



*Technical Report*

# **A Proposed BOT Bill to Enhance Public-Private Partnership in Infrastructure Development**

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**Prepared for**

**Gov. Consuelo S. Perez  
Board of Investment  
Department of Trade & Industry  
Republic of the Philippines**

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# Preface

This report is the result of technical assistance provided by the Economic Modernization through Efficient Reforms and Governance Enhancement (EMERGE) Activity, under contract with the CARANA Corporation, Nathan Associates Inc. and The Peoples Group (TRG) to the United States Agency for International Development, Manila, Philippines (USAID/Philippines) (Contract No. AFP-I-00-00-03-00020 Delivery Order 800). The EMERGE Activity is intended to contribute towards the Government of the Republic of the Philippines (GRP) Medium Term Philippine Development Plan (MTPDP) and USAID/Philippines' Strategic Objective 2, "Investment Climate Less Constrained by Corruption and Poor Governance." The purpose of the activity is to provide technical assistance to support economic policy reforms that will cause sustainable economic growth and enhance the competitiveness of the Philippine economy by augmenting the efforts of Philippine pro-reform partners and stakeholders.

Board of Investment Governor Consuelo S. Perez first requested EMERGE to help her determine how the country's Build-Operate-Transfer (BOT) Law may be improved to attract new private investments in infrastructure and improve the mechanism for private sector participation in public infrastructure investments. Her request was seconded by a letter from Rafealito H. Taruc, then OIC-Executive Director of the DTI BOT Center, dated 12/13/05. This technical assistance was designed to help the Department of Trade and Industry (DTI) draft necessary amendments to the BOT Law, Republic Act 6957, enacted by Congress 1990 and amended under Republic Act 7718 in 1994. These requests followed a lengthy process to review and amend the Implementing Rules and Regulations (IRR) of the BOT Law, spearheaded by BOI and the BOT Center, in order to improve the implementation of BOT schemes and encourage greater private sector participation in infrastructure provision. However, reactions in public hearings on the proposed amendments to the IRR in early 2005, and discussions among the members of the technical working group in charge of recommending amendments to the IRR, revealed the need for certain amendments in the BOT Law itself, because some of the reforms/changes sought to improve the implementation of BOT type projects could not be handled by mere amendment of the IRR. A team of consultants composed of Dr. Dante B. Canlas, Team Leader, Dr. Gilbert Llanto, Atty. Domingo C. Palarca, Atty. Rean Botha, and Ms. Rowena M. Cham undertook this task, and this is their report.

The team acknowledges with gratitude the financial support from USAID through the EMERGE Project. They also thank all the resource persons, too many to be named individually here, from the government and the private sector who provided useful information and insights during various discussions with the authors. However, the views expressed and opinions contained in this publication are those of the authors and are not necessarily those of the resource persons, USAID, the GRP, EMERGE or the latter's parent organizations.

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## List of Abbreviations

BLT	-	Build Lease Transfer
BOO	-	Build Operate Own
BOT	-	Build Operate Transfer
BT	-	Build Transfer
CAO	-	Contract Add Operate
BSP	-	Bangko Sentral ng Pilipinas
CCPAP	-	Coordinating Council for Philippine Assistance Program
DA	-	Department of Agriculture
DBM	-	Department of Budget and Management
DILG	-	Department of Interior and Local Government
DOE	-	Department of Energy
DOF	-	Department of Finance
DOT	-	Design Own Transfer
DOTC	-	Department of Transportation and Communication
DPWH	-	Department of Public Works and Highways
DTI	-	Department of Trade and Industry
EO	-	Executive Order
GOCC	-	Government Owned and Controlled Corporation
GSIS	-	Government Service Insurance System
GPPB	-	Government Procurement Policy Board
HB	-	House Bill
IA	-	Implementing Agency
ICC	-	Investment Coordination Committee
Infracom	-	Infrastructure Committee
IC	-	Insurance Commission
IRR	-	Implementing Rules and Regulations
IRA	-	Internal Revenue Allotment
LGC	-	Local Government Code
LGU	-	Local Government Unit
MTEF	-	Medium Term Expenditure Framework
MTPDP	-	Medium Term Philippine Development Plan
MTIPI	-	Medium Term Philippine Investment Program
NEDA	-	National Economic and Development Authority
ODA	-	Official Development Assistance
OPIF	-	Organizational Performance Indicator Framework
PDF	-	Project Development Facility
PPIDC	-	Public Private Infrastructure Development Committee
PPP	-	Public Private Partnership
PPPC	-	Public Private Partnership Center
RA	-	Republic Act
ROT	-	Rehabilitate Own Transfer
TRB	-	Toll Regulatory Board
TWG	-	Technical Working Group
WACC	-	Weighted Average Cost of Capital

## **Executive Summary**

This report proposes a BOT bill amending Republic Act no. 7718, also known as the Philippine BOT law. The bill seeks to enhance public-private partnership (PPP) and to make the latter a declared policy of the state in infrastructure development.

The huge investment requirement of the infrastructure sector amid tight budgetary constraints has prompted the national government in the early 1990s to tap the private sector as a partner in development. The BOT law was enacted to encourage private participation in public-infrastructure investments. Following the law's enactment, the BOT program was able to generate a number of projects in the power and transport sectors in the early 1990s. The program's momentum, however, slowed down as the country entered the first decade of the 21<sup>st</sup> century. The government's tight fiscal situation along with the voiding of a large airport terminal project dampened somewhat interest in the BOT program.

To rekindle private interest in PPP, certain principles must be observed from the very start; these include transparency, accountability, fiscal soundness, financial viability, institutional credibility, and genuine commitment to PPP.

Moreover, profound policy reforms are indicated to restore confidence in the BOT law. Foremost is creating a legal framework that protects property rights and is committed to enforcement of contracts. Moreover, the legal and judicial system in place must be conducive to contractual performance, and to fair and timely adjudication of any contractual dispute that may emerge. In addition, the legal framework must be backed by a substantive and operationally efficient set of implementing rules and regulations (IRR).

The records suggest that some BOT projects that encountered legal problems were generally of low quality at entry level. The implementing agencies (IAs) of government approved the proposed BOT projects at their levels without proper screening for quality prior to endorsing the projects to the Investment Coordination Committee (ICC) of the NEDA Board. This resulted in delays in the final approval

process, thereby eroding confidence of the private sector in the BOT program. Congressional investigations and court cases that intervened later on did not also help.

To overcome obstacles to successful formulation and implementation of PPP projects, institutional reforms must be pursued. Government IAs and local government units (LGUs) must acquire the necessary technical, legal and financial expertise to be able to identify, design, implement and monitor PPP projects. At the same time, regulatory bodies involved in the implementation of PPP projects must be credible, transparent, accountable, and technically competent.

The approving government authorities, likewise, need to be facilitative without compromising their mandate, while ensuring the consistency of their decisions with existing fiscal and investment incentives and procurement policies of the government.

Taking the various concerns at this stage about the existing BOT law, the BOT bill proposed here is guided by principles aligned with making PPP a state policy in infrastructure development. It upholds competitive bidding as the core of government procurement policy. It makes government agencies project owners and holds them responsible for first-pass approval. It maintains the window for unsolicited proposals but is firm about the government not extending any subsidy or performance undertaking to the project.

## **A Proposed BOT Bill to Enhance Public-Private Partnership in Infrastructure Development**

### **I. Introduction**

This Technical Memorandum proposes a bill to amend Republic Act (RA) no. 7718, the existing legal framework for build-operate-transfer (BOT) projects. We believe that the bill has strong potentials for enhancing public-private partnership (PPP), a declared policy of the state in infrastructure development. The bill seeks to overcome constraints to successful implementation of the present BOT law. These constraints, which were reported earlier in Technical Memorandum no. 1, emerged in the course of our review of the law and of the consultations that we had with representatives from the public and private sectors.

To have a strong PPP anchored on the BOT law, it is vital to establish a legal environment where property rights and contractual agreements are protected and enforced. To create such an environment, the institutional framework for the implementation of the BOT law requires as a first step all government implementing agencies (IAs) responsible for infrastructure development to have the technical, legal, and financial expertise needed for project identification, design, and implementation.

Institutional strengthening of the IAs helps improve project quality at entry level, an attribute that will facilitate the evaluation and approval process conducted by the inter-agency oversight body, the Investment Coordination Committee (ICC) of the National Economic and Development Authority (NEDA) Board. Meanwhile, the oversight function of the ICC, in coordination with the Infrastructure Committee (Infracom), another inter-agency body of the NEDA Board, may be streamlined and focused on ensuring that any proposed project is consistent with policies of the national government *vis-a-vis* fiscal and investment incentives and procurement.

