

THE RWANDA SMALL BUSINESS SET-ASIDE

Republic of Rwanda

Prepared for:

**The United States Agency for International Development
Kigali, Rwanda**

Under a Subcontract to:

**LABAT-ANDERSON INCORPORATED
2200 Clarendon Boulevard, Suite 900
Arlington, Virginia 22201
(703) 525-9400**

Prepared by:

R. Axel Magnuson

January 15, 1990



THE RWANDA SMALL BUSINESS SET-ASIDE

Republic of Rwanda

Prepared for:

The United States Agency for International Development
Kigali, Rwanda

Under a Subcontract to:

LABAT-ANDERSON INCORPORATED
2200 Clarendon Boulevard, Suite 900
Arlington, Virginia 22201
(703) 525-9400

Prepared by:

R. Axel Magnuson

January 15, 1990

TABLE OF CONTENTS

EXECUTIVE SUMMARY	ii
I. PRIVATE SECTOR DEVELOPMENT AND A SMALL BUSINESS SET-ASIDE PROGRAM	1
1.1 Constraints to Private Sector Development	1
1.2 Aims of a Small Business Set-Aside Program	1
1.3 Limitations in the Design of a Set-Aside Program	2
II. CRITERIA FOR A SUCCESSFUL SET-ASIDE PROGRAM	3
III. A SMALL BUSINESS SET-ASIDE PROGRAM FOR RWANDA	3
3.1 Regulations Limiting Firms to Government Procurements	4
3.2 Certification Criteria: "Threshold Firms"	5
3.3 Targeting Subsectors of Activity	6
3.4 Assuring that a Set-Aside Program is Legally Permissible	8
3.5 Assuring Levels of Coordination for Business Advisory Services for Set-Aside Firms	9
IV. THE SET-ASIDE PROCESS	12
4.1 Certification for Participation	12
4.2 The Set-Aside Bid Solicitation	12
4.3 Bid Preparation	13
4.4 Award	13
4.5 Post Award Business Assistance	13
4.6 Graduation from the Program	13
ANNEX A: THE U.S. SET-ASIDE PROGRAM AND RWANDAN SET-ASIDE DESIGN ISSUES	14
ANNEX B: DESIGN PARAMETERS	17
ANNEX C: BIBLIOGRAPHY	20
ANNEX D: LIST OF PERSONS CONTACTED	21

Executive Summary

The Rwanda Small Business Set-Aside Program Report is submitted to the USAID/Rwanda Mission and the Government of Rwanda by LABAT-ANDERSON INCORPORATED. This report provides a detailed assessment and description of a Small Business Set-Aside Program that would be appropriate and feasible for implementation in Rwanda.

Background

The Government of Rwanda and USAID/Rwanda signed the Policy Reform Initiatives in Manufacturing and Employment (PRIME) Program Grant Agreement in September 1985. The purpose of PRIME is to support the Government of Rwanda (GOR) in making necessary structural adjustments and policy changes to stimulate production and employment in the manufacturing sector, particularly in the small- and medium-sized enterprise (SME) subsector.

As part of the program component of PRIME, the GOR and USAID have been considering various proposals aimed at identifying policies and programs that will alleviate some of the major constraints facing Rwandan SMEs and improve the business climate.

This study, which responds to one of those proposals, focusses on assessing the feasibility of developing and instituting a Set-Aside Program for Rwandan SMEs. Initially, the Rwanda procurement process was reviewed in order to assess the potential of small-scale enterprises to participate in the process. Based on the findings, it was determined if a set-aside procurement program to promote SMEs would be warranted, and how such a program could be set up. Specifically, the following tasks were carried out: 1) Analysis of the PRIME/MINIMART team report; 2) Analysis of the capacity and organization of Rwandan SMEs and evaluation of their potential to satisfy the GOR and Project procurement needs and product requirements; 3) Determination of the areas that are the most promising and the products that should be given priority under the public purchasing contracts; and 4) Proposal of mechanisms and procedures for setting an SME Procurement Set-Aside Program.

The consultancy was carried out upon the request of USAID/Rwanda by Mr. R. Axel Magnuson for LABAT-ANDERSON INCORPORATED. Mr. Magnuson reviewed documents, interviewed key people in Rwanda, and wrote this final report. The consultancy took place in Rwanda from December 3-21, 1989. Additional time was spent in the United States preparing and translating the final report.

Report Summary

This report begins with a general discussion of private sector development and a small business set-aside program in Rwanda. A review of criteria for a successful set-aside program follows this discussion. The next section describes in detail the proposed Rwanda Set-Aside Program. The last part discusses the set-aside process and general implementation procedures. Annexes A and B review the U.S. Set-Aside Program and Design Parameters to consider in establishing the Rwandan Small Business Set-Aside Program.

Findings-Recommendations

A limited small business set-aside program is feasible under Rwandan laws currently in force and with little modification of existing institutional arrangements. The proposed program is built around the existing GOR procurement process. It adds two elements.

- A special competition procurement program that limits competition to the small, disadvantaged firms certified for the program.
- A follow-on program of business advisory services to firms providing contracted goods or services to the government.

