

June 12, 2008

FY08 NLTA Status Completion Note**A. Task Objectives**

1. The Government of India (GOI) has established a Task Force (TF), constituting members from various ministries and Public Sector Undertakings and headed by a representative of the Department of Economic Affairs (DEA), to lead work in review and modifications of the bidding documents that are currently used for World Bank (WB) funded projects so that they are in-line with the changes made at the World Bank. The work of the Task Force is also expected to define ways to address obstacles to efficient procurement outcomes. The Non-Lending Technical Assistance (NLTA) is designed to provide support to the Task Force in carrying out its work.

In accordance with the NLTA Inception Note the activities that are expected to occur as a part of this NLTA include:

- a. Technical assistance, by way of liaison and technical support during review process and in respect of incorporating the agreed modifications of documents to be used in Bank-funded projects in India, pursuant to the revisions in Bank's SBDs.
 - b. Technical assistance in understanding the real import of and development of options/ remedies/ measures to eliminating obstacles to effective procurement in World Bank funded projects that have been identified during the course of various portfolio reviews and other discussions between the World Bank and the GoI.
2. The NLTA has been scheduled to be completed by the end of September 2008 with the FY08 delivery by the end of May 2008.
 3. This completion note summarizes the Activities and Outputs of this task in Section B and the assessment of the work done under this task in Section C.

B. Task Activities and Outputs

4. The Task Force was established by the Department of Economic, PMU Division, of the Ministry of Finance in India. The TF included Sub-committees responsible for the review of SBD for Goods, Works, S&I and SRFP for Selection of Consultants.
5. The NLTA supported the Bank's dialogue with the TF to clarify the Bidding Documents, discuss specific issues pertaining to the projects in India and agree on the use in the Bank-financed project of the Bank's standard bidding documents for ICB with the minimum changes and those reflecting the specific needs of the projects.

6. Review and comments of the Task Force on the Bank's SBDs

The Task Force examined the versions of the SBD for Goods, Works, Consultants and S&I (2004 or 2005 whichever version was available when the TF started its review), which are compliant with the May 2004 WB Procurement Guidelines and which have been harmonized with the documents used by other International Financing Institutions. The TF provided to the Bank, in its Report received in the Bank on May 1, 2007, with subsequent addition/ modifications in June 2007, its comments for each document it reviewed.

The Bank divided the task into two, separating the comments of the S&I SBD given the bulkiness of those comments.

In September 2007 the Bank's Team prepared and shared with TF the WB SBD Discussion-Starting Paper that contained preliminary responses to the TF's comments with the intent that the document would help guide the discussion during the planned meeting with TF and facilitate achieving a joint understanding between the Bank and the TF on the issues at hand. This paper contained responses for the task related to the comments on the Goods, Works and Consultants documents.

The dialogue with the TF and the deliverables are described below.

6.1 Dialogue of the Bank with the Task Force

6.1.1 SBDs

The Bank's representatives¹ visited the TF Chairman, Mr. Nagaraju, on December 18, 2006. Though the review was planned to be completed by November 2006, at the time of the meeting only the review of the SBD for Goods was completed by the subcommittee of the Task Force and not yet discussed internally. Therefore, Mr. Nagaraju could not discuss the SBDs with the Bank's delegation. The Bank's representatives made the reference to the Transport Workshop held in 2004, which had focused on the issues that were raised by the various state Government agencies as well as contractors and consultants providing services for implementing various projects in the Transport sector. Some important issues that are still valid were raised then and the Bank's representatives suggested that TF looks at these issues to find the best solution to address them.

During the meeting views on some commonly occurring issues in the procurement process and contracting, were discussed. The Bank's delegation raised some issues and provided their opinion to bring these issues to the attention of Mr. Nagaraju. These issues are presented in the section below.