As important as amending the legal framework is the need to formulate substantive implementing rules and regulations (IRR) with utmost clarity. Moreover, the IRR must be procedurally efficient in enforcing property rights, along with contractual rights and obligations, to bring about a successful PPP.

The rest of this memorandum is organized as follows: In Section II, we spell out some principles that in our opinion are vital in enhancing PPP in infrastructure development. Then as a background, we present in Section III the main provisions of the present BOT law and discuss some of its limitations. We likewise revisit in Section IV the concerns that were reported in Technical Memorandum No. 1. In Section V, we critically evaluate the recently filed House Bill (HB) no. 5002, which aims to amend RA no. 7718. We present and describe in Section VI, the main features of our proposed BOT bill. We summarize and make concluding remarks in Section VII.

## **II. Principles for Enhancing Public-Private Partnership**

### ***Principle 1: Accountability***

The IA, as the procuring agent of the national government, is accountable for the successful commissioning of the project. It takes credit for the success of the project, but its officials directly involved in implementing the procurement contract are liable in case any investigation is warranted by circumstances.

Under the above arrangement, the IA owns the project and as such is also responsible for monitoring the project. It must make sure that the private entity to which the contract has been awarded complies with its obligations and delivers the project specifications that have been agreed upon.

Before the IA awards the contract to a private entity, it must satisfy the requirements of a government oversight body. In the case of BOT projects, this is the ICC. During contract implementation, the IA provides the NEDA as secretariat of the ICC copies of periodic narrative and financial reports about the progress of the project. In case the IA and the private proponent contemplate variations from the awarded contract, existing ICC rules and procedures on variation orders must be observed.

In line with this principle of accountability, the endorsement by the IA of the proposed project to the ICC can constitute the “first pass” provided for in the current rules of the ICC. Approval by the ICC, meanwhile, represents the “second pass.” The ICC then elevates the project to the NEDA Board, chaired by the President of the Philippines, the final approving authority.

## ***Principle 2: Transparency***

The IA observes transparency from start to finish of the procurement process. The same is observed during contract implementation. The ICC, although only indirectly involved in the procurement of the project, must also be held accountable along with the IA in case certain actions taken during the procurement process and during contract implementation are warranted by circumstances to be investigated. The IA shall likewise provide the ICC a copy of the signed contract. Any request from the public for a copy of the signed contract should be directed to the IA.

## ***Principle 3: Fiscal Soundness***

Any claim of the proposed project on government budgetary resources during construction and the entire cooperation period must be clear and well understood. Fiscal soundness dictates that such claim is aligned with the balanced-budget program of the national government over the medium term. In furtherance of fiscal soundness, any proposed project must avoid enlarging the government bureaucracy unduly and imposing new claims on government budgetary resources.

A BOT project is part of the country's social overhead capital that is to be built based on a partnership between the government and the private sector. In view of the public-good features of the project, the government through the IA claims ownership over the project. The government, however, understands that in the interest of the public, the burden of taxation and its associated deadweight losses must be minimized. This goal can be achieved by allowing the private proponent to levy user charges that allow a return commensurate to the opportunity cost of its invested funds. In so doing, users pay for the services derived from the project, thereby easing taxpayers' burden.

In any partnership, the proper allocation of cost- and risk-sharing is crucial. The sharing arrangement must not tolerate any form of opportunistic behavior from either of the two parties involved. Some project costs, for instance, are sunk and rightfully considered undertaking of the government. Such costs, once expended, need not be recovered; any attempt to do so makes user charges prohibitively high, effectively blocking demand for the services of the project. Right-of-way costs for a road project and cost of building the runway for an airport come to

mind. Meanwhile, the private partner must bear and seek proper insurance cover against all market risks, such as, those arising from price and income uncertainty.

Some risks are uninsurable. In this case, the partnership must allow for some form of co-insurance that provides for sharing of the liabilities attendant to the occurrence of an unfavorable state of nature. In other words, the government can provide some insurance cover or guarantee to the project, but it should be able to charge a premium that is actuarially fair

#### ***Principle 4: Financial Viability***

It is in the interest of both the government and the private proponent to ensure the financial viability of the project. Both parties benefit if the project delivers revenues that allow for cost recovery, including, normal profits. This helps achieve uninterrupted service delivery and debt servicing.

Realistic user charges are key to achieving financial viability during the period of cooperation. Hence, the government regulatory body responsible for hearing petitions for user-charge adjustments must act in a timely and decisive manner. It must, however, carefully weigh competing efficiency and equity concerns prior to rendering a decision.

#### ***Principle 5: Institutional Credibility***

The IA in charge of procuring a BOT infrastructure project and the government bodies with oversight or regulatory mandates over the project must be credible and fair. They gain credibility by endorsing and approving only projects that benefit society in the large. They lose it if they develop a reputation of approving projects that benefit mainly some interest groups and the latter's cohorts of employees, suppliers, and subcontractors.

It is understood that to be credible and be trusted by various stakeholders, both the implementing and oversight agencies must invest in people; the agencies must develop a human-resource pool endowed with technical, legal, and financial expertise.

### ***Principle 6: Genuine Commitment to Effective Public-Private Partnership***

An effective PPP hinges on the following: (a) a legal and economic environment that is conducive to a mutually beneficial partnership; (b) clarity in articulating the duties and responsibilities of the parties to the contract; and (c) certainty of recovering investments and availability of mechanisms for dealing with risks and unforeseen events.

PPP is an appropriate framework since it spans a range of options that may be used to deliver infrastructure services. These include service or management contracts, lease, concession, and BOT, including possible variants.

PPP serves both to attract private capital and to mobilize efficient managerial, technical and financial arrangements. Properly structured performance-based concessions, such as, water concessions, can provide cost-effective and sustainable infrastructure services to a wide population base.

### **III. Overview of RA 7718**

RA 7718, to the best of our knowledge, represents the first attempt to develop a comprehensive, stand-alone legislative framework for PPP infrastructure projects in Asia. Subsequently, many other countries have emulated its approach and adopted separate legislation for private-sector investment in infrastructure. Today, this is well observed in many emerging markets worldwide.

Recently, governments have been increasingly relying on the private sector to provide services traditionally undertaken by the public sector. The possibility of pricing infrastructure services and the availability of technologies capable of excluding non-payers from availing of the service have made these arrangements possible. In the Philippines, this has occurred for example, in the Bureau of Immigration's information technology project and the Department of Science and Technology's proposed biotechnology projects. Private entities have proposed projects that seek to unlock value from government asset holdings by permitting, for instance, the commercial exploitation of state-owned land. This may involve the construction of infrastructure, such as, shopping centers and government central headquarters with office accommodation. At the local level, project proposals received by local government units (LGUs) include public food and commodity markets, bus terminals, and shopping centers.

The BOT law comprises 13 sections. The law was amplified in 1994 through amendments that (a) expand the range of contracts that government authorities may conclude; (b) stipulate a procedure for the approval of projects falling within a given cost range; and (c) introduce a procedure for the treatment of unsolicited proposals. The detailed rules and procedures for project preparation, approval, evaluation, bidding, and implementation are enumerated in the IRR that is issued by a committee appointed by the Philippine president. The members of the committee include government oversight and implementing agencies, e.g., NEDA, Department of Finance (DOF), Department of Public Works and Highways (DPWH), Department of Transportation and Communication (DOTC), Department of Energy (DOE), Department of Agriculture (DA), and the BOT Center, which is attached to the Department of Trade and Industry (DTI). The IRR has been updated twice since the first BOT law was adopted in July, 1990.

The BOT law has five main focus areas. Section 1 is a declaration of policy that confirms the private sector's role as the main engine for growth and development of the economy. It also provides for the granting of appropriate incentives aimed at encouraging the private sector to finance the construction, operation, and maintenance of infrastructure and development projects that would otherwise be financed by the government. Incentives proposed in the law include (a) financial incentives; (b) a climate of minimum government regulation; and (c) specific government undertakings.

Section 2 is a list of definitions. A prominent feature is the variety of contractual arrangements for PPP in infrastructure that are individually defined. In its original version, the law mentioned only two contractual forms, namely, BOT and build-and-transfer (BT). In 1994, additional BOT variants were added and defined, namely, BOO, BLT, BTO, CAO, DOT and ROT<sup>1</sup>.

Section 2 contains additional definitions. "Private-sector infrastructure and development projects" are defined listing the areas within which private investment may be sought<sup>2</sup>. It is confirmed here that project finance may be sourced domestically or internationally. In view of

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<sup>1</sup> These abbreviations refer to build-own-operate, build-lease-transfer, build-transfer-operate, contract-add-operate, develop-operate-transfer & rehabilitate-operate-transfer, respectively.

