

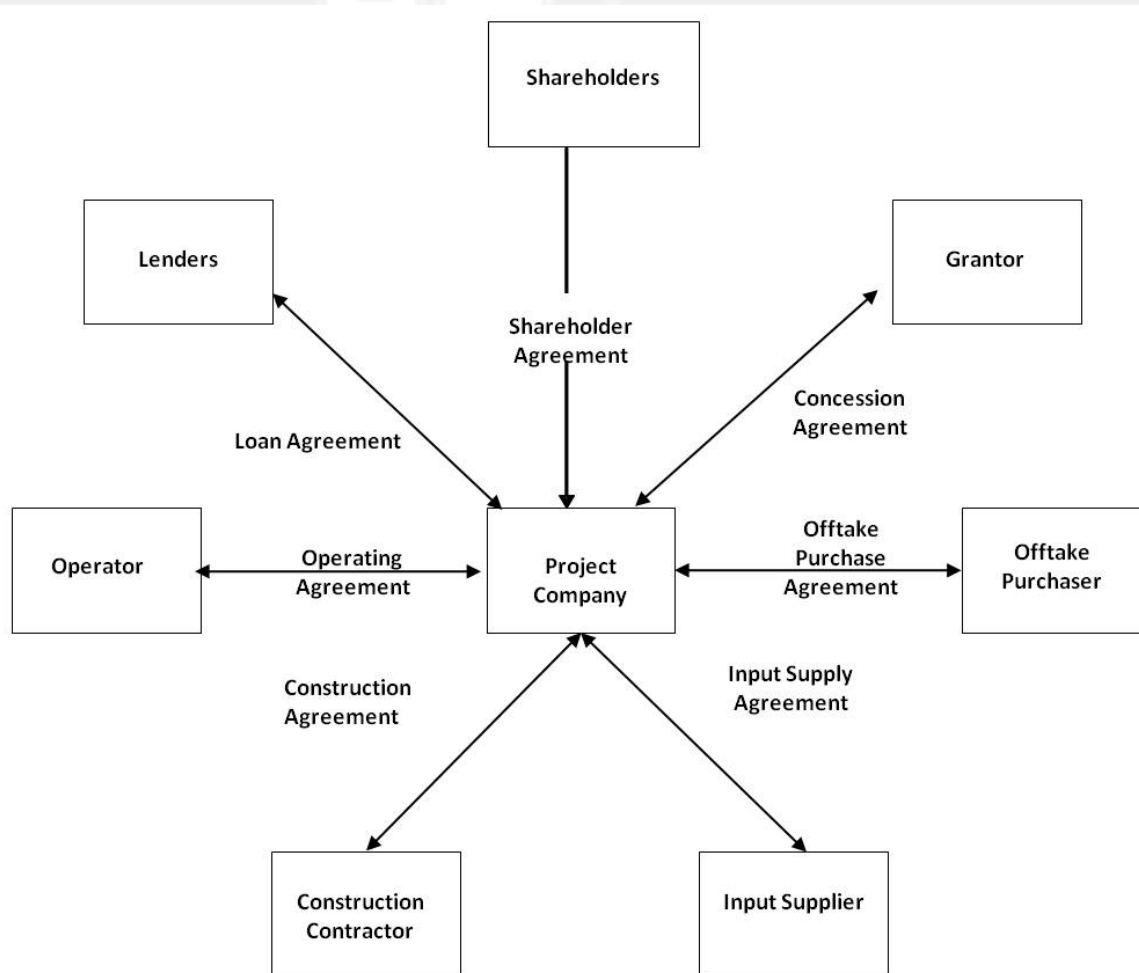


# The Involvement of Financing Institutions

The weight of DB/DABs in the decision making process of banks and funding institutions

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- **General Observations:**

- MDBs (ADB/AfDB/EBRD/WB)
  - Bilateral Funding Institutions (KfW, JICA)
  - Private Banks
- **have a split approach, since**
- » at tender stage: they insist on the entry of Dispute Resolution Clauses
  - » after Contract award: they do not systematically insist on the use of DBs
    - **Reasons:** Misconception of potentials and skills of DBs (frequently the perception is that DBs substitute arbitral tribunals).