Since only formally registered firms and non-profit associations like cooperatives can currently participate in the GOR's procurement program, participation must initially be restricted to small, formal but otherwise disadvantaged firms and cooperatives. Certification criteria should include measures that indicate small firms' limited access to training, credit and business advisory services.

The procurement process would remain essentially unchanged except that the Ministries of Finance and Industry would be responsible for identifying firms for limited competition or sole source bids on selected procurements suitable for small business participation. The other unique feature of the process is that participating firms would be allowed to seek joint venture partners who would assist in bid preparation and later provide production and management consulting services.

The government contracting process is essentially used as a vehicle to provide business development skills to participating firms. A set-aside program without an accompanying business assistance program is not a useful tool to develop the capacities

of small- and medium-scale industries. These are firms that lack the production skills, management capacities and financial resources to compete effectively in private and public markets in the first place.

During the contract period, participating firms would be provided with business advisory services through one of several modes:

- Through the Ministry of Industry and project level business advisory services available through SERDI, EWACU, Technoserve or the PRIME program.
- Through local private consulting firms who would provide contract consulting services on an as-needed basis.
- Through joint venture partners who would provide production and management expertise as part of their participation in the contract team.

This set of arrangements will require only minimal changes in existing administrative systems. As it will rely heavily on private sector resources it will not require any further build-up of government services.

The feasibility of this program will be largely determined by two factors.

1. A legal confirmation that the proposed changes in the law on public procurement permit the type of limited competition called for in this set-aside program. Current readings do seem to permit this type of program.
2. Agreement on an institutional arrangement that would provide the kind of business advisory arrangements necessary for the developmental aspect of this program. Current administrative arrangements and the existing business advisory programs alone do not constitute a sufficient base from which to provide business assistance functions. The government will need to consider the use of additional, local private sector sources of business advisory services.

I. Private Sector Development and a Small Business Set-Aside Program

Analyses of the business environment in Rwanda confirm that a considerable public sector procurement market exists in Rwanda (see Bibliography, Annex C). The analyses also indicate that some portion of that market can be taken care of by existing smaller Rwandan firms. The role of such firms in the public and private markets can be enhanced if they are provided with technical and business assistance services during the period in which they are contracted to supply those goods or services. A small business set-aside program could provide that developmental push to selected SMEs. There are, however, significant constraints in the general business environment that define some of the design parameters for the program.

1.1 Constraints to Private Sector Development

A number of factors in the overall business environment make private sector development in Rwanda difficult. Levels of production technology, management capacities and small markets are active constraints that constitute the major design issues for any business assistance program. In Rwanda's case a number of government policies and procedures contribute to an already difficult environment in which to do business. Complicated business registration procedures, a regressive tax structure and credit policies that in effect restrict credit and guaranties to "formal" firms are the most important of these. Annex B, Design Parameters, describes these constraints in more detail.

1.2 Aims of a Small Business Set-Aside Program

Despite these limitations, a small business set-aside program has features which could measurably contribute to the development of the private sector in Rwanda. The proposed program has a structure that seeks to use government procurements as a means to building the competitive capacities of firms. It is important to understand that the program is wider than simply giving enlarged, special access to public procurement contracts.

The goal of a small business set-aside program is to create jobs and increase income levels for those who own and are employed by the participating business. At the level of the national economy, the goal is to expand employment in the off-farm sector of the economy in higher value-added industries.

The purpose of a small business set-aside program is to permit existing firms to be more competitive on the private sector market. They become more competitive through improvements in

their technical and business capacities and through improvement of their financial condition. A set-aside program is designed to help firms to these ends.

The set-aside program has two parts, enlarged market access and business advisory service.

The government provides enlarged access to public sector procurements and targeted business training to the firms during a fixed period of participation in the program while they are providing contracted goods or services to the government. Participating firms are enrolled in the program for a set number of years and must gradually reduce the percentage of their business that is derived from government contracts under the program.

Once certified for participation, they are then provided with a variety of services.

- Financial assistance in the form of business assistance loans and advances on contract payments. Assistance may be given for production assistance, management training or consulting services. This assistance may also extend to the level of bonding and surety assistance.
- Training and advisory services are supplied on an as-needed basis through private sector training and consulting firms, joint venture partners or government business advisory resources.

1.3 Limitations In the Design of a Set-Aside Program

The same factors which make progress in the general business area so difficult make access to public sector procurements nearly impossible for all but a few firms in the private sector.

The most significant constraint for access to public sector markets is that only firms or cooperatives that are already "formally" registered can participate in public procurements. A major conclusion of this study, then, is that a small business set-aside program would have to start off by working only with those firms that are already formally registered and therefore legally permitted to participate in public sector procurements.

The limitations of alternative designs are clear. Waiting to change the laws that would open up these markets to non-formal firms would postpone the start of a set-aside program indefinitely since government officials feel that the current registration requirements are basic to the success of the

procurement program. Likewise, working with firms to get them through the current registration process and the various sub-tasks required would also require a highly intensive management assistance program. The government's capacity to create such a program is limited. Thus, any set-aside program must initially be designed to accommodate existing regulations and prevailing administrative capacities.