<sup>2</sup> E.g., Power plants, highways, ports, airports, canals, dams, hydropower projects, water supply, irrigation, telecommunications, railroads and railways, transport systems, land reclamation projects, industrial estates or townships, housing, government buildings, tourism projects, markets, slaughterhouses, warehouses, solid-waste management, information technology, networks and database infrastructure, education and health facilities, sewerage, drainage and dredging.

restrictions on the operation of public utilities provided for by the Constitution of the Philippines, the law requires that the facility operator of a public-utility franchise be a Filipino or a corporation that is at least 60% Filipino-owned. A final condition is that no more than 50% of the project cost may be provided through direct government funding or official development assistance (ODA).

Moreover, Section 2 contains separate definitions for: “project proponent”, “contractor”, “facility operator”, “direct government guarantee”, “reasonable rate of return on investments and operating costs” and “construction”.

Section 3 provides the basic authority for government agencies to contract with private-sector entities. The government agencies with contracting authority are listed as follows: government infrastructure agencies, government-owned and controlled corporations (GOCCs) and LGUs. This authority is qualified by the requirement that projects should be “financially viable” and that the contractors should have “extensive experience” in projects of this nature.

Section 4 lays down the procedure for initiating projects for bidding under the law. Government agencies, GOCCs and LGUs, are required to prepare “priority” projects that are included in their respective development programs. These are then advertised every six months as eligible for private financing.

Section 4 also specifies nominal peso limits for the approval of projects under a particular mode. A distinction is made between national projects and projects initiated by LGUs. The NEDA Board is the final approving authority for national projects. Depending on the value of the project, either the NEDA Board or the ICC is responsible for approving a project. Projects above P 300 million, for instance, are approved by the former. Below this amount, the ICC approves the project while the NEDA Board merely notes.

A different approval process applies to projects of LGUs, which have constitutionally enshrined autonomy. The law requires local government projects to be confirmed by various local authorities depending on the total cost of the project. Confirmation is required from municipal government councils (for projects costing up to P 20 million), provincial development councils (for projects costing between P 20 and P 50 million), city development councils (for all projects up to P 50 million), regional development councils (for projects costing between P 50 and P 200 million) and the ICC (for projects costing above P 200 million). While not explicitly

stipulated in the BOT law, final approval of local government projects is vested in the Local Sanggunian as provided for in the Local Government Code (LGC).

Section 5 describes the treatment of unsolicited proposals, a major addition to the amended BOT law. National and local government agencies are allowed to accept unsolicited proposals, subject to certain conditions, namely: (a) the project should involve a “new concept or technology”; (b) may not be part of the list of “priority” projects identified by the agency under Section 4; and (c) no direct government guarantee, subsidy or equity is required. Section 5 also requires the agency to solicit a comparative proposal or what is commonly termed as “Swiss challenge”. The agency receiving an unsolicited proposal after verifying compliance with these conditions, must advertise comparative or competitive proposals for three consecutive weeks and may accept the original proposal if no other proposal is forthcoming after a period of 60 working days. The law gives the original proponent the right to match the competing proposal within 30 working days.

Section 6 outlines the procedure to be followed in project bidding. It directs the head of an infrastructure agency or LGU to advertise approved projects at least once a week in newspapers of general and local circulation for three consecutive weeks. A two-stage/two-envelope bidding procedure must be followed. Consortium bidders are required to present proof that they are jointly and severally liable for the project completion. Withdrawal of a consortium member before project completion may be a ground for contract cancellation.

The section also prescribes the method for evaluating winning bids in the case of BOT, BT and BLT contracts. For a BOT contract, the law requires the bid to be awarded to the bidder whose bid is the lowest based on the present value of its proposed tolls, fees, etc over the fixed term of the project. In the case of a BT and BLT contract, the bid must be awarded to the lowest complying bidder based on the present value of its proposed schedule of amortization payments. There is a proviso, however, that preference must be given to a Filipino “contractor if its bid is equally advantageous to the bid of a foreign “contractor”.

Section 7 outlines the circumstances under which a contract may be awarded through direct negotiation. This is permitted if:

- only one bidder applies for prequalification;
- there is only one pre-qualified bidder;

- more than one bidder is pre-qualified, but only one submits a compliant bid; or
- more than one bid is received, but only one is compliant.

Prospective bidders can appeal their disqualification. Appeals must be directed to the head of the agency in the case of a national project and to the Department of Interior and Local Government (DILG) for a local project. The law also specifies time limits within which appeals must be lodged and acted upon.

Section 8 describes the “Repayment scheme”. This section is wide-ranging and deals not only with the manner in which a project proponent recovers its investment, but also with the regulation of tolls, fees and other charges that a proponent may levy, its maintenance obligations, and various other issues.

The section confirms that a BOT proponent can recover investment in a project by levying tolls, fees and other charges that are “reasonable” and should not exceed those specified in the contract. Repayment can also be done by granting the proponent a revenue share or some non-monetary payment, such as, granting of a share in “reclaimed land”. In the case of a BT contract, the proponent is repaid through amortization payments that follow the scheme proposed in the bid and incorporated in the contract.

Negotiated contracts granting a natural monopoly or contracts where the public has no access to alternative facilities, tolls, fees, and other charges are subject to government regulation based on a reasonable rate of return. The section contains various provisos:

(a) the term for which tolls, fees and other charges may be collected must be fixed in the bid and may not exceed 50 years;

(b) tolls, fees and other charges may be adjusted during the lifetime of the contract using a predetermined formula based on official price indices and included in the instructions to bidders and the contract;

(c) tolls, fees and other charges and adjustments must take into account the reasonableness of the rates to end-users; and

(d) the proponent must undertake the necessary maintenance and repair of the facility during the lifetime of the contract.

Section 9 provides for “contract termination”. It stipulates that if a contract is terminated through no fault of the proponent or by mutual agreement, the government must compensate the proponent the actual expenses incurred plus a reasonable rate of return that may not exceed the rate stipulated in the contract. Government is required to insure this interest with the Government Service Insurance System (GSIS) or an insurer accredited with the Insurance Commission (IC). The bidding terms are required to allow for costs of such insurance.

The section further allows a proponent to terminate a contract if government defaults on “certain major obligations” and (a) the default cannot be remedied; or (b) it can be remedied but the government fails to do so for an unreasonable length of time. Termination must be preceded by prior notice, specifying the effective date of termination. The proponent must be compensated a reasonable equivalent or proportionate cost.

Section 11 provides that each project must be undertaken in accordance with the approved plans, specifications, standards, and costs, and that it is subject to the supervision of the agency or LGU concerned. This should be read along with Section 14, which stipulates that all projects are coordinated and monitored by the Coordinating Council of the Philippine Assistance Program. In 2002, the CCPAP was renamed the BOT Center under EO 144.

Section 13 mandates the issuing of the IRR by a committee. The IRR sets out the criteria and guidelines for the evaluation of bid proposals and list the financial incentives and arrangements that the government may extend to projects. The committee is also mandated to amend the IRR from time to time after undertaking public hearings and publication.

Sections 10, 12 and 15 to 18 contain various miscellaneous provisions. These include Regulatory Boards, Investment Incentives, Coordination and Monitoring of Projects, Repealing Clause, Separability Clause, and Effectivity Clause.

#### **IV. Areas of Concern about RA 7718**

An analysis of the current law and an assessment of some factual and anecdotal evidence surrounding its implementation suggest that there is a need to update and/or amend the current law to address the various issues at each stage of the project cycle, from entry level to implementation and eventual completion.

## ***Project Quality at Entry***

In initiating PPP, the law envisions national and local government agencies to be active in identifying and preparing project opportunities suitable for private investment. This assumes that government agencies have sufficient technical capacity to undertake project preparation.

Envisaged as output of this active project-identification process is a steady stream of “priority projects” of national government agencies and of GOCCs to be listed in the Medium-Term Public Investment Program (MTPIP). The MTPIP is a companion document of the Medium Term Philippine Development Plan (MTPDP), the preparation of which is coordinated by the NEDA. At present, the NEDA and DBM are seeking to synchronize the planning and budgeting process by preparing a three-year rolling capital budget under the MTPIP. The MTPIP forms a large part of the annual capital budget of the national government, fleshed out by the project submissions of various IAs. With regard to LGUs, their priority projects are to be included in their local development plans.

Currently, however, many IAs still lack the capacity for project identification and preparation. This is an area where the Infracom can come in. Under EO 230 (Reorganization of the NEDA), the Infracom’s primary mandate is to advise the President and the NEDA Board on matters concerning infrastructure development. In line with this mandate, it is to formulate policies and programs consistent with national development objectives and to assist IAs in the identification and prioritization of projects for government and PPP support. The Infracom, in coordination with the infrastructure line agencies and the NEDA secretariat, formulates and approves the criteria to be used in the MTPIP prioritization process. Unfortunately, many of the IAs still have to internalize the MTPIP process. Their submissions are still not rank-ordered and are often limited to the usual projects to be funded entirely from the national government budget. With no “priority” status accorded and no planned mode of implementation, infrastructure projects have no choice but to compete against all non-infrastructure projects for the budget’s discretionary part that over the past few years has not been increasing in a meaningful way.

