously approved by the Transporter.
Qualifying Guarantee

Where a Counterparty proposes to provide a Qualifying Guarantee as Security Cover, the Counterparty shall provide the proposed form of Qualifying Guarantee to the Transporter in advance of issue along with evidence that the entity providing such a guarantee has an Approved Credit Rating. The Transporter will review the proposed form of Qualifying Guarantee and verify that the entity providing such Qualifying Guarantee has an Approved Credit Rating. If the Transporter is satisfied with the proposed form of Qualifying Guarantee and has so verified the issuer thereof, the Transporter shall approve the proposed form of Qualifying Guarantee and shall confirm such approval to the Counterparty.

The Counterparty shall thereupon immediately arrange for the issue of two (2) signed copies of the Qualifying Guarantee and send to the Transporter the two (2) signed original copies of the Qualifying Guarantee and a legal opinion or other confirmation satisfactory to the Transporter from lawyers (other than the Counterparty’s in-house lawyers) qualified in the laws of the place of incorporation of the entity that has issued the Qualifying Guarantee that the Qualifying Guarantee comprises enforceable obligations of that entity. The Transporter shall review the documents sent to it and if satisfied sign the Qualifying Guarantee. The Transporter shall then return a copy to the applicant Counterparty.

The Counterparty will be deemed to have provided Security Cover by a Qualifying Guarantee on the date that the original signed copies of the Qualifying Guarantee are received by the Transporter from an entity which has an Approved Credit Rating in a form previously approved by the Transporter and if the Transporter is satisfied with the legal opinion or confirmation that the obligations of the issuer of the Qualifying Guarantee are enforceable ones.

Other

Where the Transporter with the approval of the Commission has agreed to accept some other form of Security Cover, the procedure to be followed by the Counterparty and the Transporter in approving the form of such Security Cover shall be specified by the Transporter to the Counterparty at the relevant time.

The Transporter shall notify the applicant Counterparty, when the applicant Counterparty has successfully complied with all the relevant Security Cover provisions.

Changes to forms of Security Cover

The Transporter’s requirements with respect to the form and content of Letters of Credit, Account Charge, Deposit Agreement, Qualifying Guarantees and other forms of Security Cover may change over time to reflect, among other things, changes in applicable law and regulation and market practice. Where such changes are material the Transporter will issue the changed pro-forma document(s) to the Commission for review.

Subject to Commission approval the Transporter may require Counterparties to amend or procure the amendment of the Security Cover provided by them. The Transporter, where
appropriate, will advise all relevant parties in advance of any required amendments and the time available to the Counterparty to comply therewith.

Where the Transporter’s requirements with respect to the form and content of Security Documents change, the Transporter will, notify the Commission of such changes and where appropriate, publish new Appendices to this Package to reflect its changed requirements.

Compliance with Package

A Counterparty shall be deemed to be in compliance with such Counterparty’s obligations to comply with this Financial Security Package from time to time when and for so long as such Counterparty shall have provided to the Transporter and maintains Security Cover in respect of the Financial Security Amount (as same may be recalculated from time to time).

2. SITEWORKS

The provision of Security Cover is required from Counterparty’s engaging in Large New Connections and/or Connection Siteworks and/or Operational Siteworks Services in addition to Security Cover for such Capacity Bookings and Use of Transmission and Distribution Systems. Calculation of the amount of cover required is set out in full under Section 5.

Large New Connections

A large new connection is deemed to be any connection with an Annual Quantity (AQ) greater than 0.5 Million Standard Cubic Meters (mscm) or with connection costs greater than €100k;

The Financial Security Amount required for a Large New Connection will be determined by the Transporter and specified in the agreement with the Counterparty.

Connection Siteworks

Connection Siteworks are activities outlined in the Siteworks Charges Document and which may be undertaken by Bord Gais pursuant to the Shippers Connection Siteworks Agreement at the request of the Counterparty.

The Counterparty to such an agreement shall be required to provide Security Cover for such services to be included in the Financial Security Amount as calculated under Section 5. The Transporter will review the Financial Security Amount as deemed necessary depending on the level of activity and in accordance with Section 6.

Operational Siteworks Services

Operational Siteworks Services are activities outlined in the Siteworks Charges Document and which may be undertaken by Bord Gais pursuant to the Shippers Operational Siteworks Services Agreement at the request of the Counterparty.
The Counterparty to such an agreement shall be required to provide Security Cover for such services to be included in the Financial Security Amount as calculated under Section 5. The Transporter will review the Financial Security Amount as deemed necessary depending on the level of activity and in accordance with Section 6.

3. FINANCIAL SECURITY AMOUNT

Overview

Financial Security Amount in respect of the period commencing on 1st July, 2005 and any period thereafter is based on seventy-two (72) calendar days’ worth of Capacity Charges, Commodity Charges and VAT as appropriate for Use of the Transmission and Distribution System and provisions for Siteworks and/or NDM Change of Shipper Cover (to allow for overnight switching) and/or Large New Connections (as appropriate).

Financial Security Amount in respect of the period up to the 1st July, 2005 is based on three (3) months worth of Entry Capacity Charges and three (3) months of Exit Capacity Charges.

Calculation of Financial Security Amount

The Transporter shall calculate the Financial Security Amount in respect of the period subsequent to the 30th June, 2005 as follows:

Entry Capacity Cover;

\[
\text{Entry Capacity Cover} = \sum \text{Entry Capacity Bookings} \times \text{Capacity component of the Entry Tariff} \times 72 \text{ Days in Year} \times \text{VAT}
\]

Exit Capacity Cover;

\[
\text{Exit Capacity Cover} = \sum \text{Exit Capacity Bookings} \times \text{Capacity component of the Exit Tariff} \times 72 \text{ Days in Year} \times \text{VAT}
\]

Supply Point Capacity Cover;

\[
\text{Supply Point Capacity Cover} = \sum \text{Supply Point Capacity Bookings} \times \text{Capacity component of the Distribution Tariff} \times 72 \text{ Days in Year} \times \text{VAT}
\]

Commodity Cover;

Commodity Cover is calculated as follows:

(a) where the Counterparty has at least six (6) continuous months worth of historical data for Entry and/or Exit and/or Supply Point Commodity Charges:
Total Commodity Cover = $\Sigma$ Entry Commodity Charges * 72 X * VAT plus $\Sigma$ Exit Commodity Charges * 72 X * VAT plus $\Sigma$ Supply Point Commodity Charges * 72 X * VAT

Where “X” equals 365 (or 366) calendar days where 12 months historical data is available or such less period in respect of which historical data is available (being not less than 183 days) where twelve (12) months historical data is not available,

(b) where the Counterparty is a new entrant to the market until such time as the Counterparty has six (6) months historical data available Commodity Cover is calculated as:

Total = Commodity Cover $\Sigma$ Capacity Bookings * Capacity component of the Tariff * 72 Days in Year * Percentage Default * VAT

Where the Percentage Default is equal to 115%

NDM Change of Shipper Cover;

Further to Section 6 the Transporter will review the level of Counterparty’s activity within the NDM sector. Should the level of NDM Change of Shipper activity result in an aggregate increase of Supply Point Capacity (SPC) of 10,000kWh in any given month the Counterparty will be required to provide additional cover in the form of a deminimis amount of Fifteen Thousand Euro (€15,000). The Transporter may increase the amount of such cover as deemed necessary based on further reviews of the Counterparty’s level of activity.

For the avoidance of doubt, such additional cover is in addition to the Supply Point Capacity Cover provided by the Counterparty’s for their existing NDM SPC and all other cover required in accordance with this Financial Security Package.

Connection Siteworks Cover;

Further to Section 6 the Transporter will review the level of Counterparty’s Connection Siteworks activity. Should the level of such activity exceed in value an aggregate of Five Thousand Euro (€5,000) in any given month the Counterparty will be required to provide cover in the form of a deminimis amount of Five Thousand Euro (€5,000). The Transporter may increase the amount of such cover as deemed necessary based on further reviews of the Counterparty’s level of activity.

Operational Siteworks Services Cover;

Further to Section 6 the Transporter will review the level of Counterparty’s Operational Siteworks activity. Should the level of such activity exceed in value an aggregate of Five Thousand Euro (€5,000) in any given month the Counterparty will be required to provide cover in the form of a deminimis amount of Five Thousand Euro (€5,000). The Transporter may increase the amount of such cover as deemed necessary based on further reviews of the Counterparty’s level of activity.
Total Financial Security Amount;

Financial Security Amount = Σ Entry Capacity Cover + Σ Exit Capacity Cover + Σ Supply Point Capacity Cover + Total Commodity Cover + NDM Change of Shipper Cover + Operational Siteworks Services Cover + Connection Siteworks Cover

And/Or

Large New Connections;

Large New Connections Cover = As determined by the Transporter on a case by case basis

Where:

where appropriate to the Counterparty

VAT (Value Added Tax)

Value added tax is applied at current rates. For those Counterparties exempt from Value Added Tax (VAT) the provision of Security Cover shall be the net amount as calculated in Section 5.2 exclusive of VAT.

Calculation of Financial Security Amount

The Transporter shall calculate the Financial Security Amount in respect of financial obligations pursuant to the Agreement[s] in respect of the period up to the 1st July as follows:

Entry Capacity Cover:

Entry Capacity Cover = Σ Entry Capacity Bookings * Capacity component of the Entry Tariff * 3

Exit Capacity Cover:

Exit Capacity Cover = Σ Exit Capacity Bookings * Capacity component of the Exit Tariff * 3.

Total Financial Security Amount:

Financial Security Amount = Σ Entry Capacity Cover + Σ Exit Capacity Cover

Notification of Financial Security Amount

The Transporter will issue a notice (a “Security Cover Notice”) to an applicant Counterparty containing the details of the Financial Security Amount required and the calculations used to derive this amount.

4. REVIEW OF FINANCIAL SECURITY AMOUNT
Review Time Scale

All sites

The Financial Security Amount in respect of which Security Cover is required to be provided by a Counterparty may be reviewed on a monthly basis and in any event will be reviewed annually. The existing Financial Security Amount shall be compared against the Financial Security Amount that would be required based on new or revised capacity bookings, Change of Shipper, and/or Siteworks and/or Large New Connections.

Large New Connections

The Financial Security Amount provided by Counterparties in relation to Large New Connections may be reviewed on a monthly and/or yearly basis and/or upon a revision of the estimated cost of the project. The existing Financial Security Amount shall be compared against the Financial Security Amount that would be required based on any revision and/or payment to date and/or completion of a phase of the project as set out under Section 4.1.

The Transporter will issue either a Security Cover Increase Notice or Security Cover Decrease Notice to a Counterparty where the amount of existing Security Cover is not the same as the amount of Security Cover that is required based on new or revised capacity bookings and/or Change of Shipper, and/or Large New Connections and/or Siteworks.