II. Criteria for a Successful Set-Aside Program

A set-aside program is developmental in the sense that it aims at getting firms to a level of competence that will allow them to more effectively compete in the private sector marketplace. Special access to the government procurement process is simply a means to accomplishing that end.

Therefore, success of the program needs to be measured in two ways.

- First, it must assist firms in their business development without creating a high level of dependency on favored access to government contracts.
- Secondly, it must provide the government with goods and services at levels of quality and delivery assurances that are not either more costly or less reliable than would otherwise be provided by full and open competition.

This latter measure is important for the institutional viability of the program as much as it is for the proper functioning of the government services being supplied through the set-aside program. As will be described later in the detailed program description, this program criterion plays an important role in the design of a set-aside program for Rwanda. The most important consequence of this criterion is that program participation must be limited to a number of firms that can be adequately monitored to assure levels of quality and delivery.

III. A Small Business Set-Aside Program for Rwanda

A small business set-aside program is feasible for Rwanda. There are limits to the scale of the program that can be initially implemented in Rwanda however. It can serve only a specified number of firms both for legal and administrative reasons. Our analyses indicate that at the present time a set-aside program cannot serve all firms but can help those already at a "threshold" level of development proceed to another point of growth. This includes private firms and cooperatives.

The program concept is simple in its general thrust. Firms qualifying under the criteria established for the program are certified for participation in the set-aside process. For selected firms meeting the requirements of particular procurements, the government provides enlarged access to public sector markets. During their participation in the program they are given production and business management training while they are providing contracted goods or services to the government. These business advisory services can be provided through either existing, government sanctioned projects or directly from private sector consulting firms.

Five issues need to be considered in order to understand the limits imposed on this design by the legal, administrative and business environments of Rwanda.

3.1. Regulations Limiting Firms to Government Procurements

Current regulations prohibit non-formal, unregistered firms from participating in government procurements. This attempt of the government at quality control in its procurements must be acceded to in the design of the program. Therefore for the initial phase of this program two target groups have been identified as potential participants in this set-aside program:

- Small- and medium-scale formal enterprises (SMEs).
- Cooperatives which group together smaller producers.

As those requirements become more flexible, a larger pool of firms can be considered for participation in the program.

The logic of this approach to the set-aside is based on existing conditions and regulations. The existing government procurement program is centralized through the Ministry of Finance for the Government's recurrent budget and through the Ministry of Plan for the Investment budget. Orders above a certain value are passed from the purchasing agency [Ministere de Tutelle] to the Ministry of Finance where the purchase request is first compared to the budget for that ministry. It then passes into one of three procurement modes; Open competition, limited competition and sole source procurements. Orders below a certain value may be done through a direct purchase by the government. The magnitude of these smaller purchases is not specified in the PRIME report.

For any participation in the public sector procurement process, an enterprise must be registered as a formal business, either for profit or not-for-profit (Association But Sans Benefice- ABSB),

as is described in Annex B of this document. This process is composed of a number of separate approvals ranging from certification that a firm has paid its taxes, and is therefore registered as a firm, to statements of registration with the Ministry of Commerce and the Chamber of Commerce.

Given these legal restrictions in the procurement process, there are limits to the types of firms that might be included in a program to benefit SMEs. Two target groups have been identified as potential participants in this set-aside program: Small- and medium-scale formal enterprises, and cooperatives which group together smaller producers. The set-aside program can admit more participants in the future if the government continues its reform of the registration process. By making the registration process more appropriate to the needs and capacities of small- and medium-scale industries, more firms will become eligible to participate in government procurements. More firms can be admitted when there are business advisory resources to served them, either in the public or private sectors.

3.2. Certification Criteria: "Threshold Firms"

The criteria for certifying individual firms and cooperatives for inclusion in this program will have to be discussed more carefully with the Ministries of Industry and Finance, among others, but certain common criteria stand out from the studies previously done for PRIME and other groups in the government.

The most common criterion for all enterprises in the program is that they have a basic level of competence in their product or service area. They must be able to satisfy minimum levels of quality acceptable to the government markets. In the U.S. program this is done through an examination of past work.

Secondly, they must be what are called "threshold" firms. Participation in the program must balance the consideration of existing capacity, restricted access to finance or training, and potential for growth. Firms that are registered, but "small" in size and constrained in their ability to move to higher levels of production or employment are considered to be threshold firms.

An example of this type of firm is provided by the case of a furniture manufacturer in Butare. He has fifteen or so employees, a sizeable factory of about 5,000 square feet, power machinery and an accountant/bookeeper. He has financed the business through personal loans from friends and the revenues of the firm. An inspection of the work indicated that the level of quality placed him in a category of firms that was somewhat higher than could be expected from "corner carpenters"

(menuisiers du coin) but not at a level where he could expect to get very extensive business from more sophisticated clients who order in large lots. He has had only limited success in getting work from the local non-governmental organizations and has seldom received work from the local government. They have instead ordered materials from Kigali. In short his firm is a good candidate for technical and managerial assistance that would put him into a higher business category.