Following receipt of the TF's comments on the Bank SBDs, the Bank's Team and TF agreed to meet and discuss these comments. The expected outcome of the meeting is to have a common understanding of the TF's concerns related to the procurement in India, how

¹ Mr. Sunil K. Bhattacharya, Ms. Elzbieta Sieminska, Mr. Manmohan Singh Bajaj

they can be addressed under the Bank's procurement policies and to define the next steps.

The meeting was held on October 8, 2007 in DEA of the Ministry of Finance in New Delhi. The TF was represented by the members of all its subcommittees and the WB was represented by Ms. Elzbieta Sieminska and Mr. Manmohan Singh Bajaj. This meeting was followed by a preliminary meeting with the members of the TF responsible for the comments on SBD for Supply and Installation. This section of the TF Report being voluminous, the discussions could not conclude with TF and need be followed up later.

All comments provided by the TF on the SBDs for Goods, Works and SRFP for Selection of Consultants were discussed. A number of issues raised by the TF were clarified. Some points were taken for providing changes in the SBDs/ SRFP. However, some issues remained unresolved and were taken by the Bank's Team for discussion with the Management. These issues related to the venue of arbitration, the way of appointing the auditor in case of the Bank's right to audit the procurement process and the contract, and an additional provision on confirmation by the bidders to observance of the India Anticorruption Law (1988), which was proposed by the TF since this was an existing insertion in documents as were in use based on agreement with an earlier Task Force. On the first two issues, the Bank's and TF's positions differed while, following the clarifications provided by the TF, the last one required the Bank's legal opinion.

Though the Health Sector SBDs were not directly addressed at the October meeting, TF informed that their comments to SBDs for Goods are equally applicable to the Health Sector SBDs and that, aside from these, TF has offered no comments on the Health Sector SBDs. Further, TF informed the Bank that they had neither questions nor concerns following its review of the Bank's Pre-Qualification Document

Other procurement issues

During the meeting on December 18, 2006 the Bank's delegation raised the following issues:

- a. NCB exceptions: the use of NCB under the Bank-financed projects had been agreed with the Government of India, which provide for use of bidding documents that are in use by the implementing agencies, but that would comply with Bank procedures. Broadly, there is an agreed list of exceptions to the procedures used in open tender in India. Upon the DEA's request made in the past for the India projects the list of the exceptions is included in the Minutes of Negotiations, at the time of project preparation and loan negotiations. The Bank's representatives requested DEA to reconsider including them in the Financing Agreement. It would make monitoring the States' performance by the DEA easier. In addition, the Bank's representatives indicated the need to review the current list of the NCB exceptions in the light of the changes in the law. In 2005 new General Financial Rules (GFR) were adopted at the central level and some States. Some States also adopted new procurement laws.
- b. Suo motu discounts: there is common practice in India that the bidders may (and do) offer voluntary (suo motu) discounts after the bid submission, either at the evaluation stage or after the contract award. This practice has been creeping onto the procurement process under the Bank-financed projects. The Bank's representatives explained that this practice violates the Bank's procurement Guidelines. Depending on the stage this discount is offered it may be interpreted as either bid alteration, bracketing or negotiations and may raise the question if