Security Cover Increase Notice

If the aggregate amount secured pursuant to a Counterparty’s existing Security Cover (after reducing the amount by Demands made) is less than the Financial Security Amount applicable to such Counterparty upon a recalculation of such Financial Security Amount in accordance with Section 5, the Transporter shall notify the Counterparty in writing (a “Security Cover Increase Notice”) of the applicable recalculated Financial Security Amount and the Security Cover Increase Amount.

The Counterparty shall forthwith procure that the Transporter receives the necessary additional Financial Security Cover in respect of the increased Financial Security Amount by 5pm on the tenth (10th) Business Days after the date of issue of a Security Cover Increase Notice, as follows.

Letter of Credit

The Counterparty may procure the issue of a new Letter of Credit for an amount equal to the new revised Financial Security Amount or an additional Letter of Credit for an amount equal to the Financial Security Amount from an entity that satisfies one of the criteria set out in Section 3.2.1(a) or (b) and shall follow the procedures specified in Section 3.3 for issue of that Letter of Credit unless the Letter of Credit is in terms identical (except with respect to amount) to one being relied upon as Security Cover, when the Counterparty may arrange for issue without prior approval of the Transporter; or
Charged Account

The Counterparty may make a deposit of the Security Cover Increase Amount to an existing Charged Account that is being used as Security Cover and provide evidence of the account balance in such Charged Account together with such other documentation as may be necessary to ensure that the Account Charge extends to and applies to such increased balance to reflect the new amount; or

Cash Deposit Option

The Counterparty may make a Deposit of the Security Cover Increase Amount to a cash deposit account designated by the Transporter that is being used as Security Cover, provide evidence of such Deposit to the Transporter and sign an appendix to the Deposit Agreement specifying the new amount or such other documentation as may be reasonably required by the Transporter to ensure that the Deposit Agreement extends to and includes the deposit of the Security Cover Increase Amount.

Qualifying Guarantee

The Counterparty may provide an acknowledgement by the issuer of a Qualifying Guarantee that the Qualifying Guarantee being relied upon as Security Cover covers any increase in liability of the Counterparty resulting from the recalculation on the Financial Security Amount; or

Other

The Counterparty may provide such additional cover for the Security Cover Increase Amount by such other means as shall be acceptable to the Transporter with approval from the Commission, within the timeframe allowed.

For the avoidance of doubt, the Counterparty may provide Security Cover for the Security Cover Increase Amount by a combination of options available under Sections 6.2.1 to.

Security Cover Decrease Notice

If the aggregate amount secured pursuant to a Counterparty’s existing Security Cover (after reducing the amount by Demands made) is greater than the Financial Security Amount applicable to such Counterparty upon a recalculation of such Financial Security Amount in accordance with Section 5, the Transporter shall notify the Counterparty in writing (a “Security Cover Decrease Notice”) of the applicable recalculated Financial Security Amount and the Security Cover Decrease Amount.

The Counterparty shall be entitled to request the Transporter to review such Counterparty’s existing Security Cover as follows:

Letter of Credit
Where a Letter of Credit has been provided as Security Cover, the Transporter shall notify the Counterparty that the maximum liability under the Letter of Credit may be reduced by the Security Cover Decrease Amount and, if requested by the Counterparty, return the original Letter of Credit to the issuer upon receipt of a new Letter of Credit from the issuer in the same terms (except reduced in amount by the Security Cover Decrease Amount) as the original; or

Charged Account

Where a Charged Account has been provided as Security Cover, the Counterparty shall then have five (5) Business Days, from the date of the Security Cover Decrease Notice, to notify the Transporter if they wish to reduce their Security Cover (e.g. for reasons of administration costs or likely future increase). If such notification is made, the Transporter shall have ten (10) Business Days from the date of receipt by the Transporter of such notice from the Counterparty to notify the issuer with which the Charged Account is held to transfer the excess from the Charged Account into the Counterparty’s trading bank account, as advised; or

Cash Deposit Option

Where a Cash Deposit has been provided as Security Cover, the Counterparty may within five (5) Business Days, from the date of the Security Cover Decrease Notice, to notify the Transporter if they wish to reduce their Security Cover (e.g. for reasons of administration costs or likely future increase). If such notification is made, the Transporter shall have ten (10) Business Days from the date of receipt by the Transporter of such notice from the Counterparty to transfer the excesses from the Cash Deposit Account into the Counterparty’s trading bank account, as advised.

Other

Where some other form of Security Cover has been accepted the Counterparty may within five (5) Business Days, from the date of the Security Cover Decrease Notice, notify the Transporter if they wish to reduce their Security Cover;

Substitute and replacement Security Cover

If the issuer of a Letter of Credit provided to the Transporter as Security Cover ceases to be an entity which satisfies one of the criteria set out in Section 3.2.1(a) or (b) the Counterparty shall forthwith procure the issue of a substitute Letter of Credit by an entity that satisfies one of such criteria or provide Security Cover in one of the other forms set out in Section 3.2.

If the issuer of a Qualifying Guarantee provided to the Transporter as Security Cover has its credit rating withdrawn or downgraded to less than an Approved Credit Rating, the Counterparty shall forthwith procure a replacement Qualifying Guarantee from an entity having an Approved Credit Rating, or provide Security Cover in one of the other forms contemplated by Section 3.2.
If the Security Cover provided by the Counterparty under Section 3.2.5 ceases to satisfy the Transporter and the Commission the Counterparty shall forthwith procure a replacement form of cover in one of the other forms contemplated by Section 3.2.

Consequences of Breach of the Financial Security Package

The consequences of breach or non compliance by a Counterparty with this Financial Security Package at any time shall be as prescribed in the Agreement(s).

In addition and without prejudice to the rights and remedies available to the Transporter pursuant to the Agreements in respect of any breach, or non-compliance, by a Counterparty with this Financial Security Package where the Financial Security Package has not been complied with by the Counterparty within the time specified in this Financial Security Package or any Agreement a Fee of EURO 250 per Business Day will be charged to the Counterparty until the Financial Security Package is complied with or the date the Agreement(s) terminate in accordance with the Code or the Agreement. At the end of each month, the Transporter shall issue an invoice for the amount of such Fees accrued by the Counterparty in the preceding month. The Counterparty shall pay the Transporter the sum set out in the invoice by the Due Date as set out under the Code.

The Transporter shall notify the Commission at the end of April and October of the financial amount of these Fees collected from each Counterparty during the gas year to that date.

5. DEMANDS ON SECURITY COVER

Overview

Subject to the terms of the relevant Security Cover, the Transporter shall be entitled to make a Demand on the Security Cover provided by a Counterparty if the Counterparty has failed to pay any amount due and payable under or pursuant to the Code or any Agreement on the fifth (5th) Business Days after the Due Date thereof.

Demand on Security Cover

Subject to the minimum Demand amount specified in Section 7.3, if by 10:00hours on the fifth (5th) Business Day after the Due Date the monies are still outstanding (in whole or in part), the Transporter may without prejudice to any other rights of the Transporter under the Code or Agreement(s) make a Demand on the Counterparty’s Security Cover by issue of a notice (a “Demand Notice”) for all or part of any amounts outstanding including any interest accruing

Letter of Credit

Where a Letter of Credit has been provided as Security Cover, the Transporter shall make a Demand in accordance with the terms thereof to the issuer thereof for payment of an amount thereunder not exceeding the aggregate amounts including interest unpaid by the Counterparty,
Charged Account

Where a Charged Account has been provided as Security Cover, the Transporter shall appropriate from the designated Charged Account the monies owed including interest, in accordance with the Account Charge.

Cash Deposit Option

Where a Cash Deposit has been provided as Security Cover, the Transporter shall appropriate from the designated cash deposit account the monies owed including interest, in accordance with the Deposit Agreement.

Qualifying Guarantee

Where a Qualifying Guarantee has been provided as Security Cover, the Transporter shall make a Demand in accordance with the terms thereof to the issuer thereof for payment of an amount not exceeding the aggregate amounts unpaid by the Counterparty including interest and instruct the Counterparty’s guarantor to transfer the outstanding amount to the Transporter’s account.

Other

In the case where the Transporter has accepted some other form of Security Cover, the Transporter shall take whatever action is required to draw down the monies owed (in whole or in part) including interest in accordance with the agreed arrangements.

Minimum Demand Amount

For outstanding amounts less than EURO 2,500 a Demand shall not be made on the Security Cover but interest shall accrue in accordance with the Agreements until paid however, should the amount remain unpaid for more than 90 calendar days and be greater than EURO 1,000 at the end of the 90 day period, then a Demand shall be made on the Security Cover. Demands thereafter in respect of amounts less than EURO 1,000 may be made at the discretion of the Transporter.

The Transporter will calculate the interest to be charged on a monthly basis as defined under the Code or the Agreement and where the principal plus interest exceeds the minimum Demand of EURO 2,500 then a Demand shall be made.

Replenishment

Following a Demand on a Counterparty’s Security Cover the Counterparty shall be obliged to replenish by 5.00 pm on the fourth Business Day the Security Cover such that the Counterparty shall have provided Security Cover in respect of the Financial Security Amount (after taking account of the Demand(s) made). The Transporter shall on the Date of Demand, notify the Counterparty (the “Call Notice”) of:
(a) the fact that the Demand has been made; and
(b) their obligation under their Agreements to replenish Security Cover up to the Financial Security Amount and that this replenishment will be required by 5pm on the fourth (4th) Business Days after the date of Demand on the Security Cover.

Immediate Drawdown

The Transporter will be entitled to and will with immediate effect make a Demand on the Counterparty’s Financial Security Cover, to the value of the Counterparty’s total debt exposure pursuant to the Agreements including interest, upon the occurrence of any event as specified in Part I (Legal and General) Section 4.4.2 of the Code.

6. RETURN OF SECURITY COVER

Upon termination of the Agreement(s), entered into between a Counterparty and the Transporter any Security Cover remaining once all the Counterparty’s payment obligations arising under or in connection with such Agreement(s) have been irrevocably and unconditionally discharged in full (and in the case of a Cash Deposit or Charged Account, any interest accrued, at market related rates of interest, in respect of such an account, less any bank and similar charges and any taxes deducted by the bank) will be returned to the Counterparty (or, in the case of a Letter of Credit or Qualifying Guarantee, to the issuer thereof) within ten (10) Business Days of the Transporter being satisfied that all such payment obligations have been irrevocably and unconditionally discharged in full.

Return of Security Cover is without prejudice to the rights of the Transporter under the Agreement(s) or the Code and does not relieve the Counterparty of any of its obligations or any liability in respect of the Agreement or the Code.
Appendix 7. Financial Security Package – Transport Sector

In preparing guidance for financial security packages for the transport sector, we selected toll roads because that is the area of sub-sector activity in which there is immediate activity for conducting PPP projects in Kenya. There is substantial interest in, and speculation on, various projects for airports and ports, but the roads transport sub-sector is the most advanced in terms of progress toward tender, bid, and contracting. Our approach to this section is as follows:

- Present a case study of a toll roads project in which we served as advisors;
- Highlight the financial security arrangements of the case study; and
- Provide an international best practice example of related legislation.