Criteria developed in previous studies by PRIME and other government programs for specific subsectors can be used to target firms for participation in a set-aside program. For instance, in the furniture industry, suggested criteria have included a scale of twenty or fewer employees with a gross income level of less than one million Rwandan francs. Similar criteria exist for defining small firms in the construction industry.

Cooperatives engaged in supplying commercial quantities of goods to the government are apparently not as numerous, but according to interviews there are several that can clearly already supply considerable supplies of foodstuffs to various services of the government. Prospects for bringing some cooperatives into the wider government markets for furniture also appear to be interesting. A cooperative was used in the development of the furniture for the Banque Populaire several years ago. Involving cooperatives in this program would have the special benefit of involving smaller groups and microenterprises.

3.3. Targeting Subsectors of Activity

Further work needs to be done on the identification of the best areas for concentration of activity. Studies done by PRIME (Nguyen Huu, et al.) indicate that the construction and furniture areas are among the largest of the procurements done by the government that might be appropriate to SMEs. For example, some sixty percent of the work done by the Ministry of Public Works is in the construction of buildings. Little has been done to identify the "fournitures" procurements that the government makes and what roles PME's might fill in that area. The study done by PRIME, "Acces des Artisans at des Petites Producteurs aux Commandes Publiques," indicates that the volume of openly competed, public sector procurements of goods and services over the past four years ranges from four to eleven billion Rwandan francs or between \$55.3 and \$197 million dollars at current, unadjusted exchange rates. Public works are by far the largest proportion of each year's expenditures in the procurements, with just over 50% of the 1989 expenditures and over 77% of the 1988 expenditures going to public works. Of those amounts a large proportion each year goes to building construction. The

percentage of public works going to Rwandan firms has ranged from 13% to 56% over the last four years, with Rwandan firms getting less than fifty percent of the contract work for three of those four years. A similar pattern is noted for the procurement of supplies and furnishings, with a high percentage of contracts going to foreign and large national firms.

In the analyses done by PRIME of the type of materials purchased by the government, the results indicate that furniture, office materials, agricultural materials and a variety of other goods are purchased primarily from large producers and importers. The PRIME study asserts that many of these items could be produced by local small- and medium-scale industries and cooperatives. Particularly interesting is the fact that the largest part of the construction materials purchased by the government are from small and artisinal producers.

The report cites several areas as being targets of opportunity for the promotion of small industries and cooperatives. They include: office and residential furniture, agricultural implements, clothing for the army and police forces, housing rehabilitation and renovation, office equipment repair and foodstuffs.

Other reports, including those of the PRIME program and USAID, cite strong small business capabilities in the construction, construction materials and office furniture industries. They also cite the already important role of cooperatives in providing foodstuffs to the army and other government services. The base of activities in these areas constitutes a large part of the formal and informal off-farm employment opportunities in the economy. Yet only a small percentage of the existing mass of firms in these areas are formally registered. In terms of firms in the construction sector, approximately 160 firms appear to be registered. Only slightly more than one hundred appear to be registered in the furniture industry.

Within these two fields alone one would not expect that many of the firms would be classified as large in any sense. One would expect that most of them are relatively small in terms of their total number of employees and volume of business. They are characteristically not well managed financially, lack access to financial resources, and have staff with little specific management training suitable to their needs.

A set-aside program with a business assistance component could serve these firms well as a developmental tool. The firms already have an established business base with experience in production and marketing. Access to public markets and business

assistance would address the issues of contract management, production quality, and financial management in an environment that would encourage improved performance. Administratively, the focus and small size of the potential pool of certified participants would make the initial program manageable. Time would be spent on on-site training and consulting rather than having to train firms from the ground up.

3.4. Assuring That a Set-Aside Program is Legally Permissible

A set-aside program is based on the legal ability of the government's procurement process to permit limited competition among small firms. Competition is limited to restrict larger firms from certain procurements that can appropriately be supplied by smaller firms.

In the case of Rwanda, interpretation of the existing procurement laws would have to be clarified to determine if they would permit set-asides of some procurements for selected groups of smaller firms. A limited reading provided during the three week consultation seemed to indicate that the current and proposed laws governing public sector procurements do permit the creation of a set-aside program.

Conceptually the program would have to take advantage of the opening allowed for "limited competition bids" (appel d'offre restreinte) and sole source contracting (gré à gré) in the current and proposed laws on public procurement. This key element could, according to at least one jurist, permit the purchasing agency [Ministre de Tutelle or Prefecture] or the Ministry of Finance to preselect a short list of firms from the set-aside program to be bidders on a contract. In any case this is the process as it is already observed now and it should be possible to use SMEs in this process on the condition that they can meet the registration requirements.

Legal clarification is also needed on the functioning of the local government procurement programs at the Prefecture level. They already purchase considerable goods from the small firms and cooperatives in local markets, particularly in supplying food, office furniture and other services. The law appears to say that they must purchase goods in the same way as the central government, but it is not clear what process takes force in the case of small-lot, incidental purchases.