The lack of project identification and preparation capacity has resulted in the inconsistent application of Section 4 (Priority Projects) in the BOT process. It has opened up opportunities for the private sector to crowd out projects that ought to be in the priority list and jurisdiction of the national government. As a result, an unusually large number of unsolicited proposals are

being submitted to government agencies for endorsement to the NEDA in line with the ICC process. Many of these unsolicited proposals, however, are mere attempts to circumvent the law and to avoid competitive bidding through lobbies to delist some projects from the original priority list of the government. This has the effect of rendering a statutory requirement meaningless, a situation that must not persist.

Moreover, most IAs experience difficulty in moving projects from identification to the approval stage. At this stage, their weak technical, financial, and legal capacity to evaluate proposals, especially unsolicited ones, tends to delay project processing and ICC approval. The existing concern about the long approval process, that of requiring a first pass, then a second pass for the contract approval can be effectively addressed by delegating to IAs the first-pass approval. But they must develop the capability to evaluate proposed projects. Once the IAs acquire the needed capacity for a first pass, and are made responsible and accountable for the projects they endorse to NEDA, the approval process can be shortened. For one, the ICC will not need a long time to validate the IAs' submissions. This helps overcome delays in the processing and approval process, thereby restoring private-sector confidence in the BOT process.

### ***Contracts and Regulation***

The law is unspecific about the institutional framework for PPP in infrastructure and lacks clarity in areas like allocation of roles, functions, duties, and risks to be assumed by the IAs and the private parties involved in the BOT process.

There is anecdotal evidence that contract writing, especially for unsolicited projects, is left for the most part to the private proponent. The result is that during negotiations, the IAs may not be adequately informed about the implications of the contractual provisions they have committed to the private partner.

The responsibility of contract writing, including the analysis of the provisions, rests on the IAs. The sections that IAs need to analyze closely include obligations of each party in a project; financial terms (including guarantees, subsidies, or equity to be provided if the project is eligible); and contractual provisions on risk allocation, including assisting the project secure financing and ensuring its financial viability and sustainability. While the project and the contract are subject to the oversight process of the ICC, the latter should not be made chiefly

responsible for determining if the project is technically, economically, socially, and financially viable. This responsibility mainly rests with the IA that owns the project. Under our proposal, the IA provides first-pass approval of the project based on established standards for technical, economic, social and financial viability.

Monitoring of contract implementation throughout the cooperation period is likewise an important responsibility of the IA. To inform the government that the private proponent is fulfilling its obligation under the contract, the IA needs to be updated about any development or issue that may arise and for it to report the same to the ICC for its information or resolution if necessary.

Regulation is also an area that needs improvement. The financial stability of a BOT project rests on the ability of the IA to allow the private concessionaire to charge user fees and implement a fare or use fee-adjustment mechanism under clearly specified conditions. These are also stipulated in the contract. Meanwhile, regulators continue to be challenged in balancing the welfare of the public, on one end, and allowing the private-sector proponent to recover its investment with some reasonable return, on the other. For the private sector to continue supporting government projects, the regulatory bodies must be credible, transparent, and accountable.

To sum up, the rationale for the IAs to obtain sufficient expertise in technical, financial, and legal matters is to enable them to assume the lead in contract negotiations and writing, as well as in monitoring contract compliance during implementation. The government has tried to address this concern when it issued Executive Order (EO) no. 144, converting the CCPAP to the BOT Center in 2002. The modified mandate, however, did not generate the expected result. This suggests that empowering the implementing agencies is requisite to a successful PPP.

### ***Enabling legal and regulatory environment and need for flexibility***

The past experience with BOT implementation indicates the need to provide a clear legal and regulatory framework for PPP in government infrastructure projects. At the same time, such framework must give enough flexibility to the IAs and the oversight body to adjust the rules and regulations governing PPPs that passage of time and specific circumstances may require.

In principle, a primary statute like the BOT law should contain the broad enabling framework for a given sector or activity. It should identify the primary roles, functions, powers, duties and rights of government agencies responsible for project preparation and implementation, as well as oversight over the implementing agencies. A primary statute is also an instrument of policy and should set out the institutional framework within which that policy is to be executed and overseen by the various branches of government. The country's institutional framework for PPPs, we submit, should be clearly stated in the primary statute.

The detailed procedures to implement the law are spelled out in the IRR. Such rules and procedures are normally of a technical or operational nature. Very often they are too detailed to be handled in a primary statute.

As is to be expected, the IRR is amended more frequently than the primary statute. This happens because the practical experience of government agencies in applying the IRR brings out issues that were not anticipated when the primary law was adopted, including, financial innovations, advances in technology and engineering, etc. This is also one reason why contract renegotiation is provided for. The IRR can usually be amended more easily by way of an administrative procedure, thereby avoiding delays that may arise from a usually lengthy and ponderous legislative process.

## **V. A Critique of HB 5002**

We review here the proposed amendments to RA 7718 or the BOT law as contained in House Bill (HB) no. 5002 introduced by Rep. Joey Sarte Salceda. The bill seeks to amend some sections of the BOT law and introduces new provisions designed to encourage PPP in the infrastructure development program of the government, both local and national. The proposed amendments and our comments on them follow:

### ***On Section 1 (Declaration of Policy)***

This section should be kept simple and direct to state the general principle of PPP. The provision as stated in RA 7718 already contains the intent of the law in terms of the rationale for private-sector provision of public services. The second and third paragraphs of the bill are redundant. They are already subsumed in the other sections on provision of government support or approvals. As a matter of policy, the government should explicitly recognize in this

section the need to provide an environment conducive to attracting private participation in government undertakings, even as we note that special government fiscal incentives are not necessarily the primary factor for the private sector to achieve a reasonable rate of return.

### ***On Section 2 (Definition of Terms)***

In this section, the bill introduces many new terms and re-defines and/or clarifies existing ones. The bill proposes transferring BOT variants and their definition from Section 2 of the BOT law to Section 4 of the bill.

We do not support the inclusion of bulk grains handling facility or other logistic support system as part of the eligible *private-sector infrastructure or development projects*. This project group can be undertaken purely by the private sector and the government is well advised not to invest in these types of activities. There is, however, merit in the proposal to remit the government's share for projects partly financed by ODA for the sole purpose of repaying the ODA loans incurred. It is, thus, important to establish a mechanism that helps verify if the stated rate-of-return of the project has been reached to trigger the remittance of the government share to the national treasury.

The bill expands the conditions for the *project proponent* to have adequate financial capacity to implement the project. It now includes a stand-by letter of credit that is sufficient to cover the total estimated cost of the project. While this additional requirement may strengthen the financial capability of the proponent, we note that a stand-by letter of credit is not costless. The private proponent eventually passes this additional cost to end-users. This added feature should be reconsidered since the financial implication may adversely affect investors' interest.

Instead of providing definitions for *direct and indirect government guarantee*, we advise a definition for *government guarantee* in general. Guarantees, direct or indirect, are usually required by the lenders of the project to ensure smooth repayment of loans incurred for the project. The government acknowledges that at times, guarantees are required for the project to push through. We note, however, that government guarantees are contingent liabilities; they become actual liabilities when a particular event spelled out in the contract occurs, or when an IA, say a government corporation, is unable to deliver on its financial obligations that have the "full faith and guarantee" of the government. Once an unfavorable state occurs, it is difficult to pinpoint responsibility. A moral-hazard problem may in fact be at work. Either one or both

parties may have been careless. And so, instead of providing a hundred-percent government guarantee, a co-insurance scheme may be thought of. A co-insurance scheme acknowledges the need for some form of risk-sharing between the parties, and helps mitigate moral-hazard problems.

There have been some controversies about what constitutes a direct and indirect government guarantee, given that the law forbids “unsolicited” BOT projects from availing of direct government guarantee, but could be entitled to an indirect government guarantee subject to the approval of the NEDA Board. Neither RA 7718 nor its IRR clearly specify what is an indirect government guarantee; as a result, private proponents have been able to justify that the assumption of full or partial responsibility of the obligations of the private proponent by any other government institution other than the national government is acceptable. This cannot go on. Whether it is the national government or the government financial institution assuming the obligations of the private proponent to its lenders, such act constitutes a guarantee and the oversight body, in this case the ICC, should declare the project ineligible for guarantee under the unsolicited-project mode.