I. The Tribasa Toll Road Trust

With construction completed on two of its toll road concessions, Grupo Tribasa, S.A. de C.V. (Tribasa), one of the largest construction companies in Mexico, sought to arrange long-term financing for those roads in the international capital markets. The financing was to be secured by the toll revenues, which were estimated to be about N$70 million in 1994 and were expected to grow throughout the term of the concessions. In November 1993, a US$110 million financing was completed that securitized the future toll revenues from these two highway concessions.

The financing represented a huge breakthrough for the private companies involved in the construction and improvement of infrastructure in developing countries. Consortiums bidding on such projects were dominated by construction companies with limited capital. They needed to remove equity investment and debt from their balance sheets so that they could invest in other projects. The sale of long-term US-dollar-denominated securities supported by Mexican peso-denominated cash flow overcame many difficulties and showed that financings of this nature could be feasible and economically attractive. How was this innovative financing structured to convince investors to make a long-term commitment on the basis of forecasted toll revenues? And how could this technique be used to arrange financing for other highway and facility concession projects in the developing world?

Background

Since 1989, the Mexican Government had sought to promote investment in the construction and improvement of highways by granting concessions to private sector entities. The concessions were of specified duration, granted by the Federal Government or a state government, to build,
operate, and maintain a limited access highway facility. In return, the concessionaire had the right to retain substantially all of the revenues derived from the concessioned facility for the life of the concession. Upon termination of the concession, the right to operate the highway and to collect toll revenues reverts to the government. The highway itself and the equipment related to its operation remain the property of the government throughout the term of the concession.

Each concession sets forth a schedule of tolls by category of vehicle. Most concessions allow concessionaires to increase tolls semi-annually in accordance with the consumer price index. These toll increases may be made without government approval, although supporting documentation must be filed with the Secretariat of Communications and Transport (SCT). Toll increases above the levels set forth in the concession require government approval. In certain cases, the SCT has approved extensions of the term of the concessions to allow the concessionaire to recover its investment. In all cases, the SCT has insisted that a parallel free road must be available for motorists.

As part of this program, the SCT granted a concession to a subsidiary of Tribasa to improve and operate the existing toll road between Ecatepec and Pirámides to the northeast of Mexico (the “Pyramids Toll Road”). The road, a 22.2 kilometer limited access highway that terminates at the pyramids east of Teotihauan, lies in the heavily traveled corridor leading northeast from Mexico City to Tulancingo and the Gulf of Mexico. The original concession started in January 1991 and Tribasa opened the road to traffic in December 1991. Under an addendum to the original concession, Tribasa holds the rights to collect all tolls in connection with the Pyramids concession until December 2011.

The SCT granted a concession to another subsidiary of Tribasa to improve and operate the 37-kilometer toll road between Armería and Manzanillo along a stretch of the Pacific Coast. In December 1992, the SCT extended the term of the concession until November 2004 and added a four lane section on the eastern side of Armería making the total length of the “Manzanillo Toll Road” 47 kilometers.

**Arranging Financing**

In early 1993, Tribasa (acting through its subsidiary concession holders) decided to seek financing in the international capital markets and Salomon Brothers was selected as the underwriter for the transaction. Tribasa’s goal was to remove the infrastructure indebtedness from its balance sheet while retaining control of the roads. It sought a financing structure in which the debt service payments would be secured solely from the future cash flows from the roads and Noteholders would have no recourse to the corporate assets of Tribasa or its subsidiaries.

To facilitate a financing of this nature, Tribasa, sponsored a single purpose Mexican Trust with a Mexican bank as Trustee. Tribasa then transferred its right to collect toll revenue to this trust, along with the investment income the Trust earned on its assets, and any proceeds from insurance policies arranged for the two toll roads. The Notes to be issued would be secured solely from the assets of the Trust and are explicitly not an obligation of Tribasa or its subsidiaries.
II. Financial Security Arrangements

The Trustee entered into an agreement with a third subsidiary of Tribasa to continue as the toll road operator after the sale of the Notes. The operator has the responsibility of running the toll roads, collecting the tolls, paying VAT, maintaining the roads, paying insurance deductibles, and preparing operations and performance reports. The operator was to be paid a management fee equal to 14 percent of the net toll revenues during each calendar month and would take the risk for any costs or expenses in excess of the management fee.

Toll revenues collected by the operator were to be segregated into accounts to ensure that taxes are paid and operating, maintenance and administrative expenses are met before Noteholders received payments of principal or interest. Tribasa was not entitled to receive any dividend distributions from the toll revenues unless funds remain after all of the obligations of the Trust are met. To ensure that toll revenues flow appropriately to meet operating expenses and administrative expenses and pay debt service, the Trustee established and maintained three accounts to hold the Trust’s assets:

1. General Account - a general-purpose account to hold revenues until needed for operating expenses or debt service payments.

2. SCT Account - a segregated account to hold funds for payments that are required to be made to the Transportation Ministry.

3. Major Maintenance Account - a segregated account to ensure that funds are available to make necessary repairs or major maintenance.

A fourth account, the Debt Service Reserve Fund, was established with a US bank as fiscal agent. The debt service reserve holds funds in US dollars, which are available to pay debt service if funds are not available in the General Account to make timely payments of interest or principal. The Debt Service Reserve Fund would be funded with an initial deposit from the proceeds of the Note sale. Thereafter, cash remaining after the payment of operating and administrative expenses would be deposited into the Debt Service Reserve Fund as necessary to maintain an amount equal to the greater of 10 percent of the Notes outstanding or the next scheduled semiannual debt service payment.

Net Toll Revenues equal gross toll revenues less VAT and reserves for required payments to the Transportation Ministry.

Each week, the operator would transfer toll revenues (net of the VAT) to the General Account. Cash received by the Trust was used first to pay certain royalties to the Mexican Transportation Ministry, then taxes and operating expenses related to the roads and finally to make principal and interest payments on the notes. The Trustee withdrew funds in the following order:

Each month:
• funds were deposited into the SCT Account for payment to the Transportation Ministry
• funds were used to pay the Trustee and the US Fiscal Agent, insurance premiums, the Operator’s management fee for the preceding month and other administrative and operating expenses
• funds were set aside for later payment of withholding taxes (so that payments received by Noteholders are free of withholding taxes)
• if necessary, funds were converted to US dollars and transferred to the US Fiscal Agent for deposit into the Debt Service Reserve Fund
• if necessary, funds were deposited into the Major Maintenance Account to maintain the required balance.

Semi-annually:

• funds were transferred to Mexican tax authorities for payment of withholding taxes
• funds were converted to US dollars and transferred to the US Fiscal Agent for payments of principal and interest to Noteholders
• if available and required, funds were converted to US dollars and transferred to the US Fiscal Agent for payment of late payment premiums
• if there is excess cash available, after payment of all of the above, remaining funds were transferred as dividend distributions to Tribasa (subject to certain restrictions described below)

**Debt Service Requirements**

The Notes required interest payments at a rate of 10.5 percent per annum, payable semi-annually beginning June 1, 1994. Failure to make interest payments in accordance with this schedule was an event of default. Principal payments did not begin immediately. The Notes were issued with two amortization schedules, indicating when principal should be repaid. “Contractual Amortization” was the minimum amount of principal that must be paid on or prior to each Debt Payment Date. The Contractual Amortization schedule required principal payments to begin not later than June 1, 1997 and required that the principal of the Notes would be fully repaid by December 1, 2011 (coinciding with the end of the Pyramid Concession). An event of default occurs if the Trust fails to make payments in accordance with this schedule.

The VAT is deducted and paid directly by the Operator to the Mexican government.

Subject to the availability of funds, the Notes required the Trust to make payments in accordance with the more aggressive “Scheduled Amortization” schedule, which starts principal payments a year earlier and results in a final principal payment in December 2005. Failure to meet the Scheduled Amortization Schedule does not result in an event of default, but a Late Penalty Premium accrues at the rate of one percent per annum on the unpaid Scheduled Amortization amounts. In addition, non-payment of Scheduled Amortization is a Blockage Event, which triggers the following restrictions on the actions of Tribasa and the Trust:

1. Dividend payments may not be made to Tribasa
2. The Trust may not issue subordinate debt
3. Payments will not be permitted on any outstanding subordinate debt
These restrictions limit Tribasa’s actions and provide additional means to retain cash flow in the trust. In the more extreme occurrence of default, the Noteholders may declare the principal on the Notes to be immediately due and payable and the Trustee will liquidate the assets of the Trust to satisfy outstanding obligations. If these assets are not sufficient to pay Noteholders in full, as a practical matter, the only remedy available to the Noteholders will be to apply Toll Revenues to the repayment of the Notes if and when they are received by the Trust.

Dividend Distributions

Dividend distributions to Tribasa are not permitted in the first two years after the issuance of the debt. Thereafter, semi-annual dividend distributions are permitted to the extent cash remains under the following circumstances:

1. All payments for operations, maintenance, administration, insurance, and debt service have been made
2. Funds have been set aside for one month’s operating and administrative expenses and for withholding taxes to be paid on the next semi-annual payment date
3. The ratio of net cash flow to scheduled debt meets specified levels

Other Blockage Events that trigger the same restrictions include:

1. Insufficient amounts in the Debt Service Reserve Fund or the Major Maintenance Account
2. Any outstanding Late Payment Premium
3. Bankruptcy (voluntary or involuntary)
4. Breach of the Trust or Operating Agreement
5. The sum of the amounts held in the debt service reserve fund (US Dollars) plus the amounts held in the General Account is at least 25 percent of the outstanding balance of the Notes

Borrowing Capacity

The forecast of potential revenues was a key input to determine the borrowing capacity of a project. For this financing, URS Consultants, an internationally known transportation consulting firm, was engaged to develop and present forecasts of annual toll traffic and annual net revenues to be derived from the two toll road concessions over the period from November 1, 1993 until the end of each concession. The model of the highway’s annual net revenues took into consideration gross toll revenues and maintenance and operating expenses, and the sensitivity of these revenues to changes in economic conditions and travel demand.

The Trust Agreement requires taxes, operating and administrative expenses to be paid from project revenues before debt service. Accordingly, the borrowing capacity is determined by looking at the net revenues available to pay debt service after taxes, operating and administrative expenses are accounted.

Three financial ratios were presented to inform potential investors about the project’s ability to cover the required interest and principal payments:
- Ratio of Revenues Available for Debt Service to Total Debt Service
- Ratio of Net Cash Flow to Total Debt Service
- Ratio of Net Cash Flow plus beginning General Account Balance to Total Debt Service

The second measure was more conservative, since it considered the Net Cash Flow available to pay debt service after the required deposit to the Major Maintenance Account was taken into account.