- there is a downward trend in price; otherwise why the lowest bidder would reduce its price voluntarily. Given that the cost estimates are often outdated while they are the target to achieve through the suo motu discounts, such price decreases lead to decrease of the delivered quality and undermines the transparency of the process. It may lead other higher prices to reduce their prices voluntarily. This is a serious violation of the Bank's Procurement Guidelines that say that no bidder should be allowed to change the substance or price of its bid after the bid submission deadline.
- c. Two-envelope system: this system deviates from the Bank's Guidelines and its consideration of transparency not to mention the perception of its abuse. The prices should be read out publicly immediately after the deadline for bid submission. The TF is requested to raise it with the Borrowers in order for them not to use the two envelope system under the Bank-financed projects. The Bank's representatives suggested also that the GOI should also consider not using it in their own procurement as well. However, presently this practice is almost uniformly followed in the procurement undertaken by the various state entities. About three years ago when GOI requested the Bank to consider possibility of using this system, the Bank suggested DEA to agree on a comprehensive study to evaluate the impact of this system and to determine pros and cons of this procedure.
 - d. Assignment: Some Borrowers split the S&I contract into three, goods, works and transport, with the cross-bridged responsibility. This is understood to be for reasons of affecting savings in applicable taxes, as the application of sales tax and works contract taxes are often interpreted by various state authorities differently, being a state subject. While the bidding procedure is for the entire S&I scope, the winning bidder is required to assign contracts/ or sign several split contracts, as explained above. Splitting of contract elements for tax purpose is unjustified and is not a good practice. This leads to a very complex contractual arrangement and can be difficult to manage as opposed to a single contract with single point responsibility of one contractor; and can easily result in the implementation problems. The Bank's representatives requested that TF clarifies this with the Tax Authorities. The S&I contract includes separate Price Schedules for Goods, Installation (Works) and Transport and each of these elements can be taxed separately.
 - e. Dispute Resolution Board: The Bank's representatives reiterated the importance of using DRBs in the large works contracts. This facilitates dispute resolution and minimizes the costs. The DRB members have technical knowledge and are respected members of the professional community. In India the DRB is often challenged though, as the study on DRB shows, the DRB decision usually is sustained. This leads to loss of time, increased cost and loss of trust in the industry. The Bank's representatives offered that the Bank would be willing to provide assistance and to work together with the GoI to explore achieving better performance of DRBs and acceptance of their decisions in the context of faster resolution of disputes that arise during implementation enabling faster delivery/ completion.
 - f. Deviations: The Bank's representatives informed Mr. Nagaraju of instances where bidders specified the deviations to the bidding requirements in eg. cover letter instead in their bid. The cover letter needs to be considered together with the bid while in some cases the Borrowers refuse to do so. This results in omitting the reservations and deviations included by the bidders in the cover letter.
 - g. Slice and package evaluation: The Bank's representatives reiterated and suggested to pay more attention to package homogenous contracts as lots (slices) into packages and invite cross-discounts, which could bring down prices for such procurements and encourage both

smaller and larger contractors to bid. Further the lots are evaluated in combination to establish the lowest evaluated combination of contracts for award. While slicing into lots allows more competition, packaging increases economy of the process.

- h. Cases referred to the High Court: The Bank's representatives informed instances where certain contracts under ICB were referred to the High Court which ruled against the provisions the Bank's Guidelines. The Bank's representatives suggested that DEA TF checks with the Ministry of Law how the national ruling would be considered in relation to the application of the Bank's Guidelines given that the Financing Agreement signed with the WB is an international treaty.

7. WB response to the Task Force's comments on the Bank's SBDs

Following the meeting with DEA in October 2007, several issues were referred to OPRC for advice given the position of the DEA TF opposing the Bank's position. OPRC referred a couple of issues to the Procurement Sector Board and appropriate changes to the SRFP shall be made. The issue of the additional reference to the India 1998 Anticorruption Law was referred to the Procurement Counsel for advice.

Based on the advice obtained through the above process and discussion with the Procurement Counsel the Bank responded to DEA TF on June 5, 2008. The matters discussed at the October meeting are summarized in the report that was appended to the letter. This report details the status of those SBD provisions on which TF commented. The report is divided into four sections. The first section includes SBD provisions which have been clarified and explained by the Bank. The second section includes those SBD clauses which have been updated in light of TF's comments. The third section includes SBD clauses which cannot be amended or modified. The fourth and final section includes those SBD clauses for which TF's comments are still under review.