The bill defines *reasonable rate-of-return* as the prevailing weighted average cost of capital (WACC) plus 6%. We disagree with this definition. The prevailing cost of capital whether in the domestic and international markets already imputes inflationary expectation and a risk premium for investing in a public project, making the additional 6% a veritable rent, an arrangement that is very disadvantageous to the government. Alternatively, to determine the rate-of-return at contract inception, the rate may be inferred from the prevailing yield on a Philippine treasury bill or bond adjusted for the expected depreciation of the Philippine peso over the period of cooperation plus perhaps a liquidity premium. The expected depreciation of the peso may be gleaned from the treasury-rate differential between the Philippines and the US.

The provision of a *government subsidy* is sometimes required to make the project viable. We agree with giving subsidies on a case-to-case basis. In some cases, the subsidy should be treated as taking care of sunk cost. This is cost that once expended need not be recovered. Attempts to recover lead to a prohibitively high price for the service, causing potential customers to shun the service. No mutually beneficial exchange takes place. That is, the market fails. To overcome this failure, the government treats its subsidy as sunk cost and does not try to recover it from the user fees; in other words, the government, through its subsidy, acknowledges the public-good nature of the project. The government, however, continues to discriminate among

BOT projects being proposed and carefully selects the ones that ought to be given subsidy. All this is consistent with assuring the financial viability of the project during the period of cooperation between the government and the private sector.

*Government equity*, meanwhile, is normal in joint ventures and can be defined where the provision on joint ventures appears. The bill also defines *credit enhancements* to mean direct and indirect support, including government guarantees. We maintain that to avoid confusion about what constitutes credit incentives or enhancements and to differentiate them from government guarantee or support, credit incentives or enhancements can be stipulated in the IRR under the section on investment incentives, similar to what appears in RA 7718.

Lastly, the definition of *total project cost* proposes including working capital of six months on top of the cost of the feasibility study, detailed engineering, design construction, equipment, land and right-of-way. We advise caution. The pitfall is double counting. The standard definition of project cost as used in project finance or in financial and economic analysis does include working capital in the determination of project cost. It does not, however, specify the number of months required. Moreover, in the conduct of financial and economic analyses of the project, the working capital is already incorporated in the various cost items, e.g., recurrent costs.

### ***On Section 3 (Private Initiative in Infrastructure)***

The bill is proposing that all national government priority infrastructure projects be submitted to a proposed BOT Authority<sup>3</sup> for approval. LGU projects with the private sector are likewise required to submit to the BOT Authority for information. We disagree with the proposed creation of a BOT Authority. First, it takes over the mandates of implementing, regulatory, and oversight government agencies, raising a host of conflict-of-interest issues. In addition, given the BOT Center's present capacity, the only way for it to discharge its enlarged mandate is to expand its staff, a move that runs counter to current efforts of the national government to streamline the bureaucracy. In view of the fiscal and other constraints that the national government faces, it is difficult to build a sound argument for the proposed BOT authority

To determine whether the project is technically, financially and economically viable as well as socially desirable, there is already an existing inter-agency committee with oversight

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<sup>3</sup> HB 5002 proposes creating a BOT Authority from the existing BOT Center, which is currently under the Board of Investments (BOI), an attached agency of the DTI. The center at present is in charge of promoting PPP projects of both national government agencies (NGAs) and LGUs.

function over BOT projects, namely, the ICC. The DOF chairs the ICC and looks at any government guarantee that may be given to BOT projects. As co-chair, the NEDA sees to it that BOT projects are in the MTPIP. The Department of Budget and Management (DBM) determines the impact of the project on the national government budget and ensures consistency with government procurement policy. The Bangko Sentral ng Pilipinas (BSP) looks at the implications to the money supply and official foreign reserve assets. Lastly, the DTI is in the ICC to determine the eligibility of the project for special investment incentives.

In this context, the proposed BOT Authority merely duplicates the various functions of existing implementing, regulatory, and oversight agencies, and is out of line with the principle of fiscal soundness.

Section 4 in the bill enumerates additional types of contractual arrangements. These additional contractual obligations should be approved by the ICC given the nature of their requirements. This is justified in view of the inability of contracting parties at the time of writing the contract to anticipate all states of nature in the future. Defining individual contractual obligations may prove restrictive and may unduly hamper negotiations over specific contractual provisions.

There are four additional contractual obligations defined in the bill as follows: (a) concession; (b) joint venture; (c) management service contract; and (d) lease of *afferimage*

Under a *concession arrangement*, transfer of ownership of a facility is not usually included in the arrangement. The reference to a possible transfer arrangement of the facility after the concession period should be deleted. On *joint-venture arrangements*, the definition of government subsidy should be incorporated, as this is a major consideration in such an arrangement.

There is also a need to distinguish among the definitions of various arrangements, e.g., concession, lease of *afferimage* and management of service contract, to avoid possible confusion. For example, both concession and lease of *afferimage* involve some rental or concession fee for the operation, management of the facility for an agreed period, and the arrangement can also include some investments or improvements. What is their major difference? These must be sorted out.

The section on *priority projects* proposes an amendment requiring all national government agencies and LGUs that intend to undertake PPP arrangements to submit to a BOT Authority and to a Public-Private Infrastructure Development Committee (PPDIC) the list of projects for PPP. This is required, the bill says, for centralized publication, road-show presentations, and most important, provision of clearance in compliance with the BOT law for the said projects. The need to provide a clearance in compliance with the law is unnecessary. Why should the list, which from time to time is being updated, be cleared? Not much information can be gathered from a list unless substantive information is being provided. At present, all national government agencies are required to submit their prioritized projects for inclusion in the MTPIP. Among LGUs, the local development plans would have included such projects.

It is doubtful whether the above requirements of the bill improve on the existing process for the formulation and review of BOT projects. No doubt there is room for improving the process, but this rests on, one, improving the capacity of IAs to formulate and review BOT projects, not in reducing their role to mere preparation of a list of BOT projects. Two, there is scope for reducing the ICC requirements, thereby, cutting down the timelines for review process before recommending approval by the NEDA Board.

Section 4-A (Unsolicited Proposals) of the BOT law will be Section 5-A in the bill. The latter seeks to amend the law by deleting the conditions to qualify as an unsolicited proposal<sup>4</sup>. It expands the period of the preparation of a comparative proposal to allow potential bidders to challenge the original proponent's unsolicited offer.

We agree that the provision on *unsolicited proposals* is still necessary at this point. By maintaining this provision, the government may be able to tap innovations and technological advances wherein some private proponents hold private property rights. But any edge of the private sector over the IAs may narrow down over time as the latter strengthen their capacity to plan and prepare projects. This is in line with the Organizational Performance Indicator Framework (OPIF) and the corresponding Medium-Term Expenditure Framework (MTEF) espoused by the DBM as it tries to strengthen the links between planning and budgeting. This is further reason to reject the setting up of a BOT Authority. In contrast with OPIF that aims to

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<sup>4</sup> Section 4a of RA 7718 states that if one of the following conditions is met: (a) project is a new concept; (b) no direct government guarantee, subsidy or equity is required; or (c) the government agency or LGU has invited by publication for three (3) consecutive weeks comparative proposal and that no other proposal is received for a period of 60 working days; then the project is qualified to be an unsolicited proposal..

strengthen the capability of IAs for forward planning and budgeting, the bill, downgrades IAs to a mere “post office box” function; this is a disincentive for IAs to own and be accountable for development projects, in violation of the principles of accountability and transparency.

We also support the proposal not to extend any form of government guarantee to unsolicited proposals. We believe that the private proponent should source its revenues solely from user charges, and the government will offer no form of insurance payment on incurred commercial risks that attend the imposition of such charges.

We also recommend a detailed description in the IRR of a government “priority” and a “new” project. For example, we do not agree that merely changing the alignment of an existing light railway project of the government makes the newly aligned project a non-priority or a new project, thereby rendering it eligible as an unsolicited proposal.

The bill sees the BOT Authority spearheading the *public bidding of projects* under Section 5. The bill views the centralization of such function as facilitating the processing, approval and monitoring. We see things differently. The proposal defeats the purpose of having the IAs assume responsibility for their projects. We regard an arrangement, whereby the IAs take the lead in the solicitation of private partner, whether solicited or unsolicited, as the one truly supportive of the objective of making the IAs accountable for their projects.

A provision for direct negotiation of contract, Section 5-A, is being proposed to include the period through which an appeal can be made by disqualified prospective bidders and the period the IA/LGU should act on the said appeal. The indication by the bill of a specific time frame for required actions is aimed at facilitating the process. With the enactment, however, of RA 9184 or the Government Procurement Law, any provision relating to procurement of goods and services under the project should be consistent with this RA. The DBM chairs the newly formed Government Procurement Policy Board (GPPB), furthering the argument for the ICC as the proper inter-agency body to exercise oversight function over BOT projects.