Revenues Available for Debt Service 61.6
Deposit to Major Maintenance Account -4.6
Net Cash Flow 57.0
Ratio of Net Cash Flow to Total Debt Service (57.0/40.9) 1.46x

The third measure looked beyond the project cash flows to consider the balance in the General Account at the end of each fiscal year. These funds would also be available to pay debt service if there was a shortfall in the operating revenues. For each period, the remaining balance in the General Account was calculated by subtracting the Total Debt Service, Payments to the Debt Service Reserve Fund (as necessary) and Distributions to Tribasa (as permitted) from the Net Cash Flow. This amount was then added to the starting balance in the General Account. For 1994, this would be calculated as follows:

Net Cash Flow 57.0
Interest Payments -38.9
Withholding Tax Payments -2.0
Scheduled Amortization Payments 0
Total Debt Service -40.9
Period Cash Flow 16.2
Payments to Debt Service Reserve Fund -5.9
Distribution to Tribasa 0
Ending General Account Balance 10.3
Ratio of Net Cash Flow plus General Account balance 1.55 x Total Debt Service (57.0+10.3/40.9)

Tribasa provided insurance and administrative expenses. The projections assumed that the principal of the Notes is retired in accordance with the Scheduled Amortization Schedule (see Exhibit 3) and interest is calculated at the rate of 10.5 percent per annum. Contractual Amortization payments, period inflation and the Peso/US Dollar exchange rate are listed for information.

URS also prepared a reduced economic activity scenario with more conservative forecasts of traffic projections and toll revenues. Peso denominated debt service requirements also increase in the alternative case because of the projected depreciation in the Peso. Coverage ratios in the alternative case are 2-3 percent lower than the base case, but the project still meets the Scheduled Amortization schedule (although dividend distributions to Tribasa are delayed by one year).

III. International Best Practice Example of Related Legislation
In the financing of toll roads and other PPP projects in Kenya, and in most emerging economies, it is common practice for international financing consortia to put pressure on Governments to provide cover in the form of sovereign guarantees in their various forms, ranging from “comfort letters” through the acceptance of either explicit or implicit contingent liabilities, counter-guarantees to accompany loans from multilateral development banks, on up to outright sovereign guarantees that place the full faith and credit of government behind a project’s debt repayment obligation.

One way to address this problem is to mitigate the financing risk by using financial security packages, as discussed in this document. However, risk mitigation through the use of financial security measures does not eliminate all of the risks, so the pressure on Governments to provide guarantees, or at least quasi-guarantees, can return. One way to reduce such pressure from international financiers is to take measures to mobilize domestic capital. An increasingly popular mechanism for mobilizing domestic capital is to finance infrastructure PPP projects with domestic bond offerings. There are some good credit enhancement tools available from multilateral development banks and bilateral donors that can be used to improve the ratings on such bonds, thereby reducing the rate of interest that has to be offered in order to sell the bonds. Such bond finance also adds depth to the domestic capital market.

Another way of reducing dependency on foreign capital, and the sovereign guarantees often required by international financiers, is to mobilize domestic capital through the use of Government guaranteed loan programs. Such guarantees reduce the rate of interest and lengthen the tenor of domestic loans, making them competitive with international capital. In the U.S. such Government guaranteed loan programs have been highly successful, such as the ones issued by the Small Business Administration for domestic small and medium sized enterprises, and the ones issued by the Export-Import Bank for U.S. manufacturers of goods destined for foreign markets.

Another highly successful U.S. Government loan guarantee program, one that is not as commonly known overseas but which has been very effective in mobilizing domestic debt capital for transport infrastructure project finance, is the Department of Transportation’s loan guarantee programs made available by the Transport Infrastructure Finance and Innovation Act, provided below. Such legislation can be very effective for mobilizing domestic capital for toll roads project finance. The IP3 consultancy recommends that the Government of Kenya review this document for the purpose of considering similar legislation to mobilize domestic debt capital for toll roads project finance.

**Government Guarantees for Transport Project Finance**

**TEA-21/Transportation Infrastructure Finance and Innovation Act (TIFIA)**

SEC. 1501. SHORT TITLE. <>

This chapter may be cited as the "Transportation Infrastructure Finance and Innovation Act of 1998".

SEC. 1502. FINDINGS. <>
Congress finds that--

(1) a well-developed system of transportation infrastructure is critical to the economic well-being, health, and welfare of the people of the United States;

(2) traditional public funding techniques such as grant programs are unable to keep pace with the infrastructure investment needs of the United States because of budgetary constraints at the Federal, State, and local levels of government;

(3) major transportation infrastructure facilities that address critical national needs, such as intermodal facilities, border crossings, and multistate trade corridors, are of a scale that exceeds the capacity of Federal and State assistance programs in effect on the date of enactment of this Act;

(4) new investment capital can be attracted to infrastructure projects that are capable of generating their own revenue streams through user charges or other dedicated funding sources; and

(5) a Federal credit program for projects of national significance can complement existing funding resources by filling market gaps, thereby leveraging substantial private co-investment.

SEC. 1503. ESTABLISHMENT OF PROGRAM.

(a) In General.--Chapter 1 of title 23, United States Code, is amended by adding at the end the following:

``
SUBCHAPTER II--INFRASTRUCTURE FINANCE

Sec. 181. Definitions

In this subchapter, the following definitions apply:

(1) Eligible project costs.--The term 'eligible project costs' means amounts substantially all of which are paid by, or for the account of, an obligor in connection with a project, including the cost of--

(A) development phase activities, including planning, feasibility analysis, revenue forecasting, environmental review, permitting, preliminary engineering and design work, and other preconstruction activities;

(B) construction, reconstruction, rehabilitation, replacement, and acquisition of real property (including land related to the project and improvements to land),

environmental mitigation, construction contingencies, and acquisition of equipment; and

(C) capitalized interest necessary to meet market requirements, reasonably required reserve funds, capital issuance expenses, and other carrying costs during construction.

(2) Federal credit instrument.--The term 'Federal credit instrument' means a secured loan, loan guarantee, or line of
credit authorized to be made available under this subchapter with respect to a project.

``(3) Investment-grade rating.--The term `investment-grade rating' means a rating category of BBB minus, Baa3, or higher assigned by a rating agency to project obligations offered into the capital markets.
``(4) Lender.--The term `lender' means any non-Federal qualified institutional buyer (as defined in section 230.144A(a) of title 17, Code of Federal Regulations (or any successor regulation), known as Rule 144A(a) of the Securities and Exchange Commission and issued under the Securities Act of 1933 (15 U.S.C. 77a et seq.)), including--
``(A) a qualified retirement plan (as defined in section 4974(c) of the Internal Revenue Code of 1986) that is a qualified institutional buyer; and
``(B) a governmental plan (as defined in section 414(d) of the Internal Revenue Code of 1986) that is a qualified institutional buyer.
``(5) Line of credit.--The term `line of credit' means an agreement entered into by the Secretary with an obligor under section 184 to provide a direct loan at a future date upon the occurrence of certain events.
``(6) Loan guarantee.--The term `loan guarantee' means any guarantee or other pledge by the Secretary to pay all or part of the principal of and interest on a loan or other debt obligation issued by an obligor and funded by a lender.
``(7) Local servicer.--The term `local servicer' means--
``(A) a State infrastructure bank established under this title; or
``(B) a State or local government or any agency of a State or local government that is responsible for servicing a Federal credit instrument on behalf of the Secretary.
``(8) Obligor.--The term `obligor' means a party primarily liable for payment of the principal of or interest on a Federal credit instrument, which party may be a corporation, partnership, joint venture, trust, or governmental entity, agency, or instrumentality.
``(9) Project.--The term `project' means--
``(A) any surface transportation project eligible for Federal assistance under this title or chapter 53 of title 49;
``(B) a project for an international bridge or tunnel for which an international entity authorized under Federal or State law is responsible.
``(C) a project for intercity passenger bus or rail facilities and vehicles, including facilities and vehicles owned by the National Railroad Passenger Corporation and components of magnetic levitation transportation systems; and
``(D) a project for publicly owned intermodal surface freight transfer facilities, other than seaports and airports, if the facilities are located on or adjacent to National Highway System routes or

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connections to the National Highway System.

(10) Project obligation.--The term 'project obligation' means any note, bond, debenture, or other debt obligation issued by an obligor in connection with the financing of a project, other than a Federal credit instrument.

(11) Rating agency.--The term 'rating agency' means a bond rating agency identified by the Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization.

(12) Secured loan.--The term 'secured loan' means a direct loan or other debt obligation issued by an obligor and funded by the Secretary in connection with the financing of a project under section 183.

(13) State.--The term 'State' has the meaning given the term in section 101.

(14) Subsidy amount.--The term 'subsidy amount' means the amount of budget authority sufficient to cover the estimated long-term cost to the Federal Government of a Federal credit instrument, calculated on a net present value basis, excluding administrative costs and any incidental effects on governmental receipts or outlays in accordance with the provisions of the Federal Credit Reform Act of 1990 (2 U.S.C. 661 et seq.).

(15) Substantial completion.--The term 'substantial completion' means the opening of a project to vehicular or passenger traffic.

Sec. 182. Determination of eligibility and project selection

(a) Eligibility.--To be eligible to receive financial assistance under this subchapter, a project shall meet the following criteria:

(i) Inclusion in transportation plans and programs.--The project--

(A) shall be included in the State transportation plan required under section 135; and

(B) at such time as an agreement to make available a Federal credit instrument is entered into under this subchapter, shall be included in the approved State transportation improvement program required under section 134.

(2) Application.--A State, a local servicer identified under section 185(a), or the entity undertaking the project shall submit a project application to the Secretary.

(3) Eligible project costs.--

(A) In general.--Except as provided in subparagraph (B), to be eligible for assistance under this subchapter, a project shall have eligible project costs that are reasonably anticipated to equal or exceed the lesser of--

(i) $100,000,000; or

(ii) 50 percent of the amount of Federal highway assistance funds apportioned for the most recently completed fiscal year to the State in which the project is located.

(B) Intelligent transportation system projects.--In the case of a project principally involving the installation
of an intelligent transportation system, eligible project costs shall be reasonably anticipated to equal or exceed $30,000,000.

``(4) Dedicated revenue sources.--Project financing shall be repayable, in whole or in part, from tolls, user fees, or other dedicated revenue sources.
``(5) Public sponsorship of private entities.--In the case of a project that is undertaken by an entity that is not a State or local government or an agency or instrumentality of a State or local government, the project that the entity is undertaking shall be publicly sponsored as provided in paragraphs (1) and (2).