In the particular case of cooperatives and other non-profits, the registration requirements are less stringent and it appears that they could supply at least foodstuffs and other limited ranges of goods they normally produce. They already supply foodstuffs to

local governments, the army, and other groups. This channel of activity seems to be particularly promising in that it can involve larger numbers of microenterprises in the form of member units of existing cooperatives.

3.5. Assuring Levels of Coordination for Business Advisory Services for Set-Aside Firms

Business advisory services will be required at several points in the set-aside process. Those include:

- Bid proposal activities, including cost proposals, management plans, technical proposals, and financial plans for the contract.
- Post-award business advisory services that include quality control and delivery assurance up to and including final contract completion. Services anticipated in this period of the program include assistance in financial management (cash flow monitoring, cost control, stock purchasing), production quality, and contract documentation. These may be in the form of consulting services or short-term training.

There are two potential institutional forms for the business advisory services that are needed for this program. The design criteria used in selecting among these must take account of the government's limited capacity to establish a full-service business advisory program. The recommended approach avoids the necessity of expanding the GOR's business advisory program. The GOR's role in this approach would be limited to administration of government contracts. Business advisory services would be provided by private sector consulting firms and joint venture partners to the largest extent possible. Projects like SERDI, EWACU and Technoserve could continue to play important roles but would not be the central points of the program.

- Government Business Advisory Services

One option is that the business advisory services provided by the MINMART (Ministere de l'Industrie, des Mines et de l'Artisanat) with the Direction General Petites et Moyen Industries performing a contract monitoring function. At the beginning of a firm's certification for participation in the program it would be assigned someone like the SBA's Business Opportunity Specialist who would work with the firm throughout its participation in the set-aside program. As a firm prepared to bid on a set-aside procurement the Specialist would direct an advisory resource to the firm if it needed assistance in preparing the bid documents. The assistance would come from one of the existing business

advisory services/ projects now working under the Ministry. Examples of these are SERDI, Technoserve and EWACU, all of which provide one level or another of services and training to enterprises.

After a contract is awarded the Specialist would monitor contract performance with the firm. On the basis of those findings the Specialist would assign further advisory services to the firm to strengthen performance.

This approach has the advantage of using the existing services in Rwanda. It has the serious disadvantage that these services are currently very limited and already overextended in providing services to a large number of firms. The possible exception to this is EWACU, since it trains centralized cooperative staff which in turn assist in training the cooperatives' smaller group members. Even in this case EWACU is not set up to provide case-specific business advisory services on a very large scale.

- Private Sector Business Advisory Services

The second, preferred approach uses private, non-governmental, local business advisory resources. In the U.S. set-aside program the business advisory function is seen as a partnership between the public and private sectors. Training is never provided by the U.S. Government directly. It is financed through purchasing those services directly from the private sector. If, for instance, a firm requires consultant services on a production problem, the SBA program will provide financing for that service on the basis of the recommendation of the contract monitor assigned to the firm and its contract activities. It is paid for out of funds assigned to the SBA and not directly from funds provided for in the participating firm's contract with the government.

The situation in Rwanda is somewhat different in that private sector business advisory and consulting services are not as well developed as they are in the U.S. Rather, they are largely found in the form of project assistance available in donor programs such as that funded by USAID through Technoserve.

- Rationale

The basic limitation inherent in the government providing that type of advisory service is that its ability to service firms is limited by the availability of project finance and competent staff. These programs are generally understaffed relative to the demand for such services largely because skilled advisors are difficult to find and employ in such positions. Additionally,

government administrators are often not aware of the needs, or the urgency of the needs of private sector firms trying to fill contract orders on a fixed delivery date. It is this condition, in particular, that strongly supports considering the alternatives to the government provided business advisory services and the realistic possibility of using those services in the set-aside program.

In the particular case of Rwanda, there are other constraints as well to the government participating directly in the monitoring and business assistance process. The Ministry of Finance has said that it does not want to have to monitor the performance of small business contracts in this program or provide training. Individual purchasing agencies such as the Ministry of Public Works will also not be comfortable with this kind of activity.

The alternative is based on the fact that private business consulting services do exist on a limited scale in Rwanda. Three consulting firms were identified in the MAPS exercise. Designing the set-aside program so that it permitted the use of Rwandan business advisory services or firms would encourage their growth and establish an indigenous base for such services rather than perpetuating the current situation of dependence on outside expertise. The relative underdevelopment of private sector training and advisory services is something that this program could address fairly simply in two ways:

- By allowing the set-aside firms to team up with "Business Advisory Partners" during the bid phase of the procurement process. The Partner would in essence be a co-bidder on the procurement, assuring itself of direct costs and a fee for its participation if the firm successfully completed the contract. This is essentially a joint venture model, with the consulting firm acting as a management and training partner.
- By allowing firms participating in the set-aside program to contract with private sector consulting firms after a contract was awarded and have that service paid for by funds from the set-aside program as part of the procurement cost. This approach echoes the idea of the government providing the service directly, except in this case it would provide services purchased from the private sector instead of through government administered, foreign-financed assistance programs.