Section 8 of the bill proposes the creation of a Project Development Facility (PDF) that will assist IAs prepare projects under a PPP arrangement. We support the creation of a PDF; we believe it favors the formulation of solicited over unsolicited proposals by raising the capacity of IAs to come up with a robust pipeline of priority projects. Such PDF is also consistent with OPIF. But administering the fund through a steering committee under a BOT Authority defeats

the objective of making the IAs more responsible and accountable for their respective proposals.

The ICC has proposed the creation of a project preparation facility since the late 1990's. The DBM has been supportive, but severe budgetary constraints have hampered the allocation of such funds to the budget of IAs. Following the recent enactment of tax enhancement measures, it may be worthwhile to explore the possibility of including the PDF in the coming budget-preparation exercise or solicit grant assistance from ODA donors to jumpstart the process.

The provision on *Contract Termination* has always been a standard provision in contracts here and abroad. The language for the said provision should be reviewed and tailored to current industry practice. Creditors normally demand provisions on contract termination as a protection. They do not lend to projects unless such provisions are expressed with clarity and sufficiently cloaked with enforceability.

In Section 8, the bill proposes attaching the Toll Regulatory Board (TRB) to the BOT Authority. This must not be allowed. The TRB is a regulatory authority and its proposed transfer to an agency that is supposed to approve PPP projects poses a conflict-of-interest. In fact, the desired policy of the government as stated in MTPDP is to de-link provision of service from regulation of the service.

The bill proposes including a new Section 12 -- *Warranty to Uphold the Validity of the Contract*--that seeks to address the issue of judicial risks faced by PPP projects. Unfortunately, the provision states that the Executive Branch of the Government "may inquire and review the terms and conditions set forth in a previously approved and signed agreement and that it can cause the rescission of the said agreement." This defeats the purpose of minimizing judicial risks. In fact, the latter is heightened since under existing laws, the Executive Branch cannot cause the rescission of a signed contract; this resides in the judiciary,

On the proposal to include a new Section 14 on PPIDC, we likewise reject this. We submit that the ICC continues to be the proper body to recommend the approval of BOT projects. The ICC works closely with the Infracom in establishing the merits of any proposed infrastructure project of the government.

In the interest, however, of facilitating the approval process governing BOT projects, it is useful to streamline the membership of the ICC to include only agencies that look after the financial, technical and economic implications of development projects, whether ODA-funded or through a PPP mode. These would be the DOF, NEDA, DBM, DTI, the BSP, and the office of the legal counsel in the Office of the President (OP) constituting an ICC subcommittee for BOT projects.

To sum up, the institutional framework that the HB 5002 envisions only serves to weaken the mandates of IAs and bypasses the established oversight functions of key agencies. In so doing, the proposed framework suffers from a lack of transparency, accountability, fiscal soundness, financial viability, and credibility.

## **VI. A Proposal for an Amended BOT Law**

We propose that RA 7718 be amended in pursuit of the goal of the government to enhance PPP in infrastructure development, in general, and promote the use of BOT schema and its variants, in particular. In this regard, observance of the principles enunciated in Section II above is essential.

In addition, the legal framework we are proposing must be conducive to the protection and enforcement of property and contractual rights, backed by a substantive IRR of maximum clarity. To make the IRR operationally efficient, some institutional reforms are indicated.

IAs must be empowered to render a first-pass approval in line with the desire to make them assume project ownership. Capacity building aimed at raising the technical, financial, and legal expertise of the IAs is crucial. Meanwhile, the oversight function the ICC exercises over BOT projects may be delegated to a subcommittee whose membership may be stipulated in the IRR. The requirements for a second-pass approval to be retained by the ICC should be focused on aligning any form of government support being contemplated with the existing policies on government procurement, and special fiscal and investment incentives,

Herewith, the main strategic approaches we propose to strengthen PPP and use of BOT:

- *Transforming RA 7718 into the principal legal framework for PPP in the Philippines:* The policy declaration in the law must explicitly say that PPP is the state policy in infrastructure development. In this regard, the role of the NEDA Board as approving authority must be upheld.
- *Emphasizing that competitive-bidding procedures remain the central tenet of government procurement policy.* Competitive bidding enables the government to get value for its money. The law should thus forthrightly express the government's preference for competitive bidding, and affirm that direct negotiation remains the exception.
- *Asserting the sanctity of contract:* Human welfare emanates for the most part from mutually beneficial exchanges made possible by markets guided by a decentralized price system. And all exchanges are governed by contracts, whether explicit or implicit. Large infrastructure projects are always governed by explicit contracts. Hence, the law must affirm government's binding commitment to honor and defend contractual rights and obligations. The law must also counter ruinous attack on contracts--especially after a relatively long period of time has elapsed since the contract was signed--by limiting options to annul contracts on procedural grounds. This includes providing for greater transparency with regard to the content of contracts. (This assumes that IAs are assigned the responsibility to write and evaluate contractual provisions.)
- *Providing legal recognition to the importance of building PPP implementation capacity at all levels of government and raising overall project quality:* The entry point of the private sector in partnering with the government in an infrastructure project is at the level of the IAS. In view of this, the framework emphasizes the importance of building and rebuilding capacity for project design and implementation within an implementing agency.
- *Ensuring the formulation of a substantive and operationally efficient IRR:* Granting that the desired legal framework has been set up, the IRR with the desired features follows as a matter of course. The operational details must facilitate smooth implementation with hardly any contractual dispute requiring court intervention emerging.

The table below shows the sections of the law that can be relegated to the IRR:

Sec 1: Declaration of Policy	Retain in law with amplification
Sec 2: Definition of Terms	Replaced with a new section (Scope of PPP Contractual Arrangement)
Sec 3: Private Initiative in Infrastructure	Retain in law
Sec 4: Priority Projects	Retain in law with amendment Relegate approval limits to IRR.
Sec 5: Unsolicited Proposals	Subsume under Section on public bidding; unsolicited mode can be undertaken under exceptional cases.
Sec 6: Public Bidding of Projects	Re-affirm in the law the principle of competitive bidding as the principal means of procuring private investment. Law also needs to confirm the principle of publication of contract terms and notification to Congress  Relegate provisions dealing with (a) advertisement of project opportunities; (b) financial criteria for identifying winning bids; (c) liability of bidders; and (d) bidding procedures to IRR
Sec 7: Direct Negotiation of Contract	Subsume under section on public bidding of projects, Reaffirm principle that direct negotiation may be entered into only in exceptional circumstances (subject to appeal and safeguards) in law. Relegate provisions dealing with the circumstances under which direct negotiations may be entered into to IRR.
Sec 8: Repayment Scheme	Relegate to IRR
Sec 9: Contract Termination	Reaffirm in the law the principle of government liability for no-fault contract termination.
Sec 10: Regulatory Boards	For deletion
Sec 11: Project Supervision	Subsume/incorporate in the Section on monitoring
Sec 12: Investment Incentives	Retain in law but should be made consistent with Omnibus Investment Code/Investment Priorities Act
Sec 13: Implementing Rules and Regulations	Retain in law with streamlined membership
Sec 14: Co-ordination and Monitoring	Retain in law to include auditing

The BOT bill that we propose is attached as Appendix 1.

## VII. Summary and Concluding Remarks

The financing requirements of the Philippine infrastructure development program are huge. To meet these in a fiscally constrained environment, the government must rely on strong PPP arrangements. This calls for some amendments to the existing BOT law (RA 7718) backed by a substantive and operationally efficient IRR.

The proper legal environment for a strong PPP is a credible commitment to property and contract rights. To achieve least-cost purchase from an array of quality-compliant proposals, competitive bidding is a must. The use of any other form of bidding must be consistent with the recently enacted procurement law of the government.

The institutional arrangement we propose to achieve the desired PPP entails making the IAs largely responsible and accountable for their respective BOT projects. This means raising the technical, financial, and legal capacity of the IAs. The role of the ICC, the inter-agency body with oversight function over BOT, can then be streamlined and focused on ensuring consistency with existing policies of the government on investment and other special fiscal incentives, and on government procurement.

Any proposed amendment to an existing law usually involves a long deliberative political process. The goal of enhancing PPP need not be compromised by this political reality. Some Executive actions can be taken and incorporated in the IRR with dispatch. For example, capacity building for the IAs can start following the emerging framework for forward planning and budgeting by the national government. The Infracom is well-equipped, and can be convened soonest, to pass judgment on the government's priority list of projects, BOT or otherwise. At the same time, limiting BOT oversight to a subcommittee of the ICC can be expedited; it is aligned with the ongoing rationalization program of the national government.

The recent improvement in the fiscal position of the national government after the enactment of the expanded and rate-enhanced value-added tax measure is opportune for updating the infrastructure priority list. Meanwhile, in line with the provisions of the LGC on internal revenue allotments (IRA), the national government must insist that LGUs use a part of their development funds for infrastructure investments, even as the national government seeks to expand LGU access to concessional financing for infrastructure.