``(b) Selection Among Eligible Projects.--
``(1) Establishment.--The Secretary shall establish criteria for selecting among projects that meet the eligibility criteria specified in subsection (a).
``(2) Selection criteria.--
``(A) In general.--The selection criteria shall include the following:
``(i) The extent to which the project is nationally or regionally significant, in terms of generating economic benefits, supporting international commerce, or otherwise enhancing the national transportation system.
``(ii) The creditworthiness of the project, including a determination by the Secretary that any financing for the project has appropriate security features, such as a rate covenant, to ensure repayment.
``(iii) The extent to which assistance under this subchapter would foster innovative public-private partnerships and attract private debt or equity investment.
``(iv) The likelihood that assistance under this subchapter would enable the project to proceed at an earlier date than the project would otherwise be able to proceed.
``(v) The extent to which the project uses new technologies, including intelligent transportation systems, that enhance the efficiency of the project.
``(vi) The amount of budget authority required to fund the Federal credit instrument made available under this subchapter.
``(vii) The extent to which the project helps maintain or protect the environment.
``(viii) The extent to which assistance under this chapter would reduce the contribution of Federal grant assistance to the project.
``(B) Preliminary rating opinion letter.--For purposes of subparagraph (A)(ii), the Secretary shall require each project applicant to provide a preliminary rating opinion letter from at least 1 rating agency indicating that the project's senior obligations have
the potential to achieve an investment-grade rating.

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(c) Federal Requirements.--In addition to the requirements of this title for highway projects, chapter 53 of title 49 for transit projects, and section 5333(a) of title 49 for rail projects, the following provisions of law shall apply to funds made available under this subchapter and projects assisted with the funds:
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```(1) Title VI of the Civil Rights Act of 1964 (42 U.S.C. 2000d et seq.).
(3) The Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (42 U.S.C. 4601 et seq.).
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Sec. 183. Secured loans
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(a) In General.--
(1) Agreements.--Subject to paragraphs (2) through (4), the Secretary may enter into agreements with 1 or more obligors to make secured loans, the proceeds of which shall be used--
(A) to finance eligible project costs; or
(B) to refinance interim construction financing of eligible project costs;
(2) Limitation on refinancing of interim construction financing.--A loan under paragraph (1) shall not refinance interim construction financing under paragraph (1)(B) later than 1 year after the date of substantial completion of the project.
(3) Risk assessment.--Before entering into an agreement under this subsection, the Secretary, in consultation with the Director of the Office of Management and Budget and each rating agency providing a preliminary rating opinion letter under section 182(b)(2)(B), shall determine an appropriate capital reserve subsidy amount for each secured loan, taking into account such letter.
(4) Investment-grade rating requirement.--The funding of a secured loan under this section shall be contingent on the project's senior obligations receiving an investment-grade rating, except that--
(A) the Secretary may fund an amount of the secured loan not to exceed the capital reserve subsidy amount determined under paragraph (3) prior to the obligations receiving an investment-grade rating; and
(B) the Secretary may fund the remaining portion of the secured loan only after the obligations have received an investment-grade rating by at least 1 rating agency.
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(b) Terms and Limitations.--
(1) In general.--A secured loan under this section with respect to a project shall be on such terms and conditions and contain such covenants, representations, warranties, and requirements (including requirements for audits) as the Secretary determines appropriate.
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(2) Maximum amount.--The amount of the secured loan shall not exceed 33 percent of the reasonably anticipated eligible project costs.

(3) Payment.--The secured loan shall--

\( (i) \) be payable, in whole or in part, from tolls, user fees, or other dedicated revenue sources; and

\( (ii) \) include a rate covenant, coverage requirement, or similar security feature supporting the project obligations; and

(4) Interest rate.--The interest rate on the secured loan shall be not less than the yield on marketable United States Treasury securities of a similar maturity to the maturity of the secured loan on the date of execution of the loan agreement.

(5) Maturity date.--The final maturity date of the secured loan shall be not later than 35 years after the date of substantial completion of the project.

(6) Nonsubordination.--The secured loan shall not be subordinated to the claims of any holder of project obligations in the event of bankruptcy, insolvency, or liquidation of the obligor.

(7) Fees.--The Secretary may establish fees at a level sufficient to cover all or a portion of the costs to the Federal Government of making a secured loan under this section.

(8) Non-federal share.--The proceeds of a secured loan under this subchapter may be used for any non-Federal share of project costs required under this title or chapter 53 of title 49, if the loan is repayable from non-Federal funds.

(c) Repayment.--

\( (1) \) Schedule.--The Secretary shall establish a repayment schedule for each secured loan under this section based on the projected cash flow from project revenues and other repayment sources.

\( (2) \) Commencement.--Scheduled loan repayments of principal or interest on a secured loan under this section shall commence not later than 5 years after the date of substantial completion of the project.

\( (3) \) Sources of repayment funds.--The sources of funds for scheduled loan repayments under this section shall include tolls, user fees, or other dedicated revenue sources.

\( (4) \) Deferred payments.--

\( (A) \) Authorization.--If, at any time during the 10 years after the date of substantial completion of the project, the project is unable to generate sufficient revenues to pay the scheduled loan repayments of principal and interest on the secured loan, the Secretary may, subject to subparagraph (C), allow the obligor to add unpaid principal and interest to the outstanding balance of the secured loan.
``(B) Interest.--Any payment deferred under subparagraph (A) shall--
``(i) continue to accrue interest in accordance with subsection (b)(4) until fully repaid; and
``(ii) be scheduled to be amortized over the remaining term of the loan beginning not later than 10 years after the date of substantial completion of the project in accordance with paragraph (1).
``(C) Criteria.--
``(i) In general.--Any payment deferral under subparagraph (A) shall be contingent on the project meeting criteria established by the Secretary.
``(ii) Repayment standards.--The criteria established under clause (i) shall include standards for reasonable assurance of repayment.
``(5) Prepayment.--

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``(A) Use of excess revenues.--Any excess revenues that remain after satisfying scheduled debt service requirements on the project obligations and secured loan and all deposit requirements under the terms of any trust agreement, bond resolution, or similar agreement securing project obligations may be applied annually to prepay the secured loan without penalty.
``(B) Use of proceeds of refinancing.--The secured loan may be prepaid at any time without penalty from the proceeds of refinancing from non-Federal funding sources.

``(d) Sale of Secured Loans.--
``(1) In general.--Subject to paragraph (2), as soon as practicable after substantial completion of a project and after notifying the obligor, the Secretary may sell to another entity or reoffer into the capital markets a secured loan for the project if the Secretary determines that the sale or reoffering can be made on favorable terms.
``(2) Consent of obligor.--In making a sale or reoffering under paragraph (1), the Secretary may not change the original terms and conditions of the secured loan without the written consent of the obligor.

``(e) Loan Guarantees.--
``(1) In general.--The Secretary may provide a loan guarantee to a lender in lieu of making a secured loan if the Secretary determines that the budgetary cost of the loan guarantee is substantially the same as that of a secured loan.
``(2) Terms.--The terms of a guaranteed loan shall be consistent with the terms set forth in this section for a secured loan, except that the rate on the guaranteed loan and any prepayment features shall be negotiated between the obligor and the lender, with the consent of the Secretary.
Sec. 184. Lines of credit

(a) In General.--

(1) Agreements.--Subject to paragraphs (2) through (4), the Secretary may enter into agreements to make available lines of credit to 1 or more obligors in the form of direct loans to be made by the Secretary at future dates on the occurrence of certain events for any project selected under section 182.

(2) Use of proceeds.--The proceeds of a line of credit made available under this section shall be available to pay debt service on project obligations issued to finance eligible project costs, extraordinary repair and replacement costs, operation and maintenance expenses, and costs associated with unexpected Federal or State environmental restrictions.

(3) Risk assessment.--Before entering into an agreement under this subsection, the Secretary, in consultation with the Director of the Office of Management and Budget and each rating agency providing a preliminary rating opinion letter under section 182(b)(2)(B), shall determine an appropriate capital reserve subsidy amount for each line of credit, taking into account such letter.

(4) Investment-grade rating requirement.--The funding of a line of credit under this section shall be contingent on the project's senior obligations receiving an investment-grade rating from at least 1 rating agency.

(b) Terms and Limitations.--

(1) In general.--A line of credit under this section with respect to a project shall be on such terms and conditions and contain such covenants, representations, warranties, and requirements (including requirements for audits) as the Secretary determines appropriate.

(2) Maximum amounts.--

(A) Total amount.--The total amount of the line of credit shall not exceed 33 percent of the reasonably anticipated eligible project costs.

(B) 1-year draws.--The amount drawn in any 1 year shall not exceed 20 percent of the total amount of the line of credit.

(3) Draws.--Any draw on the line of credit shall represent a direct loan and shall be made only if net revenues from the project (including capitalized interest, any debt service reserve fund, and any other available reserve) are insufficient to pay the costs specified in subsection (a)(2).

(4) Interest rate.--The interest rate on a direct loan resulting from a draw on the line of credit shall be not less than the yield on 30-year marketable United States Treasury securities as of the date on which the line of credit is obligated.

(5) Security.--The line of credit--

(A) shall--

(i) be payable, in whole or in part, from tolls, user fees, or other dedicated revenue sources; and
(ii) include a rate covenant, coverage requirement, or similar security feature supporting the project obligations; and
(B) may have a lien on revenues described in subparagraph (A) subject to any lien securing project obligations.
(6) Period of availability.--The line of credit shall be available during the period beginning on the date of substantial completion of the project and ending not later than 10 years after that date.
(7) Rights of third-party creditors.--
(A) Against federal government.--A third-party creditor of the obligor shall not have any right against the Federal Government with respect to any draw on the line of credit.
(B) Assignment.--An obligor may assign the line of credit to 1 or more lenders or to a trustee on the lenders' behalf.
(8) Nonsubordination.--A direct loan under this section shall not be subordinated to the claims of any holder of project obligations in the event of bankruptcy, insolvency, or liquidation of the obligor.
(9) Fees.--The Secretary may establish fees at a level sufficient to cover all or a portion of the costs to the Federal Government of providing a line of credit under this section.
(10) Relationship to other credit instruments.--A project that receives a line of credit under this section also shall not receive a secured loan or loan guarantee under section 183 of an amount that, combined with the amount of the line of credit, exceeds 33 percent of eligible project costs.

(c) Repayment.--
(1) Terms and conditions.--The Secretary shall establish repayment terms and conditions for each direct loan under this section based on the projected cash flow from project revenues and other repayment sources.
(2) Timing.--All scheduled repayments of principal or interest on a direct loan under this section shall commence not later than 5 years after the end of the period of availability specified in subsection (b)(6) and be fully repaid, with interest, by the date that is 25 years after the end of the period of availability specified in subsection (b)(6).
(3) Sources of repayment funds.--The sources of funds for scheduled loan repayments under this section shall include tolls, user fees, or other dedicated revenue sources.