IV. The Set-Aside Process

There are six essential steps in the set-aside process as it has been conceived. The program is built around the existing Government procurement program and seeks no changes in the process except in "setting aside" portions of procurements for competition among small- and medium-scale industries. The process is designed to interfere as little as possible with the normal functioning of the agencies actually procuring goods and services. They are largely outside the set-aside process after the request for bids is announced.

The major institutional focus of the program should probably be in the Ministry of Industry, which will serve to coordinate the process with the Ministry of Finance and the participating set-aside firms.

These steps include:

4.1 Certification for Participation

This is the process of certifying firms for participation in the program. In the case of Rwanda, once the sectors of activity are agreed upon, the list of registered firms will serve as the base from which initial contacts would be made. As firms are certified by the Government for participation and then enter the program, they will need to have institutional support that helps them identify appropriate procurements. Each firm would be assigned a Business Opportunity Specialist who would categorize the firm by major industry or sector product codes and determine what type of contracts the firm may bid for. The firm's Business Opportunity Specialist would monitor the various government markets to identify upcoming bids that are appropriate for the firm. The certified firm would then be given an orientation to the government markets that it might compete in.

4.2 The Set-Aside Bid Solicitation

The government, having designated specific procurements for the set-aside program, would prequalify a select list of firms to be eligible for the competition and solicit bids from those firms. While competition would be restricted, the government's interests would be protected by setting standards for the firms entering the competition, and predetermining a fair market value for the procurement that one would have expected in the case of a fuller competition.

4.3 Bid Preparation

The selected firms would prepare cost, technical and management proposals with the assistance of either joint venture partners or the business advisory services of organizations working for the government. Their financial and cash flow needs would also be discussed with potential sources of short-term credit.

4.4 Award

The government would let the contract and assign a contract monitor from the Ministry of Industry to assure that the procurement meets the specifications established in the bid documents. [In the U.S. program, the SBA becomes the administrator of the contract for the purchasing agency, assuring delivery as specified in the contract because it has the authority to cancel the contract for non-performance. In the U.S. the SBA is given leverage in this process through its authority as administrator of the contract.] If problems arise the monitor can require remedial actions or assist in the provision of training or other technical assistance. Some enforcement authority like this will probably be required to assure that the contracting firm will follow the recommendations of the monitoring agency in fulfilling its contract.

This feature of the U.S. program may not be appropriate for Rwanda but it gives the government a level of control over the program that may make it more acceptable to agencies participating in the set-aside procurement program.

4.5 Post Award Business Assistance

As the contractor fulfills the contract, production and business assistance may be provided as deemed necessary by the contract monitor and the contracting firm. These services may be procured directly from the private sector and paid for with set-aside program funds, or they may be provided through government-administered assistance programs.

4.6 Graduation from the Program

Once a firm has reached a volume of business that puts it outside the limits established for participation in the program, or the firm has participated in the program for the maximum time permitted, then it is graduated from the program. Given their fulfillment of the firm size and time criteria for participating in the program, these firms are then considered technically and financially capable of competing for contracts under full and open competitive modes.

Annex A: The U.S. Set-Aside Program and Rwandan Set-Aside Design Issues:

This section briefly describes how the 8(a) Small Business Set-Aside program works in the United States. The comparison between it and what is being proposed for Rwanda is important because the U.S. Program illustrates the potential problem areas to watch out for in developing the principle for Rwanda and the institutional difficulties in setting up such a program. Commentaries are provided on the U.S. program that apply equally to Rwanda.

Components of the U.S. Program

In the U.S. program run by the Small Business Administration, two sources of financing are available to small business. One is a programmatically separate program run by the Small Business Administration for initial financial assistance. The other, specifically for firms in the 8(a) Program, offers "Economic Opportunity Loans" and are provided through the Finance and Investment Division of the SBA. The financing provided is only intended to be a supplement for funds available in the private sector. Financial assistance is provided for specified business expenses and not to supply either operating or long-term credit.

1. Certification

Admission to the program is obtained through a certification process which is based primarily on two criteria. The firm must be majority owned by a person considered to be disadvantaged by the program criteria, whose personal net worth must be less than \$250,000, not including residential property. Secondly the firm's revenues, as averaged over the last three years, must not exceed a certain level. That level is determined for particular product and service categories. A determination is made concerning the firm's appropriateness to provide goods or services to established government markets. Firms that do not manufacture goods or provide services sought after by the government do not normally become certified by the program.

2. Business Plan Development

Once a firm is certified, assistance is provided in the development of a business plan and orientation to the government markets that the firm may compete in. The firm is assigned a Business Opportunity Specialist who categorizes the firm by major standard industry code product codes and determines what type of contracts a firm may bid for. For each firm in the program, the Business Opportunity Specialist determines a "competitive

mix" for the firm which outlines the firm's targets in contracts other than those offered in the 8(a) program. This mix is part of the business plan that is developed with the firm. The business plan is redone annually.

3. Fixed Period of Participation

To insure that the firm moves toward a competitive capacity in the private sector, the program reduces the level at which a firm can participate in contracts awarded in the 8(A) program over the period of eligibility in the program.

During the first four years, the developmental period, the firm is permitted to have up to 90% of its total contract revenue come from government contract sources. During the last four years, the transitional period, that value must gradually decline to the point that in the last year of eligibility in the program the firm must have no more than ten percent of its contract value from government sources.

