

# Lessons in Public Investment Management

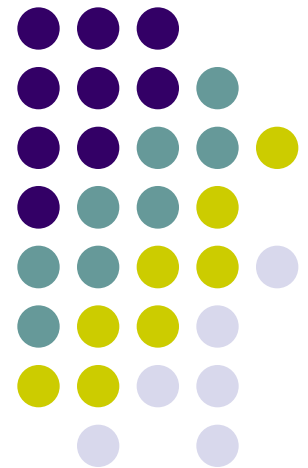
**Experiences of selected EU member states in managing transport infrastructure investments**

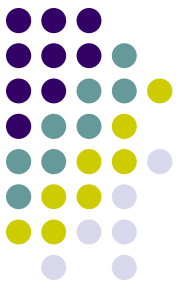
**PEMPAL: PIM Conference**

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**Bernard Myers, World Bank**





# Methodology and Cases

- **Source:** 2009 World Bank Working Paper Series
- **Cases:** UK, Ireland, Spain, Slovenia, Slovakia, Poland, and Latvia\*
- **Approach:** Country researchers adapting the Bank's analytical framework of “must-have” features in PIM

\* Includes also incorporates findings of subsequent Bank missions to Romania, Bulgaria

# “Must-have” features for efficient public investment management



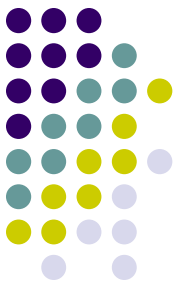
1. Investment guidance and preliminary project screening;
2. A formal project appraisal processes (with cost-benefit analysis being best practice);
3. Independent review of appraisals (e.g. including consideration of alternatives);
4. Project selection and budgeting need to establish envelopes for public investment so that a sustainable investment program can be undertaken;
5. Implementation plans need to be realistic;
6. Adjustment for changes in project circumstances;
7. Facility operation—asset registers need to be maintained and asset values recorded; and
8. Evaluation—to ensure that there is some learning and feedback.

**Source:** *A Diagnostic Framework for Assessing Public Investment*, Policy Research Working Paper 5397, World Bank, August 2010.

# Key Findings on 11 Areas of Public Investment Management



1. Role and impact of strategic planning
2. Budgeting for public investment projects
3. Project appraisal and selection
4. Risk Mitigation and project planning
5. Role of the MOF / External bodies
6. PPPs and off-budget entities
7. Procurement strategies
8. Project monitoring and accounting
9. Audits and Ex-post Review
10. Capacity development



# 1. Strategic Planning\*

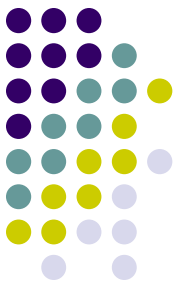
- Unless strategic plans are linked to a realistic medium term resource envelope, they are likely to lead to a large pipeline of approved projects that cannot be completed on a timely basis
- Strategic planning is done primarily within sectors rather than across sectors. While national strategic documents can help set broad guidance on cross-sectoral goals, they cannot facilitate project prioritization.
- EU processes and priorities heavily influence national policymaking, while parallel processes exist for nationally-financed projects

# 1. Role and impact of strategic planning in the NMS



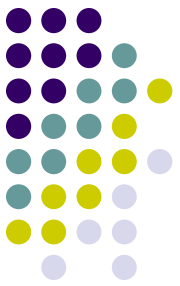
- National strategic planning efforts provide umbrella for sector planning – in principle, a basis for sectoral priorities
- Multiple planning documents/processes, some with very long-term perspective
  - 25-year Long-term Development Guidelines (Latvia)
  - Resolution on National Development Projects 2007-2023 (Slovenia)
  - Transport Policy of the State 2007-2020 (Poland)
  - Essentially broad vision statements
  - Goals and means loosely defined – establish a “transport and logistics centre”
  - Sometimes based on outdated assumptions from old planning documents

# 1. Role and impact of strategic planning in the NMS (cont...)



- In practice strategic planning results in close alignment with EU priorities
  - satisfies the form, but not the spirit of EU guidance
  - risk of EU priorities displacing national priorities
- Even medium term sector strategies can result in wish lists, rather than real prioritization
  - Three-year rolling Public Works Plan (Slovakia)
  - Resolution on Transport Policy (Slovenia, 2006)
- Missing element in sector strategies: link to a realistic resource envelope