Sec. 185. Project servicing

(a) Requirement.--The State in which a project that receives financial assistance under this subchapter is located may identify a local servicer to assist the Secretary in servicing the Federal credit instrument made available under this subchapter.
(b) Agency; Fees.--If a State identifies a local servicer under subsection (a), the local servicer--
(1) shall act as the agent for the Secretary; and
(2) may receive a servicing fee, subject to approval by the Secretary.

(c) Liability.--A local servicer identified under subsection (a) shall not be liable for the obligations of the obligor to the Secretary or any lender.

(d) Assistance From Expert Firms.--The Secretary may retain the services of expert firms in the field of municipal and project finance to assist in the underwriting and servicing of Federal credit instruments.

Sec. 186. State and local permits

The provision of financial assistance under this subchapter with respect to a project shall not--

(1) relieve any recipient of the assistance of any obligation to obtain any required State or local permit or approval with respect to the project;

(2) limit the right of any unit of State or local government to approve or regulate any rate of return on private equity invested in the project; or

(3) otherwise supersede any State or local law (including any regulation) applicable to the construction or operation of the project.

Sec. 187. Regulations

The Secretary may issue such regulations as the Secretary determines appropriate to carry out this subchapter.

Sec. 188. Funding

(a) Funding.--

(1) In general.--There are authorized to be appropriated from the Highway Trust Fund (other than the Mass Transit Account) to carry out this subchapter--

(A) $80,000,000 for fiscal year 1999;

(B) $90,000,000 for fiscal year 2000;

(C) $110,000,000 for fiscal year 2001;

(D) $120,000,000 for fiscal year 2002; and

(E) $130,000,000 for fiscal year 2003.

(2) Administrative costs.--From funds made available under paragraph (1), the Secretary may use, for the administration of this subchapter, not more than $2,000,000 for each of fiscal years 1998 through 2003.

(3) Availability.--Amounts made available under paragraph (1) shall remain available until expended.

(b) Contract Authority.--

(1) In general.--Notwithstanding any other provision of law, approval by the Secretary of a Federal credit instrument that uses funds made available under this subchapter shall be deemed to be acceptance by the United States of a contractual obligation to fund the Federal credit instrument.
(2) Availability.--Amounts authorized under this section for a fiscal year shall be available for obligation on October 1 of the fiscal year.

(c) Limitations on Credit Amounts.--For each of fiscal years 1998 through 2003, principal amounts of Federal credit instruments made available under this subchapter shall be limited to the amounts specified in the following table:

<table>
<thead>
<tr>
<th>Fiscal year</th>
<th>Maximum amount of credit</th>
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</thead>
<tbody>
<tr>
<td>1998</td>
<td>$1,200,000,000</td>
</tr>
<tr>
<td>1999</td>
<td>$1,200,000,000</td>
</tr>
<tr>
<td>2000</td>
<td>$1,800,000,000</td>
</tr>
<tr>
<td>2001</td>
<td>$1,800,000,000</td>
</tr>
<tr>
<td>2002</td>
<td>$2,300,000,000</td>
</tr>
<tr>
<td>2003</td>
<td>$2,300,000,000</td>
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Sec. 189. Report to Congress

Not later than 4 years after the date of enactment of this subchapter, the Secretary shall submit to Congress a report summarizing the financial performance of the projects that are receiving, or have received, assistance under this subchapter, including a recommendation as to whether the objectives of this subchapter are best served--

(1) by continuing the program under the authority of the Secretary;

(2) by establishing a Government corporation or Government-sponsored enterprise to administer the program; or

(3) by phasing out the program and relying on the capital markets to fund the types of infrastructure investments assisted by this subchapter without Federal participation.''

(b) Conforming Amendments.--Chapter 1 of title 23, United States Code, is amended--

(1) in the analysis--

(A) by inserting before `Sec.' the following:

``SUBCHAPTER I--GENERAL PROVISIONS'';

and

(B) by adding at the end the following:

``SUBCHAPTER II--INFRASTRUCTURE FINANCE

181. Definitions.
182. Determination of eligibility and project selection.
183. Secured loans.
184. Lines of credit.
185. Project servicing.

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186. State and local permits.
187. Regulations.
188. Funding.
189. Report to Congress.'';
and
(2) by inserting before section 101 the following:
``SUBCHAPTER I--GENERAL PROVISIONS''.

SEC. 1504. DUTIES OF THE SECRETARY.

Section 301 of title 49, United States Code, is amended--
(1) in paragraph (7) by striking ``and'' at the end;
(2) in paragraph (8) by striking the period at the end and
inserting `; and''; and
(3) by adding at the end the following:
``(9) develop and coordinate Federal policy on financing
transportation infrastructure, including the provision of direct
Federal credit assistance and other techniques used to leverage
Federal transportation funds.''.

A-80
Appendix 8. Position Descriptions for Start-Up Phase PPP Secretariat

1. Head of PPP Secretariat

<table>
<thead>
<tr>
<th>Personal Specification</th>
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<tr>
<td><strong>Position</strong></td>
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<td><strong>Education</strong></td>
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<tr>
<td><strong>Experience</strong></td>
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<tr>
<td><strong>Personality</strong></td>
</tr>
<tr>
<td><strong>Circumstances</strong></td>
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</tbody>
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<tr>
<th>Job Description</th>
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<tbody>
<tr>
<td><strong>Job Title</strong></td>
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<tr>
<td><strong>Reports to</strong></td>
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<tr>
<td><strong>Staff Responsibility</strong></td>
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<tr>
<td><strong>Main Purpose of Position</strong></td>
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<td></td>
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<tr>
<td><strong>Criteria of Success</strong></td>
</tr>
<tr>
<td><strong>Key Tasks</strong></td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>
Regulatory duties. To support the PPP Unit in the development of operational policies for the day to day working. To oversee the implementation of policy decisions and review progress against agreed time-scales.

**Criteria of Success**  
The National PPP Unit staff and the stakeholders are satisfied with the progress of PPP project implementation against agreed time-scales.

**Accountability**  
There are PPP regulations and guidelines implementation plans in place. PPP projects follow the regulatory guideline issued by the PPP Unit.

2. **Work Planning**  
The development of up to date PPP Work Plan with time scales for deliverables within 3, 6, 9, & 12 months for the Unit. To develop a planning process that involves staff in the formulation of ideas for implementation. Facilitate and resource ad hoc request within the National PPP Units mandate.

**Criteria of Success**  
The 12-month Work Plan reflects the plans of the National PPP Units staffing levels and the stakeholders' basic expectations.

**Accountability**  
There are monthly PPP planning meetings scheduled. The PPP project plans and timetables are published and slippages highlighted monthly. These are at least quarterly project and strategy reviews are undertaken with your staff and the MOF. Changes are reflected in the quarterly review.

3. **Communications with Stakeholders**  
Provide consistent communication with PPP stakeholders on the work of the PPP Unit. Communication should set out the strategies to ensure appropriate infrastructure projects are selected. Undertake a communication program on the benefits of PPP role in the community, with the development of a public awareness campaign and education programs.

**Criteria of Success**  
Staffs have clear work goals and objectives pursued in a coordinated and motivated manner. Externally there is a positive view of the work of the PPP Unit and the Government's economic PPP development policies.

**Accountability**  
Communications are review quarterly.

4. **PPP Unit Resource Management**

   a) **Internal Resources**  
   To identify and recruit and develop staff necessary to meet the National PPP Units up-dated Work Plans.

   **Criteria of Success**  
   Sufficient staffs are in place with the requisite skills.

   b) **Budget Management**  
   To ensure a sustainable budget is set for each year that meets the National PPP Units plans for each core PPP Project activity.

   **Criteria of Success**
Costs are less than or equal to budget.

**Accountability (a) and (b)** There are monthly and quarterly planning and budget reports that reflect the provision of adequate resources to meet the PPP Units needs.

5. **Transparency & Governance**
Ensure that the transparency and quality of PPP approach follows best international governance practices. The integrity of the National PPP Unit is beyond question, staff and procedures of services of the PPP procurement set down by Public procurement Oversight & Advisory Board (PPOAB) and general procurement legal requirements.

- **Criteria of Success**
  The manner National PPP Unit communicated its responsibilities by providing information on it’s governance and PPP procurement approach.

- **Accountability**
  Report on good governance and PPP procurement compliance for each PPP project undertaken, including financial commitments undertaking to the MOF quarterly.

6. **Performance, Training & Development**
A performance planning review system and competency tools are applied and set out in the procedures for all staffs involved in PPP transactions, both within the National PPP Unit and PPP Nodes. Short falls in PPP performance are addressed through the appropriate development programmes. Planned and clearly identified PPP training and development programmes are in place. A series of ‘in-house’ PPP programmes are identified to build common competencies with core support staff.

- **Criteria of Success**
  Performance measures are met or exceeded and deficiencies are resolved. All performance exceptions are being positively brought to a conclusion. Training and development plans are identified for all personnel involved in PPP transactions.

- **Accountability**
  Six monthly PPP transaction reviews are undertaken with all PPP Project staff. PPP Training Plans are implemented to meet development needs.
2. PPP Projects Transaction Coordinator

**Personal Specification**

<table>
<thead>
<tr>
<th>Position</th>
<th>PPP Projects Transaction Coordinator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>A post graduate qualification in economics and or accounting, additional qualification in technical related areas for utility position would be an advantage. He/she must have proven communication, report written and oral presentation skills.</td>
</tr>
<tr>
<td>Experience</td>
<td>He or she has worked at a senior level within the private sector in a related industry. Having lead private and public sector transaction to successful negotiation and conclusion would be essential perquisite for the position. As a Project Coordinator, he/she will expected to have had a broad commercial management experiences with the capacity to contribute to the overall organisation issues, including policies, strategies and management issues. He/she must have experience of leading a high level professional project tasks, with minimum 10 years work experience within a related industry sector environment. He/she must have a proven record in achieving results in a business environment to support sensitive commercial transactions. In addition must be capable of applying strict project ‘project management’ and or related IT project management support systems to the all the transactions allocated to him or her.</td>
</tr>
<tr>
<td>Personality</td>
<td>Must have a natural ability to meet and work with people. He / she should be both people orientated while having a strong technical understanding. Excellent report writing and communication skills will be essential.</td>
</tr>
<tr>
<td>Circumstances</td>
<td>Prepared to accept a fixed-term contract.</td>
</tr>
</tbody>
</table>

**Job Description**

<table>
<thead>
<tr>
<th>Job Title</th>
<th>PPP Projects Transactions Coordinator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reports to</td>
<td>Head of PPP Secretariat</td>
</tr>
<tr>
<td>Responsibility</td>
<td>PPP Project Transactions</td>
</tr>
<tr>
<td>Main Purpose of Position</td>
<td>To support the PPP Unit policies, work programmes and ensure project sponsors have sufficient regulatory guidelines and procedures to meet their PPP Projects work plans.</td>
</tr>
</tbody>
</table>
| Criteria of Success         | 1. **Project Feasibility Work Planning**: weekly, monthly and annual with line ministries and investors  
                              | 2. **Project Resource Management**: internal personnel, external consulting resources (procurement) and feasibility budgets  
                              | 3. **Project Approvals**: securing MOF approvals for each stage of the feasibility study  
                              | 4. **Project ‘due diligence’ & PPP compliance Information**  
                              | 5. **Management Information Systems (MIS) & Communications** |
| Key Tasks                   | In the job outline below recognises there are two dimensions to the Transaction Coordinator of PPP Projects role. **First**: is the ‘external’ management of PPP transactions with line ministries, state agencies and SOEs etc; supporting PPP Projects and appointing external consultants where necessary. **Second**: provide accuracy of information to all stakeholders on the PPP project team on best practice, ensuring the transactions are conducted in an open and transparent manner, complying with PPP procurement requirements |
                                  | There are three central components to the PPP Projects Transaction Coordinator role: |
• **Conduct and Manage Feasibility Studies** e.g. to assess project potential, affordability, value for money and risk transfer

• **Managing the ‘due diligence’ of PPP** e.g. Share holdings, labour& employment issues; land and property ownership; legal authority to undertake PPP transaction; common PPP enterprise marketing information for PPP transactions to secure investment; due diligence at each stage of the PPP feasibility approvals and negotiation. (Excluding due diligence for Private Sector stakeholders)

• **PPP project management procedures** e.g. information systems to monitor internal & external PPP project components.