## Appendix 1

### A Bill Seeking to Amend Republic Act no. 7718

#### Section 1. Declaration of policy.

1. It is the policy of the State to:

- a. recognize the indispensable role of the private sector as the main engine for national growth and development;
- b. create an enabling environment for public-private partnership (PPP) projects, that is, private-sector investment in public infrastructure for efficient provision of public services;
- c. recognize the long-term nature of private investment in infrastructure and services and to mitigate the associated risks by ensuring that the validity and enforceability of contracts are respected through the due process of law;
- d. encourage private investment in public infrastructure and/or public services that:
  - (i) yields value for money for the State by allocating risks to the party best able to manage them;
  - (ii) is affordable in light of overall budgetary sustainability, forward commitment in relation to public expenditure and the potential returns on private-sector investment;
  - (iii) maximizes the benefits of private-sector efficiency, expertise, flexibility and innovation;
  - (iv) is financially viable; and
  - (v) is desired in light of economic and social benefits and costs;
- e. ensure a clear and transparent allocation of roles and functions between the oversight and implementing agencies at the national level to ensure the effective implementation of this Act and to encourage the same at local government level;
- f. secure private investment through open and competitive bidding procedures and to permit non-competitive procedures only in exceptional circumstances as allowed by this Act, its Implementing Rules and Regulations (IRR), and consistent with the provision of RA 9184;
- g. ensure a consistent approach among government agencies at both national and local levels in the identification, design, assessment, solicitation and management of projects;
- h. build the capacity of government agencies and local government units (LGUs) to avail themselves of investment opportunities under this Act;

- i. review regularly the progress of the achievement of this policy and to report to Congress on the same.
2. The NEDA Board shall oversee the implementation of this state policy by all agencies of government at the national and local levels and shall submit an annual report to Congress on the progress achieved. To this end, the NEDA Board, through the Investment Coordination Committee (ICC), shall request national agencies and local government units to submit progress reports of PPP projects.
3. The NEDA Board shall issue the IRR consistent with the provisions of this Act and on any matter it deems appropriate to assist with the implementation of policy. The IRR shall be published in the *Official Government Gazette* and Congress shall likewise be notified of the same within one (1) month of the IRR's publication.
4. For the purpose of this section and subsequent reference in the following sections, "government agency" refers to implementing agencies of the national government, including, government-owned and controlled corporations.

## **Section 2. Scope of Contractual Arrangements**

Government agencies and LGUs may select from the list of contractual arrangements provided below. Each agency, however, may adopt other contractual arrangements that may be decided upon during contract negotiations. New contractual arrangements not listed under this Act may be adopted but shall be approved by the ICC.

**a. *Build-operate-and-transfer (BOT):*** A contractual arrangement whereby the project proponent undertakes the construction, including financing, of a given infrastructure facility, and the operation and maintenance thereof. The project proponent operates the facility over the fixed term during which it is allowed to charge facility users appropriate tools, fees, rentals, and charges not exceeding those proposed in its bid or as negotiated and incorporated in the contract to enable the project proponent to recover its investment, and operating and maintenance expenses in the project. The project proponent transfers the facility to the government agency or LGU concerned at the end of the fixed term which shall not exceed fifty (50) years: Provided, That in case of an infrastructure or development facility the operation of which requires a public-utility franchise, the proponent must be Filipino or, if a corporation, must be duly registered with the Securities and Exchange Commission (SEC) and owned up to at least sixty percent (60%) by Filipinos.

"The build-operate-and-transfer shall include a supply-and-operate situation, which is a contractual arrangement whereby the supplier of equipment and machinery for a given infrastructure facility, if the interest of the Government so requires, operates the facility providing in the process technology transfer and training to Filipino nationals.

**b. *Build-and-transfer (BT):*** A contractual arrangement whereby the project component undertakes the financing and construction of a given infrastructure or development facility and after its completion turns it over to the government agency or LGU concerned, which shall pay the proponent on an agreed schedule its total investments expended on the project, plus a reasonable rate of return thereon. This

arrangement may be employed in the construction of any infrastructure or development project, including, critical facilities which, for security or strategic reasons, must be operated directly by the government.

**c. *Build-own-and-operate (BOO)*:** A contractual arrangement whereby a project proponent is authorized to finance, construct, own, operate and maintain an infrastructure or development facility from which the proponent is allowed to recover its total investment, operating and maintenance costs plus a reasonable return thereon by collecting tolls, fees, rentals or other charges from facility users: Provided, that all such projects, upon recommendation of the ICC, shall be approved by the President of the Philippines as chair of the NEDA Board. Under this project, the proponent that owns the assets of the facility may assign its operation and maintenance to a facility operator.

**d. *Build-lease-and-transfer (BLT)*:** A contractual arrangement whereby a project proponent is authorized to finance and construct an infrastructure or development facility and upon its completion turns it over to the government agency or LGU concerned on a lease arrangement for a fixed period after which ownership of the facility is automatically transferred to the government agency or LGU concerned.

**e. *Build-transfer-and-operate (BTO)*:** A contractual arrangement whereby the public sector contracts out the building of an infrastructure facility to a private entity such that the contractor builds the facility on a turn-key basis, assuming cost overrun, delay, and specified performance risks.

"Once the facility is commissioned satisfactorily, title is transferred to the implementing agency. The private entity, however, operates the facility on behalf of the implementing agency under an arrangement.

**f. *Contract-add-and-operate (CAO)*:** A contractual arrangement whereby the project proponent adds to an existing infrastructure facility which it is renting from the government. It operates the expanded project over an agreed franchise period. There may, or may not be, a transfer arrangement in regard to the facility.

**g *Develop-operate-and-transfer (DOT)*:** A contractual arrangement whereby favorable conditions external to a new infrastructure project, which is to be built by a private project proponent, are integrated into the arrangement by giving that entity the right to develop adjoining property, and thus, enjoy some of the benefits the investment creates such as higher property or rent values.

**h. *Rehabilitate-operate-and-transfer (ROT)*:** A contractual arrangement whereby an existing facility is turned over to the private sector to refurbish, operate and maintain for a franchise period, at the expiry of which the legal title to the facility is turned over to the government. The term is also used to describe the purchase of an existing facility from abroad, importing, refurbishing, erecting and consuming it within the host country.

**i *Rehabilitate-own-and-operate (ROO)*:** A contractual arrangement whereby an existing facility is turned over to the private sector to refurbish and operate with no time limitation imposed on ownership. As long as the operator is not in violation of its franchise, it can continue to operate the facility in perpetuity.

### **Section 3. Private Delivery of Public Infrastructure and/or Services.**

1. A government agency or LGU may contract with the private sector for the delivery of public infrastructure and / or services in any of the following areas:

- a. energy, including oil and gas;
- b. transport, including railways, roads, tunnels, bridges, ports, canals, channels, airports, pipelines;
- c. water, including, water storage and wastewater;
- d. communications;
- e. information technology;
- f. education;
- g. health;
- h. tourism;
- i. culture, sports, and leisure facilities;
- j. government buildings, industrial estates and townships, and housing;
- k. markets, warehouses, and slaughterhouses;
- l. any other area as may be prescribed.

2. Contractual arrangements that may be utilized for the purposes of projects contemplated in Section 2 shall be determined during the negotiations between the government agency or LGU, on one hand, and the private sector, on the other.

3. For the purpose of this section and subsequent reference in the following sections, "prescribed" means prescribed in the IRR issued in terms of this Act, except as otherwise indicated.

### **Section 4. Project Preparation.**

1. Each government agency or LGU shall within its area of responsibility prepare a project for approval by the approving authority contemplated in Sec 5 in the manner as prescribed.

2. Prior to preparing a project for approval, the head of the responsible government agency or LGU shall review or assess:

- (a) the risks associated with the proposed project taking into account the various methods for sharing these risks; and
- (b) the economic and financial feasibility of the proposed project, including, a comparison of the costs and benefits of implementing the project in terms of this Act with the costs of implementation in another form.

3. A government agency or LGU that lacks the capacity to prepare a project in the manner as prescribed (including the pre-bidding, bidding and contract management stages of the project) can tap the Project Development Facility (PDF). The PDF will be a fund whose start-up money will come from the national government budget or where feasible, grants from donors of official development assistance (ODA). In the case of a government agency, the PDF shall be appropriated within its budget ceiling, to enable the government agency to solicit assistance or expert advice as necessary. In the interest of sustainability, the winning bidder for a PPP project shall be required to compensate for the cost the government agency expended in

developing the proposal. In the case of LGUs, the DOF shall act as custodian of the PDF and the winning bidder for a LGU-initiated PPP project shall likewise compensate the cost expended in developing the proposal. In the event that resources from the PDF are unavailable to render the required assistance within the prescribed period, the government agency or LGU shall report the same to the ICC and NEDA Board, respectively.