# 1. Strategic Planning in Ireland, Spain, UK



- No overarching national strategy document, except in Ireland. Others rely mostly on sector planning processes
- Sector plans developed with a very long-term perspective
  - Transport Infrastructure Strategic Plan 2005-2020 (Spain)
  - Transport 21 (Ireland, 10-year plan)
- Plans consistent with long-term resource commitments for the sector (UK, Ireland)
  - 10-year capital envelope agreed with Irish Dept of Finance
  - 7-year budget guideline given to Dept of Transport by the UK Treasury
  - Year-to-year decision-making in Spain



## 2. Budgeting for Investment\*



- MTEFs are most effective when they provide predictability to annual project financing, which requires some bottom-up project level detail not just high-level ceilings
- Weak MTEFs allow new projects to be introduced by delaying the completion of existing projects – i.e., the pace of financing slows down in order to create fiscal space for new projects.
- While MTEFs typically cover three years (through  $n+2$ ), a longer budget planning horizon can be helpful for capital projects in order to facilitate genuine prioritization.

# 2. Budgeting Processes in NMS



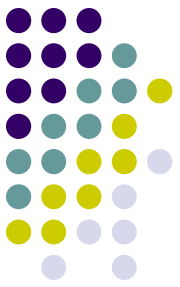
- Medium term (3-5 year) budget plans are used for investment projects. But actual project prioritization is still heavily driven by the annual budget process.
- In practice, plans show “potential” projects because not all projects can be included in the annual budget
  - Development Programs Plan (Slovenia), rolling basis for n+4 years, annexed to budget
  - Investment Register (Slovakia) – list of potential projects
  - Investment Annex (Spain) – in principle, projects to be funded
- Some projects may drop out of the plan, displaced by other priorities
- Over-optimistic rates of execution for projects, undermines prioritization, delays other project starts.

## 2. Budgeting Processes in NMS and Spain (cont...)



- Although most projects are multi-year, funding is still determined annually.
- Amounts for the second year must be re-approved in the budget (exception: Latvia MTEF baseline adjustment since 2007?)
- In Spain some opportunity to commit future funding, but still frequent changes the funding schedule, despite original project plans
  - political pressure to make fiscal space for new projects
  - projects slowed, not stopped (especially recently launched projects)
  - ‘super-projects’ started with relatively little financing in early years
  - regional-based coalitions exert pressure on central govt; need to promote regional equity out-weighs economic efficiency

## 2. Budgeting Processes in the UK and Ireland



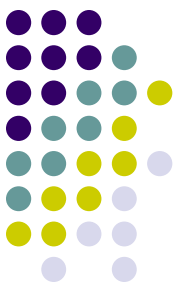
- In UK and Ireland budget resources authorized through completion of project
- Flexibility provided to shift actual funding between projects that are faster/slower moving – based on project needs, rather than political shifts
- Some limited ability to move resources between fiscal years to maximize implementation and maintain value for money (UK)
- Flexibility built on strong accounting and financial reporting practices

# 3. Project Appraisal and Selection\*



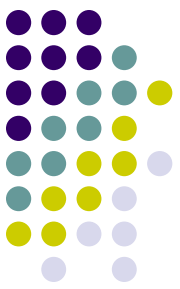
- While Cost-Benefit Analysis is frequently a component of project appraisal, the impact on project decisions is uncertain and quality of CBA is untested
- Despite its advantages, CBA may not uncover (a) over-design of projects or (b) the lack of consideration of alternative policy options.
- In the most advanced economies, CBA methodologies are refined over time to address emerging concerns.