This is a board job outline addressing 5 key areas for the role of this role in Coordination PPP Projects, these are:

1. **Project Feasibility Work Planning**; weekly, monthly and annual with line ministries and investors
2. **Project Resource Management**; internal personnel, external consulting resources (procurement) and feasibility budgets
3. **Project Approvals**; securing MOF approvals for each stage of the feasibility study
4. **Project ‘due diligence’ & PPP compliance Information**
5. **Management Information Systems (MIS) & Communications**

We set out below the general description of these five activities, including when you will be considered successful and how you will be accountable.

1. **Project Feasibility Work Planning**
   The **Project Feasibility Work Planning** for public private partnerships (PPP) is articulated in the PPP Units annual work plans. There are details for all current projects identifying resource requirements and timelines for the successful delivery of stakeholder (line ministries etc and potential investors) requirements, with the additional capacity to facilitate ad hoc requests.

   **Criteria of Success**: Plans are identified meeting stakeholder requirements with solutions put in place and articulated in the National PPP Units annual work plan.

   **Accountability**: Monthly progress monitoring and work planning meetings scheduled and quarterly performance reviews are undertaken for each PPP project.

2. **Project Resource Management**
   a) **Internal Staffing Resources**
   Identify the staff and consulting resources necessary to meet the current work plans for transactions over which you have responsibility in conjunction with the project sponsor.

   **Criteria of Success**: That sufficient staff and consulting resources with the requisite skills are in place to complete all the PPP feasibility stages.

   b) **Budget Management**
   To set in conjunction with the Head of PPP Unit and the external sponsor a sustainable Budget for each project that meets the delivery of work plans.
3. Project Approvals
To set in place the necessary operational structures and procedures to ensure that the organisation meets its Ministry of Finance (MOF) approval objectives and or the Project Development Facility (PDF) for each stage of the feasibility study. There are accurate and timely reports with quality standards for PPP transaction. There is one common standard project management system operating across all project portfolios.

Criteria of Success: PPP Feasibility Approval quality standards are met in the presentation of Reports. Project Data is accurate, timely and well presented to enable decisions to make. That decisions are clearly communicated and accepted by those directly delivering on project deadlines.

Accountability: PPP Feasibility studies are conducted to a quality standard. There are operating manual and IT systems and procedures including cross-organisational quality 'files' maintenance standards in place, with key personnel trained to operate the system effectively. This is supported by holding bi-monthly project staff communication and problem solving meetings. Outcomes are reviewed at transactions meetings at least quarterly.

4. Project Transaction ‘due diligence’
To comply with international, legal, Government, Donor and National PPP Unit procedure in respect to due diligence for each PPP transaction. Maintaining of accurate records, providing timely information to meet fixed reporting deadlines for each transaction under your management. PPP procurement procedures are followed and process for PPP transaction to follow to ensure due diligence, in respect to the legality of the project at each stage of its MOF Approval(s) and or the PDF. Your full co-operation and responsiveness will be important to support ‘transparency and integrity’ of the transaction process.

Criteria of Success
All monitoring reports are favourable on each transaction due diligence audit.

Accountability
There are monthly/quarterly due diligence standard reports completed for all transactions.

5. PPP Project Management Information Systems
The Project management information systems are standardise and utilised for all projects across the PPP Unit providing timely and accurate information to project teams and stakeholders e.g.

- Critical information is posted to the ‘intra-net’ in secure files, including reports made available for each project to the Director of Procurement &
<table>
<thead>
<tr>
<th>Contract Compliance</th>
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</thead>
<tbody>
<tr>
<td>• Financial reports are submitted to the MOF and risk management is assessed for each project</td>
</tr>
<tr>
<td>• MOF and or PDF Approvals scheduled, recorded and acted upon</td>
</tr>
<tr>
<td>• Timely reports to project sponsors, stakeholders &amp; donors</td>
</tr>
</tbody>
</table>

**Criteria of Success**

Project management information system and communication are accurate and up to date.

**Accountability**

Project management information system and communication are reviewed monthly.
3. Legal / Contracts Specialist

### Personal Specification

<table>
<thead>
<tr>
<th>Position</th>
<th>Legal / Contracts Specialist</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education</td>
<td>A qualification in Law is essential and a post-graduate qualification in management, administration and/or accounting would be an advantage.</td>
</tr>
<tr>
<td>Experience</td>
<td>He or she has worked at a senior level within the public or private sector in a related activity. Having lead private and public sector transaction to successful negotiation and conclusion would be essential perquisite for the position.</td>
</tr>
<tr>
<td></td>
<td>He/she will be expected to have had a broad commercial management experiences with the capacity to contribute to the overall organisation issues, including policies, strategies with minimum 10 years work experience within a legal contracting work environment.</td>
</tr>
<tr>
<td></td>
<td>He/she must have a proven record in achieving results in a business to negotiate sensitive commercial transactions. In addition must be capable of applying strict project ‘project management’ would be highly desirable.</td>
</tr>
<tr>
<td></td>
<td>Experience of working with a large utility <em>e.g.</em> energy, transport, communications &amp; water or commercial banking would be an added advantage. Experience of contracting consultant and working with Donors would also be an advantage, in addition; an understanding of Government organisations and working.</td>
</tr>
<tr>
<td></td>
<td>He/she must have proven communication, report written and oral presentation skills.</td>
</tr>
<tr>
<td>Personality</td>
<td>Must have a natural ability to meet and work with people. He/she should be both people orientated while having a strong legal and procurement technical understanding. Excellent report writing and communication skills will be essential.</td>
</tr>
<tr>
<td>Circumstances</td>
<td>Prepared to accept a fixed-term contract.</td>
</tr>
</tbody>
</table>

### Job Description

<table>
<thead>
<tr>
<th>Job Title</th>
<th>Legal / Contracts Specialist</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reports to</td>
<td>Head of Secretariat</td>
</tr>
<tr>
<td>Responsibility</td>
<td>Legal contacts, PPP procurement procedures and PPP Project compliance</td>
</tr>
<tr>
<td>Main Purpose of Position</td>
<td>To ensure that PPP Transactions are planned and implemented in a manner that is consistent PPP law, PDF requirements and National PPP regulations guidelines, including best international practice, good governance and Kenya general procurement laws.</td>
</tr>
<tr>
<td>Criteria of Success</td>
<td>There are no issues that cast doubts over the probity of a PPP Transaction, in whole or in part.</td>
</tr>
<tr>
<td>Accountability</td>
<td>All stakeholders including political opponents and the media are able to legitimately report that international best PPP procurement and contract compliance practices have been complied with by the National PPP Unit</td>
</tr>
<tr>
<td>Key Tasks</td>
<td>1. <strong>PPP Procurement &amp; Pre-Contract Compliance of PPP Transactions</strong></td>
</tr>
<tr>
<td></td>
<td>At the outset of a PPP Transaction; to understand and approve the probity issues contained therein.</td>
</tr>
<tr>
<td></td>
<td><strong>Criteria of Success</strong></td>
</tr>
<tr>
<td></td>
<td>That all PPP Transactions have, at the outset, PPP procurement and monitoring and compliance plan that is approved by the Acting Head of Secretariat for the MOF.</td>
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<tr>
<td></td>
<td><strong>Accountability</strong></td>
</tr>
</tbody>
</table>
|                 | Reports from LCS will provided to the Acting Head of Secretariat, plus all
exception reports to the internal PDF Committee and the Public Procurement Oversight Authority (PPOA) monthly.

2. Procurement and Contract Compliant Procedures
The LCS will set up all PPP procurement procedure specifications and standard which meet the Kenya law, PPOA standards and international World Bank guidelines for all PPP Secretariat transactions. The reporting and highlighting of any deviations will be handled in open and transparent manner reporting outside of the National PPP Secretariat.

Criteria of Success
All procedures are in place and meet Kenya law, PPOA standards and international WB procurement guidelines for all National PPP Unit transactions.

Accountability
There is continuous review of best practice and the National PPP Unit it see as taking a pro-active role in publishing guidelines bi-annually to meet the required standards.

3. Ongoing Probity Advice
During the course of PPP Transactions the LCS will be available to the PPP Transaction personnel to provide and advices on issue that have arisen but were not contemplated or dealt with at the time of the initial PPP Transaction plan.

Criteria of Success
That unplanned PPP procurement and contract compliance issues to be professionally dealt with as and when they arise.

Accountability
Reports from LCS provided to the Acting Head of Secretariat and the MOF with corrective actions taken on a monthly

4. PPP Procurement & Contract Compliance Sign Off
PPP Procurement & Contract Compliance procedure and processes will be reviewed on the completion of each PPP Transaction and formally reported on by the LCS. Items of concern / inconsistencies with either the original plan or any interim advices will be reported on by the LCS.

Criteria of Success
All PPP contracting partiers and external stakeholders will be aware of the entire probity process and the penalties associated with any violation.

Accountability
The MOF are aware of those Transactions that are satisfactorily signed off and those for which special reports have been submitted by the LCS in his/ her monthly report.

5. Links and follow up with Internal Audit
The LCS establishing strong links with the work government own audit standards to ensure his/ her actions are consistent with their practices, while seeking continuous improvements.

Criteria of Success
There is a plan of action agreed to meet best practice standards with MOF.
### Accountability
Review reports of activities are presented at least quarterly to MOF and PPP Stakeholders.