4. The NEDA Board, upon receiving such report, shall:

- (a) request the Department of Budget and Management (DBM) to allocate alternative resources from within government to assist the government agency;
- (b) seek such additional resources as may be available to government to assist the government agency or LGU; or
- (c) based on the overall priorities of the Medium Term Philippine Development Plan (MTPDP) and the government agency's prioritized projects appearing in the Medium-term Public Investment Program (MTPIP) or in the LGU's local development plan, direct the government agency, or request the LGU to re-prioritize its programs and project, or delay the project until the budget required for the proposed project can be accommodated;

5. The NEDA Board shall communicate its decision under subsection (4) to the government agency within 30 days and shall report thereon in its Annual Report contemplated in Section 1.

6. The NEDA Board may, in writing, delegate its powers under this section to the ICC.

## **Section 5. Approving Authority**

1. A national government agency that has identified and prepared a project in the manner specified in Sec 4 shall:

- (a) be required to endorse through the head of the government agency, the project proposal and contract to the ICC. This endorsement shall serve as the first-pass approval for the project and draft contract. All government agencies are required to review the technical, legal, financial, economic and social implications of the project and approve the same prior to endorsement to the ICC.
- (b) submit projects of major national importance with a contract value above an amount as may be prescribed, to the NEDA Board for approval; all other projects to the ICC for approval.

2. All local government PPP projects shall be approved following the provisions of the Local Government Code.

## **Section 6. Implementing, Monitoring, and Auditing Functions.**

1. A government agency or LGU that has secured approval for a project in the manner contemplated in Sec 5 shall be responsible for the implementation, management, and

supervision of the project. Regular monitoring reports shall be submitted to the ICC for its information.

2. Regular auditing shall likewise be conducted following Commission on Audit (COA) guidelines. Reports may be requested from the respective government agency, LGU, or COA as deemed necessary.

## **Section 7. Competitive bidding procedures.**

1. Competitive bidding procedures shall apply to all projects for which private investment is solicited in terms of this Act.

2. Under exceptional cases, government agencies may resort to direct negotiations under such conditions prescribed in Section 53 of RA 9184. LGUs may resort to direct negotiations under conditions prescribed in the Local Government Code and/or RA 9184 as applicable. Such conditions shall include a requirement that the government agency or LGU must give public notice in the prescribed manner of:

- (a) the intention to enter into direct negotiations ;
- (b) the conclusion of negotiations to enter into a contract through direct negotiation; and
- (c) the salient terms of the contract to be concluded.

3. A government agency may only entertain an unsolicited proposal provided that such proposal is not contained in its prioritized projects in the MTPIP. In the case of LGUs, an unsolicited proposal may be entertained provided it does not appear in the local development plan of the LGU concerned.

The other conditions for considering an unsolicited proposal are as follows:

- (a) the government agency or LGU has notified in writing the approving authority within seven (7) working days of the receipt of the proposal;
- (b) the head of the government agency or head of the LGU has conducted an assessment as contemplated in Section 4(2) and has certified in writing to the approving authority that it is capable of conducting all proceedings relating to the proposal;
- (c) the head of the government agency or LGU certified in writing that the proposed project serves the public interest;
- (d) the proposal does not entail the provision of any form of government guarantee, subsidy, or undertakings as may be prescribed;
- (e) the proposal complies with such requirements for unsolicited proposals as may be prescribed; and

- (f) the proponent has indicated its costs for developing the proposal in the prescribed manner.

4. Notwithstanding compliance by any government agency or LGU with the provisions of subsection (3), the ICC may direct a government agency or LGU not to proceed with its consideration of an unsolicited proposal until such time as the latter satisfies the approving authority that:

- (a) it has access to adequate resources to properly assess the proposal, to conduct the evaluation of comparative proposals, to conduct negotiations and to oversee implementation; and
- (b) the proposal meets such requirements related to the public interest as may be prescribed.

5. All unsolicited proposals shall be subject to comparative proposals, after approval by the approving authority, in the manner as may be prescribed.

6. A government agency or LGU during its negotiations and before issuing a request for comparative proposals, negotiate with the proponent that it be compensated for the cost of developing the proposal and to submit the proposal to competitive bidding procedures. The government agency or LGU shall introduce, as part of the bidding conditions, a requirement that the winning bidder (if not the original proponent) be reimbursed for its costs in developing the proposal or for such amount as the government agency or LGU and the proponent may agree beforehand in writing.

5. Non-compliance with the provisions of subsection (3) shall be a ground for declaring a contract null and void.

## **Section 8. Contracts and Public Disclosure**

1. Copies of all contracts concluded in terms of this Act shall be the responsibility of the government agency or LGU. The said government agency or LGU is required to forward a copy of the signed agreement to the ICC for records purposes.

2. The grant of access to the signed agreements by the public shall be the responsibility of the government agency or LGU.

## **Section 9. Validity of contracts**

1. No party may, in proceedings before any court, allege the invalidity of any contract concluded under this Act on the grounds of non-compliance with the provisions of this Act or its IRR after a period of 90 days has elapsed from the date of publication of the approval of the government-procured project in the *Official Gazette*.

## **Section 10. Contract Termination**

1. In the event that a project is revoked, cancelled or terminated by the Government through no fault of the project proponent or by mutual agreement, the project proponent shall be compensated by the government as provided for in the contractual agreement.
2. In cases where the government defaults on certain major obligations in the contract and such failure is not remediable or if remediable shall remain unremedied for an unreasonable length of time, the project proponent may, by prior notice to the concerned government agency or LGU, specifying the turn-over date, terminate the contract. The private proponent shall likewise be compensated by the Government according to the provisions of the contractual agreement.

## **Section 11. Investment promotion**

1. The status of the BOT Center as a unit attached to the Department of Trade and Industry (DTI) is hereby confirmed. The Center shall, henceforth, be known as the Public-Private Partnership Center (PPPC).
2. The main responsibilities of PPPC include:
  - (a) promote and market the government's private-sector investment program, including the formulation and implementation of a promotion and marketing plan, providing service as an information center for investors/developers, as well as for government agencies;
  - (b) participate in the technical working group (TWG) that may be established by the IRR Committee;
  - (c) perform business development and investment-related activities in support of the other functions and mandate of the DTI; and
  - (d) perform such other functions as may be prescribed under the IRR.

## **Section 12. Liability**

In accordance with Section 38, Chapter 9 of the Administrative Code, the head of the government agency shall not be held liable for any bona fide act or omission undertaken for the purposes of implementing this Act or its IRR unless there is a clear showing of bad faith, malice, or gross negligence.

## **Section 13. Implementing Rules and Regulations**

1. The IRR issued in terms of Republic Act No. 6957 as amended by Republic Act No. 7718 remain in force until repealed in terms of this Act.
2. The IRR committee may, subject to the approval of the NEDA Board and after conducting public consultations and publication as required by law, issue the IRR to provide for

the implementation of this Act in the most expeditious manner. The committee may, as needed, update such IRR from time to time.

3. Without limiting the generality of the foregoing, the IRR may provide for -
- (a) contractual arrangements and repayment schemes that may be entered into under this Act;
  - (b) areas in which private investment may be solicited;
  - (c) institutional arrangements for bid management;
  - (d) manner of preparation and content of documents, including, clarifications and pre-bid conferences;
  - (e) qualification of proponents, contractors, bidders and facility operators;
  - (f) procedures for competitive bidding;
  - (g) procedures for direct negotiation;
  - (h) procedures for unsolicited proposals;
  - (i) contract negotiation and award;
  - (j) contract approval and implementation;
  - (k) investment incentives, government guarantees, support, and undertakings;
  - (l) contract management, coordination, monitoring, and auditing;
  - (m) the powers, functions and duties of concerned agencies;
  - (n) any other matter required for the expeditious implementation of the Act.

4. For the purposes of this section, "committee" means a committee appointed by the President comprising one representative from each of the following-

- a. the Department of Public Works and Highways (DPWH);
- b. the Department of Transport and Communications (DOTC);
- c. the Department of Energy (DOE);
- d. the Department of Trade and Industry (DTI);
- e. the Department of Finance (DOF);
- f. the Department of Interior and Local Government (DILG);
- g. the National Economic and Development Authority (NEDA); and
- h. the Department of Budget and Management (DBM); and
- i. the Office of the President (OP).

#### **Section 14. Repeal Clause**

All laws or parts of any law inconsistent with the provisions of this Act are hereby repealed or modified accordingly.

#### **Section 15. Separability Clause**

If any provision of this Act is held invalid, the other provisions not affected thereby shall continue in operation.

#### **Section 16. Effectivity Clause**

This Act shall take effect fifteen (15) days following its publication in the *Official Gazette* and in at least two (2) newspapers of general circulation.