# 3. Project Appraisal and Selection in NMS



- Transport Ministry puts forward specific projects based on their own analysis
- All EU-funded projects, and most large domestically funded will include a formal cost-benefit analysis (CBA)
- EU technical guidance is good, but actual quality of CBA was not measured in the study;
- External checks on reliability of CBA are rare
- Despite application of CBA, actual project selection criteria leave substantial scope for political discretion

# 3. Project Appraisal and Selection in NMS (cont...)



- Other factors, including project maturity (or readiness), urgency, and ‘strategic’ nature of the project can be big factors – possibly overshadow CBA weighting
- Analysis of alternative policy options, not well-developed.
- Risk cited of possible “over-design” of projects in lieu of more cost-effective options.
- Some evidence of “path dependencies” – i.e., projects advanced based on fact that they have been in the queue longest
- Risk assessment is formally complied with, but little impact on planning

# 3. Project Appraisal and Selection in UK and Ireland



- CBA is generally the core of project appraisal
  - UK Green Book provides general technical guidance, with main infrastructure ministries providing refinements for sector specific needs
  - Ireland Department of Finance issues guidance
- Improvements made regularly to CBA techniques:
  - UK Treasury guidance refined, expanded to include risk adjustment factors
  - UK Department for Transport guidance update to include distribution of costs and benefits among stakeholders

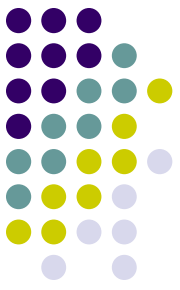


# 4. Risk Mitigation and Project Planning\*



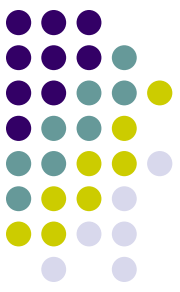
- Acknowledging project risks is not equal to risk mitigation
  - actively planning measures to reduce risks
- Quality of project management arrangements should be a more formal part of project selection decisions

# 4. Risk Mitigation & Project Planning



- In NMS, risk assessment is a formality and rarely impacts project selection or management arrangements
- In UK and Ireland, risk mitigation is more front-loaded in the project appraisal and planning processes
- Planning of project management (contract structure, allocation of responsibilities, team competencies) no longer viewed as merely a concern for “specialists” or ignored by policy officials
- Irish CBA advice has evolved to include advice on project management and implementation, e.g.,
  - Dealing with future cost increases and variation in outputs
  - Expectations for monitoring and management arrangements

# 4. Risk Mitigation & Project Planning (cont...)

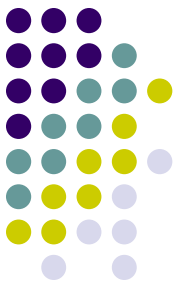


- UK and Ireland increasingly concerned with not only quantifying benefits –
  - Setting up structures to manage the risk
  - Creating appropriate management incentives
  - In some cases, building in a level of contingency
- UK and Irish requirement of a “business case” for some projects
  - Is the proposed option the best for delivering “value for money”

# 5. Role of MOF & External Bodies\*



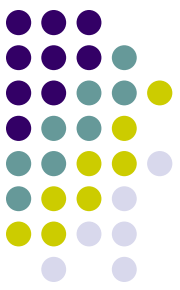
- Though line ministries have primary responsibility in selecting projects, MOF needs to assure quality standards are being met for project appraisal and that value-for-money is being assured throughout the project cycle.
- External experts or independent commissions can help supplement the knowledge gaps within MOF and help validate line ministry proposals.



## 5. Role of the MOF / External bodies

- In NMS, MOF role in evaluating infrastructure priorities is quite limited; so is capacity to assess cost-benefit analysis
- Guidance issued by UK Treasury and Irish MOF to assure processes are in place to promote good project appraisal and management
- Strong policy coordination role: UK Treasury involvement involved in the overall transport strategy and high level planning

# 5. Role of the MOF / External bodies (cont...)



- Quality assurance not dependent on capability of MOF – active use of external experts
  - Ireland: Commissions independent reviews of the business case, the CBA, or the risk management (e.g., by economic consulting firms)
  - UK: Instituted formal review mechanisms that includes experts not affiliated with the project -- “Gateway” process involves 6 stages of review
- Special reviews commissioned in the UK to identify reasons for systematic cost-underestimation

# 6 & 7. Procurement Strategies and PPPs\*



- In advanced economies procurement strategies are designed to limit risk to the public sector and are integrated into the project appraisal phase
- Public Private Partnerships (PPPs) require strong analytical expertise to assess potential risks to government – bad projects are bad projects regardless of the source of financing