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**4. Finance and Administration Manager**

<table>
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<tr>
<th><strong>Personal Specification</strong></th>
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<tr>
<td><strong>Position</strong></td>
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<td><strong>Education</strong></td>
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<td><strong>Job Title</strong></td>
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<td><strong>Reports to</strong></td>
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<tr>
<td><strong>Responsibility</strong></td>
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<tr>
<td><strong>Main Purpose of Position</strong></td>
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<tr>
<td><strong>Criteria of Success</strong></td>
</tr>
<tr>
<td><strong>Key Tasks</strong></td>
</tr>
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</table>

Provide the National PPP Unit and its related institutions with the critical management performance and financial information in a reliable and timely manner. Establish the necessary operational decision making structures and procedures to ensure the MIS is an effect working document and report mechanism.

**Criteria of Success**
The PPP Unit Staff and MOF are satisfied with the management information and the financial information that is provided to it, with emphasis on PPP transactions.

**Accountability**
There is a monthly and quarterly review of financial performance against control budget and PPP transaction business plan. The
information provided is credible and consistent with the annual audited financial statements to the MOF.

2. Financial Statements

Provide Monthly, Quarterly and Annual financial statements for audit in a reliable and timely manner. Support the MOF in setting up the PDF.

Criteria of Success
Annual financial statements are presented for audit within three months of the financial year-end. The auditors’ report is not qualified in any way.

Accountability
All stakeholders acknowledge that all financial information that emanates from PPP Unit is both timely and reliable.

3. Project Financial Assessment

Provide when required Financial Assessment in a reliable and timely manner, when requested to do so by the PDF, MOF and the PPP unit.

Criteria of Success
Provide Assessment overview reports that meet PPP Feasibility standards

Accountability
The Risk Management unit in the MOF accept you assessment as part of their overall risk evaluation.

4. Financial Standards & Controls

Suitable procedures, controls and systems are in place to ensure that all PPP Transactions (historical and future) are accounted for in a manner that is consistent with the founding legislation, legitimate amendments thereto and best practice.

Criteria of Success
PPP Unit is regarded as being a transparent organisation that deals with receipts, payments, assets and liabilities in a manner that is consistent with the best interests of the State and investors including donors

Accountability
That all internal and external audit reports and other reports have properly accounted for all transaction receipts, assets and liabilities and properly procured items of cost / expenditure.

5. Work Plans & Control Budget

To have the specific detailed operational responsibility for initiating and coordinating the PPP Work Plans and control budget process for the PPP Unit.

Criteria of Success
PPP Unit has a one-year work plan which reflects the budget. The work plan and control budget are prepared from inputs provided by each project.

**Accountability**
You carry out monthly, quarterly and annual reviews of the actual performance of the PPP Unit finances. These reviews to compare actual performance against that planned and where necessary corrective or updated action initiated and agreed monthly and quarterly.

*NB: This position will hold the main responsibility for all administrative matters of the PPP Unit, while working with the PDF when required.*
Appendix 9. PPP Policy & Procedures Manual: Draft Outline of Section Headings

As stated previously in this report, detailed Policy & Procedures Manuals for the PPP Secretariat and PPP Nodes are needed. Each such a Manual will provide the basis for clear standards that each body must be accountable for in fulfilling their functions under the new PPP Framework. These Manuals should be available as early in the PPP program as possible, to ensure there is a consistent approach at all phases of the PPP project life cycle.

Kenya’s PPP Framework:
Phases of PPP Project Life Cycle

The development, drafting, and finalization of this Manuals should be undertaken by Consultants, under supervision of the PPP Secretariat itself as a key part of its work plan to establish the new PPP Framework. The PPP Secretariat should seek to both distribute and to train Line Ministry and PPP Node staff on both understanding and using the Manual to prepare and propose PPP projects. This Manual should also be distributed to other key stakeholders to understand the steps and the requirements for PPPs.
Figure 1 - The Manual of Required PPP Procedures Project Life Cycle

Phase I: PPP Project Initiation & Screening

a. Criteria for selecting appropriate projects to screen as PPPs
b. Completing the PPP Project Screening Checklist & Concept Paper

c. Screening Checklist:
   - Need for the Project
   - Nature of the Investment
   - Duration of Project or Services
   - Size of the Project
   - Initial Budgetary Resources
   - Identify Stakeholders
   - Risk Transfer Opportunities
   - Opportunities to Bundle Contracts Together
   - Third Party Revenue Opportunities
   - Can Performance Indicators be Developed
   - Opportunities for Private Sector Innovation
   - Level of Market Appetite
   - Developing the PPP Project Concept Paper
   - Identifying Service Need & Project Objectives
   - Establish Project Scope & Identify Stakeholders
   - Identify Delivery Options
d. Review of PPP Suitability Checklist & PPP Concept Paper by PPP Secretariat & recommendation to proceed to Phase II Feasibility Analyses, or not

e. Review of PPP Concept Paper by the PPP PDF Board and decision to proceed to Phase II Feasibility Analyses, or not

**Phase II: Developing the PPP Project’s Feasibility Analyses & Proposed Risk Allocation Structures:**

a. Develop Implementation Plan and schedule for completion of Phase II: Identify resources required, propose deadlines, and estimates for Phase III-V

b. Retain Needed PPP Project Consultants

c. Refining the PPP Project Scope: Re-Specify the PPP’s required output levels of service

d. Evaluate Project Alternatives & explain why the PPP route is still proposed

e. Develop & implement PPP stakeholders consultation plan

f. Affordability Analysis: Estimating the Public Sector’s affordability limit for the project

g. Demand Analysis: Estimate the level of demand for the project’s services & update output levels of service

h. PPP Project Technical Feasibility Analysis: Evaluating all viable technical options to meet the project’s goals, identifying key technical components & suitable technologies, & revising technical output standards for the PPP project

i. PPP Project Financial Feasibility Analysis: estimate costs and probable range of required PPP tariffs, prices, “availability payments” and any needed public sector supports

j. PPP Project Economic Feasibility Analysis: Specify the planned net economic benefits from the new project

k. Legal & Institutional Feasibility Analysis: Identify all relevant laws & regulations and ensure project is legally viable; ensure Line Ministry will have institutional resources to implement, monitor, and enforce the PPP contract throughout its term.

l. Project Environmental Impact Analysis: Identify & measure all environmental impacts, and recommend required environmental mitigation measures and costs

m. PPP Project Risk Identification

n. PPP Project Risk Analysis: Estimating Risk Impacts and Probabilities and analyzing sensitivities

 o. Recommended PPP Risk Allocation Structure

p. Updating PPP Project’s Value for Money Analysis: Estimating value for money benefits and additional net economic benefits from the recommended PPP risk allocation structure

q. Assess Private Sector Market Interest in the PPP

r. P3CU Reviews the PPP Feasibility Analyses & Proposed Risk Structure & Recommends Approval or Rejection for Phase III

s. PPP PDF Reviews P3CU’s assessment and recommendations regarding further funding support for Phase III

**Template Models for Phase II:**
• Template for Terms of Reference for retaining PPP project consultants to prepare PPP Feasibility Analyses & Risk Structures
• Template PPP Financial Model for determining PPP financial feasibility, affordability, risk impacts & sensitivities, and value for money analyses

**Phase III: Conducting the PPP Tendering & Procurement**

a. Line Ministry Prepares Detailed Implementation Plan & Schedule for Phase III Tendering & Procurement (and updated estimates for Phases IV & V)
b. Line Ministry Retains & Managing PPP Tendering & Procurement Advisors
c. Completing Required Pre-Tendering Reforms
d. Preparation of Request for Qualification (RFQ) Documents: Project Information Memorandum & background data, Draft of PPP Contract(s) or risk allocation structure, Instructions for interested firms for submitting Qualifications, Qualifications evaluation criteria
e. Line Ministry issues Request for Qualifications (RFQ) to interested bidders, receives & evaluates Qualifications, and announces pre-qualified bidders short-list
f. Line Ministry conducts Bidder Conferences prepares project data room for bidders and prepares site-inspections/walk-throughs, as necessary.
g. Line Ministry Draft Final Tender Documents (RFPs) and PPP Contract(s) and submits to P3CU for review
h. P3CU updates affordability and value for money analyses, reviews Final Tender documents and approves/disapproves issuance
i. Line Ministry issues Final Tender Documents, bidders perform due diligence to Prepare their Bids
j. Receipt of Clarification Questions from Bidders & Possible Modification of Tender Documents
k. Line Ministry Receives Final Technical & Financial Bids
l. Evaluation of Technical Bids & Announcement of Technical Bid Results
m. Opening of Financial Bids
n. Review of PPP Contract Award Decision by PPP Secretariat & approval/disapproval
o. Line Ministry Announces the Selection Winning PPP Bidder
p. by Line Ministry
q. Execution of the PPP Contract (treatment of Bid Bonds)

**Annexes to Phase III:**

• Template for Terms of Reference for PPP Tendering & Procurement Advisors
• Template for a PPP Investment Memorandum
• Template for contents of a Request for Qualifications & Instructions
• Template for Contents of a Request for Proposals & Instructions
• Template for a PPP Contract
Phase IV: Finalizing PPP Contract Signing & Facilitating Financial Closure

a. Finalizing clarifications to the PPP contract and its attached schedules (technical detail vs. legal/contractual risk transfer)
b. Treatment of “Conditions Precedent” & ensuring Govt. obligations are fulfilled re conditions precedent
c. Review and approval of final PPP contract(s) & schedules by PPP Central Unit (and PPP Ministerial Committee) prior to signing (Incorporation of SPV)
d. Understanding the requirements of project-backed financing for PPPs and requirements of lenders (lender due diligence, credit enhancements, final design of facility, final financing package, signature of direct agreement, payment of success fees, etc.)
e. How Line Ministry & PPP Central Unit can facilitate/support the selected bidder & their lenders reaching successful & timely financial closure
f. How to monitor the awardee’s progress in reaching financial closure
g. How to handle instances of failure to reach financial closure (cancellation or extension, etc.)

Phase V: Post-Award Performance Monitoring

a. How to Prepare a PPP Contract Monitoring Plan (establishing Performance Monitoring Committees: Construction, Operation, & Dispute Resolution/Pre-Arbitration)
b. Monitoring Performance during project construction (Govt. & SPV agreement on appointment of Independent Advisor/supervising engineer during construction)
c. Monitoring Performance during Operation/Service Delivery Stage (Operational Performance Monitoring Committee & checklists)
d. Managing Price Adjustments (within the context of the existing PPP Contract)
e. Managing Requests to Revise or Renegotiate PPP Contracts (changing the PPP contract itself. Clarification changes vs. risk-transfer changes)
f. Managing Dispute Resolution (Dispute Resolution Committee, Alternative Dispute Resolution techniques, & Contract Termination procedures)
g. Contract Management at the End-of-PPP Contract Stage (inspections, residual asset valuation & asset transfer procedures, contract close-out protocols, termination of performance/surety bonds, PPP re-tendering options, etc.)