The government agencies determine which procurements are suitable for small business and let that be known to the SBA. Agencies usually have a predetermined target goal for set-asides for a year. For an individual procurement, the purchasing agency must determine the "fair market value" of the procurement as a basis for evaluating bids made by 8(a) firms in the limited competition permitted under this program.

4. Competitions and Awards

Once into the program, the firm's Business Opportunity Specialist monitors the various government markets to identify upcoming bids that are appropriate for the firm. The Specialist may then assist in the preparation of technical and business proposals to respond to Requests for Services or Materials.

One of the important features of the program is that it permits limiting competition to only small firms. The SBA determines which procurements are appropriate for limited competition among firms falling within a given standard industrial code category. Competitive thresholds are set for a procurement. At a certain value of contract, the award may be competed among a restricted number of certified firms. Under certain other conditions a procurement may be given on a sole source basis to an appropriate firm. For instance, a procuring agency may wish to achieve a wider geographical distribution of its procurements. The issue of the distribution of contracts among firms that are in the program has been a difficult problem for the SBA. Controversy has centered on the determination of eligibility of particular

firms to be included in one or another bid. According to Congressional testimony, criteria used in the short-list process are not clear and decisions have been based on arbitrary factors.

In each case the SBA must be sure that the award of the contract will not increase the firm's size to the point that it becomes ineligible for the program.

5. Post-Award Monitoring and Assistance

Technical assistance in marketing and business administration is the key element of the program. In the U.S. program, the SBA becomes the administrator of the contract for the purchasing agency, assuring delivery as specified in the contract. On the client business side of the program, it acts as the intermediary in seeing that the firm knows about upcoming bids. Once awarded the firm is steered toward the appropriate business assistance resources.

Once a contract is awarded, the Business Opportunity Specialist monitors the performance of the firm in fulfilling the conditions of the contract. The SBA is given leverage in this process through its authority as administrator of the contract. If problems arise the Specialist can require remedial actions or assist in the provision of training or other technical assistance. The assistance program often draws upon existing government training programs but will pay for short-term training as necessary.

One of the major weaknesses of the U.S. Program is that there are not sufficient Specialists to adequately monitor the performance of participating firms. According to Congressional testimony in 1989, this has accounted for the failure of many participating firms and abuses of the contracting system.

6. Graduation from the Program

When a firm reaches a certain level of revenues or has been in the program for the maximum number of years, it is graduated from the program. It can also be declared ineligible for further procurements before either of those landmarks if it has not conformed to the conditions agreed upon in the development of its business plan. For instance, if a firm has reached a certain level of procurement value before the end of a business year, it can be declared ineligible for further contracts bids in that year.

Annex B: Design Parameters

A number of factors in the overall business environment make private sector development in Rwanda difficult. Government policies, levels of technical and business training, and small markets are active constraints that constitute the major issues to consider in designing programs to assist small- and medium-scale industries in Rwanda. The same factors that generally make growth difficult in the private sector play even more heavily in the government markets. The particular constraint for the public sector markets is that only firms that are already formally registered as cooperatives or privately held business enterprises can participate in public procurements. This limits the number of firms that could participate, at least initially, in a set-aside program. But even within these limits there are some positive opportunities.

Our major conclusion is that a small business set-aside program would have to start off by working with only those firms or cooperatives that are already legally permitted to participate in public sector procurements: Cooperatives and already formally registered firms. This does not mean that small and informal enterprises will be initially excluded from the program. In the analyses to date it appears that cooperatives, treated as they are in tax and business law, may serve as a useful mechanism for allowing their small member groups to enter into the government markets.

The section that follows describes the major constraints briefly. They are detailed in several of the studies cited in the attached bibliography.

A. Constraints In Overall Business Environment

The GOR has a procurement program that puts a large percentage of its procurements out for open competition. There are a number of specific requirements for participating in these public procurements, which, taken together, require that a bidder be a "formal" enterprise.

This constitutes a formidable constraint in using the concept of a set-aside program for developing SMEs. There are several barriers to firms entering the "formal" business arena. These are barriers that characterize the general business market and are generally recognized as limiting business development in general. In the public sector markets they play a very specific and definite role in blocking entry into the market. It is these constraints, and not the simple opening of government markets, that are the specific problems.

There are at least three problems for a firm becoming "formal." Each is measurable to an extent and the process, if not the costs, to alleviate each problem is at least partially recognized.

1. Vulnerability to Regressive Business Taxes

While firms may actually be able to fill out the long series of forms required by various parts of the government to become registered firms, there are positive disincentives to becoming a registered firm. The taxes, which have been described in a number of studies, are regressive in the sense that they are often applied before value has been added to raw materials. The cost of these levies at various levels have been calculated in several studies, particularly that of Ngirabware and Mead. On an informal level, registering as a firm leaves the firm open to other types of informal levies that may be invoked by local authorities.