# 6. PPPs and Off-budget entities



- In new and old EU member states, PPPs and off-budget debt are attractive way to expand infrastructure investment
- Risk: Projects targeted for PPPs without adequate economic justification for the project relative to other options
- NMS have assigned institutional responsibility for PPPs, but analytical expertise is lacking
- In the UK and Ireland, policies being put in place to reduce economic bias for PPPs, e.g.,
  - change in accounting rules to level the playing field between public and private financing options
  - PPP or private finance options must show they increase efficiency or effectiveness – not just bring in extra resources
  - PPP treated as one of several “procurement options”
- Difficult lessons learned in the UK
  - Private finance option for London Underground widely viewed as a failure

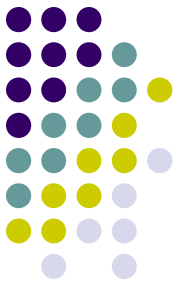


# 7. Procurement strategies



- In NMS
  - EU guidelines followed- But little evidence of modern procurement techniques to share greater risk between contractor and purchaser
  - Cost overruns are common
- In the UK and Ireland:
  - design of procurement strategies that limit risk to the public sector are part of the appraisal and planning processes
  - private financing as one option if there are efficiency or effectiveness advantages
  - “Early Contractor Involvement”
    - experimental procedure to promote innovation among contractors and hold costs down
    - Single contractor chosen to design and build
    - competition based solely on quality and “open book accounting”
    - target cost agreed before construction

# 8 & 9. Project monitoring and evaluation\*



- Monitoring of project expenditures against the annual budget is common, but falls short of what MOF needs
- MOF should compare total realized project costs against the total projected costs and timelines, with an objective to identify causes of major overruns and/or delays.
- Performance-oriented budgeting should start to link project results with sector outcomes – are the intended benefits being realized

# 8. Project monitoring & accounting



- In NMS
  - Focused on monitoring expenditures to budget amounts
  - Little comparison of actual costs with total project costs and/or original amounts proposed in feasibility study
  - Cost-overruns rarely capture the magnitude of variance
  - Limited non-financial indicators of performance
- In UK/Ireland:
  - Financial accounting more likely to include all full project implementation costs
  - Greater use of non-financial performance information

# 9. Audits and Ex-post Review

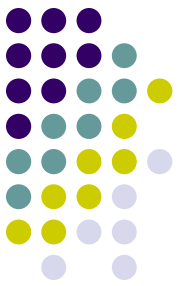


- In NMS
  - Internal and external audit focus on basic financial oversight
  - No or limited review of whether benefits were achieved
  - Transparency of information is improving, but does not yet include information on project outcomes
- In UK/Ireland:
  - Internal audit plays a role in bringing projected cost increases to the attention of Ministers
  - Introduction of new Gateway process for staged and ex-post review
  - Public transparency about project costs and procurement arrangements creates incentives for ensuring good practices

# 10. Capacity Development\*



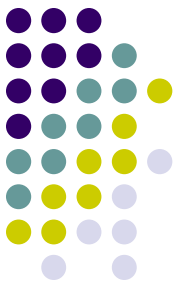
- Project appraisal requirements need to be appropriately scaled to the project risks and the administrative capacity
- Specialized PIM skills need to be developed and retained within the public sector



# 10. Capacity development

- Only the UK and Ireland discussed explicit strategies to strengthen capacity of the civil service to manage infrastructure investment programs
- Concern in the UK that government had gone too far in contracting out – needed to strengthen skills of civil servants
- Ireland has taken the most steps to build capacity, recognizing limited skill pool in a small economy
  - Appraisal guidance developed by Dept of Finance
  - specialized training for officials, covering project appraisal, procurement, project management, policy analysis
  - created a National Development Finance Agency that provides financial and risk advice on all large projects

# Administrative and Political Culture: Reflecting on What is Feasible?



- Can senior civil servants challenge the political level based on technical arguments against a particular project?
- Do managers face consequences for poor project selection or poor project management? Are good managers rewarded?
- Can public institutions give managers more discretion by issuing guidance notes rather than detailed regulations?
- Are checks and balances in the system effective for encouraging good management without stifling innovation?
- Does the financial management culture focus only on compliance and reporting, or do skills exist to assess value-for-money as well?
- Is the general public regularly informed about the quality of project management and whether outcomes are being achieved?