One of the issues included in Section III of the Report is TF's suggestion that auditors be appointed jointly by the Bank and the Executing Agency. The Bank explained why its right to independently appoint an auditor cannot be compromised in any manner. The Bank must have an unconditional right to have access to the accounts and records relating to projects financed by the Bank, and to have the right to unilaterally appoint an auditor to audit such records. The proposal that the auditor must be appointed by a mutual agreement of the Bank and the Executing Agency of the borrower significantly limits and materially impacts on the Bank's right to audit and to have access to information and, therefore, cannot be accepted. Notwithstanding the above, it should be noted that in practice, the Bank usually coordinates audit of documents with the counterpart agencies. For this reason, the standard text of this Clause will remain unchanged. Moreover, the Bank representatives explained, that this provision is not a newly introduced one and has existed in past contracts for a long period of time.

Two issues remain under review. The first issue is regarding TF's preference for the local venue of arbitration of disputes under contracts signed with an international party. The WB explained that a successful dispute resolution process is one that is perceived by all parties as fair, impartial, and independent. Locating the arbitration within the sovereign's jurisdiction creates the potential for biases, actual or perceived, on the part of the arbitral tribunal but also any court involved in the arbitration. The Bank recognizes that TF would feel more comfortable holding arbitrations in India and, to better understand this position, the Bank would like to collaborate with TF to examine the current state of arbitral practices in India. The Bank will consider the venue for arbitration on a case by case basis until its final position can be made based on the study of the current state of the Indian

arbitration system. Such study should be completed no later than June 2010, at which time the Bank will review the study's findings and determine whether arbitrations should be located in India.

The second issue remaining under review pertains to TF's suggestion that the provision relating to compliance with the Prevention of Corruption Act, 1988, be applied at the bidding stage to all Bidders by means of a provision inserted in the Bid Form. As advised by the legal counsels, the Bank representatives reaffirmed that the Bank cannot give its unqualified assent to this requirement proposed by the TF, before confirming on the full effect of such a language being used up front, including the potential effect on competition and any risk of additional burden on bidders and contractors.

The Bank's legal counsel has reviewed the text of the Act, but there remain several questions as to the potential scope of its application. The Bank is interested in working with TF to fully understand the potential impact of its suggested language. To this end, WB requests that TF appoint legal counsel to discuss the Act with the Bank's legal counsel.

C. Assessment of NLTA

7. The impact of this NLTA with regard to SBDs cannot be made at this stage. It is too early to assess the impact of the NLTA on the use of SBD given that the response on Goods, Works and Consultants has been sent recently and GOI is working on it. The response of the S&I SBD is to be sent yet.
8. Though DEA TF agreed to maintain this body for the purpose of the discussion on any procurement matters, and some of such matters were raised during the meeting in December 2006, it needs be ascertained that the TF members continue to be available for discussions in future.

Lessons from NLTA

9. In order to reach concerns on all issues it is advisable that TF includes a wider representation of the Implementing Agencies or carry out wider consultation before formulating their comments that, as a result of limited representation, in some cases are specific to some projects. Comments on S&I are example. This would help bring real issues of practical nature and quicken the agreements more effectively.
10. There is a need, also, of wider consultation within the Bank, perhaps on a concerted basis to be able to provide quicker response as delay in such responses may adversely impact the willingness of cooperation of moving the exercise forward.
11. A major learning, from the NLTA is that there is a need to consult as early as possible GOI when changes are made in the Bank's SBDs affecting policies or their interpretation.

Continued Way forward

12. During the coming months, the Bank will respond to the TF's comments on the S&I SBDs. These comments were prepared by the TF Sub-committee consisting of the officials of Power Grid Corporation Ltd., New Delhi, India (a borrower in Energy sector). The Bank had extensive discussion with Power Grid on the similar changes in the context of Power Grid's projects.

13. Continue to finalize the issues that are still under review and are explained in Section IV of the Report on SBDs and SRFP.
14. Continue the discussion with the TF in case TF has any further queries or response to the Bank's letter.
15. Further discuss the procurement matters already raised with the TF at the meeting in December 2006.

Attachments

Letter from the Bank to DEA TF with appended Report on SBD and SRFP Provisions

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