According to the recent survey research done for the USAID through the MAPS program by Ernst and Young/Austin Associates, business tax vulnerability is considered to be one of the most negative influences on business. One would expect any businessman to say that in any country. But in this case economic analyses done by Ngirabware and Mead for the study program of PRIME bear out the complaints as being real disincentives.

2. The Registration Process

The registration process itself is composed of numerous steps that involve numerous ministries and a series of interlocking requirements that make the process costly. The process itself is probably the second most significant barrier in the decision of firms whether to enter the formal marketplace and compete in government markets.

3. Implicit Requirements of the Registration Process

Implicit in the requirements of registration are assumptions that the firms will be able to put into place a number of business systems that will grant them access to the documents that are required for registration. Among those are accounting systems that would be necessary for establishing the basis for tax computations. The cost of establishing programs for training business people on a national basis for this level of skill is a further major constraint. Another important consideration is the

process of setting up a bank account that would serve as one of the items demonstrating the firm's fiscal responsibility.

B. The Special and Strategic Case of Cooperatives

Cooperatives and other not-for-profit associations are given special status in terms of the registration requirements. By virtue of their being registered as cooperatives they may participate in competition for government procurements. Acting as intermediaries for small producer groups (groupement) that are members of the collectivity, cooperatives may contract with the government to supply goods under the normal conditions of the procurement laws. There is, in fact, a strong participation by cooperatives in the supplying of foodstuffs and other consumable supplies to the government.

Bibliography

1. Mescher, Micheline with Claudine Mudenge and Khiem Nguyen Huu. Climat de l'Investissement et Environnement Operationnel de l'entreprise privée au Rwanda. Mai 1988.
2. World Bank. Rwanda Public Expenditure Program: An Instrument of Economic Strategy. Report 7717RW
3. Gakwaya, Augustin et al. Access des Artisans et des Petits Producteurs aux Commandes Publiques; Document de Travail. Programme PRIME, Ministère du Plan. Government of Rwanda. November 1989.
4. CIC Technique. Procès verbal des réunions du CIC Technique...relatives à l'examen des textes de l'avant projet de loi sur les marchés publics...Ministère des Finances et de l'Economie, Government of Rwanda. Number 1830/FIN 07.00/E 20 July 1987.
5. PRIME; Programme de Soutien à la Réforme de la Politique Industrielle et de l'Emploi. Etudes des Mesures d'Encouragement à l'Investissement et à l'Emploi.
 - Ngirabware, Augustin; Mead, Donald. Les Moyennes et Grandes Entreprises Rwandaises du Secteur Manufacturier Privé: Etudes Diagnostique et Impact des Politiques Economiques. Number 9, August 1988.
 - Nguyen Huu, Khiem. Etudes sous-sectorielle le secteur construction au Rwanda. Number 8, June 1988.
 - Nguyen Huu, Khiem. Etudes sous-sectorielle des Matériaux de Construction du Rwanda. Number 7, June 1988.
 - Nugawela, Patrick. La Prise en Charge des Activités de Promotion des Petites et Moyennes Industries et de l'Artisanat. August 1988.
6. Bilindabagabo, Frédéric, Memo: Les Différents Moyens de Passation des Commandes Publiques. Programme Prime, December 1989.
7. Centre EWACU Unite Formation. Artisans: Rapport d'Analyse de besoins en formation des Artisans. Carried out under contract with PRIME. July-August 1989.

Persons Contacted

1. Mr. BASOMINGERA, Alberto. Avocat, Bureau Evaluation, MINIFIN
2. Mr. BIZIMUNGU . Directeur Général, Investissement, MINIPLAN
3. Mr. Gregg CRUSE, Technoserve. Kigali
4. Ms. Tara GILDEA, Community Economics Corporation, Washington, D.C.
5. Mr. James GRAHAM, Director USAID
6. Mr. HAKIZAMUNGU, Joseph. Secrétaire Général, MINIFIN
7. Mr. James HERNE; Director, Technoserve, Kigali
8. Ms. Barbara HOWARD, Program Officer, USAID, Kigali
9. Mr. Roger JANTIO, MAPS Project. Austin Associates, Cambridge, MA.
10. Mr. KAMANZI, Callixte, Directeur Général de l'Artisanat et PME, MINIMART.
11. Mr. MBAGUITA, T.M.V. Coordinateur du Projet Prime.
12. Mr. NGARAMBE, Jérôme. Carpenter; Butare, Rwanda.
13. Mr. NGIRABTWARE, Augustin. Directeur Général, INDUSTRIE; Ministère de l'Industrie
14. Mr. Khiem NGUYEN HUU, Technical Assistant, Projet Prime
15. Mr. Patrick NUGAWELA, Director, Projet SERDI/UNDP/ILO.
16. Mr. NYAMIMA, Felicien. Centre OACHU; Directeur, Formation.
17. Mr. NYAMINANE, Felicien; Director of Training, Centre IWACU, Kigali
18. Mr. Henderson PATRICK, Project Development Officer, USAID, Kigali
19. Mr. RWAKAYIGAMBA Pierre, Secrétaire Général à la Présidence de la République, chargé du Service des Affaires Economiques et Financières.
20. Mr. SUGIRA, Ismael. MINIFIN.