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## Further Observations:

- Private funders will typically look at the “bankability”

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Lenders will only lend to a project if it is '**bankable**'.



- 'Bankability' is a flexible concept and it will change from project to project. Essentially, it is about whether or not lenders are prepared to provide financing for a project.

Factors involved in **bankability** include:



- proper risk sharing between all of the participants in the project
- enforceable security
- agreement by the sponsor not to withdraw cash from the project for a certain period of time (see Restrictions on distributions), and
- contractual certainty

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## Further Observations:

- Therefore they must satisfy standard debt financing requirements
  - Banks suggest using for instance
    - ICC (International Chamber of Commerce Turnkey Contract)
    - LOGIC (Leading Oil & Gas Industry Competitiveness) Contract for Supply of Major Items of Plant and Equipment and
    - FIDIC standard forms
    - ENAA
    - NEC3
- 
- including DB clauses**

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## Contractual certainty

means that the contracts which underpin the project have been properly drafted so that the counterparties cannot easily get out of them or change their terms. For example:

a construction contract is **more “bankable”** if the construction contractor must complete construction of the project by a fixed date and for a fixed price— it is **“less bankable”** if the construction contractor is able to request a lot of time extensions and price increases, ...


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- Further Observations:
  - (Public) Employers report that international funding institutions do not make dependent no objections and approvals from adopting dispute clauses.
  - (Public) Employers report that international funding institutions do not require the implementation of standing DBs – even if for instance required by the FIDIC MDB harmonized version.
  - However, the banks typically require provision of remedy mechanisms in respect of procurement decisions.



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## Use of Dispute Boards as required by MDBs

MDB SBD	Conditions of Contract	Dispute Resolution by:
Works	FIDIC MDB harmonized edition	Standing DB
Plant	ENAA form  AD hoc	Standing DB
Small Works	FIDIC Green	Adjudicator

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- World Bank's Procurement Policies are currently under update; the consultations papers show:
  - Consultation participants called for stronger mechanisms for dispute resolution. Stakeholders criticized the World Bank's current complaints handling system. There was a call for more clarity in defining what a complaint is, more transparency in complaints handling by the Bank and for the Bank to take on a more direct role in handling disputes by setting up an Ombudsman, for example. **Another alternative is to set up independent Dispute Boards, which could be financed with loan proceeds.**
  - Among the guiding themes emerging from the consultations are inter alia the incorporation of alternatives and/or expansion of governance and integrity aspects, including transparency, access to information, monitoring by civil society, internal controls, including more effective audits, and **dispute resolution mechanisms.**

**Observation: Still the banks discuss framework details but not the practical use of DBs.**

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From the lenders' perspective the ideal position for the construction contract is as follows:

the construction contracts should be turnkey, meaning that the construction contractor is responsible for all aspects of the construction and design of the project output;

**there should be a fixed price, incapable of being readjusted, and that price should be paid in one lump sum on completion;**

**completion must occur within a fixed time period;**

the events that could be considered 'force majeure' should be limited;

where there is a concession agreement the contractor should only be able to claim force majeure, an increase in price or an extension of completion time to the extent that Projectco is able to claim the same under the concession agreement;

liquidated, financial damages should be payable if completion is not achieved by a fixed date and those liquidated damages should be adequate and at least cover interest payable on the loan for a reasonable period;

there should be no contract administrator or engineer, but rather an employer's agent instead - this person would be an agent of Projectco and made subject to the restrictions contained in the project credit agreement;

there should be no – or, at least, no large - limits on the contractor's liability;

the contractors should give extensive guarantees and, if the contractor is to be released from liability for defects after a certain period has passed, that period should be long and only begin running after a well-defined completion test has been passed.

<http://www.out-law.com/en/topics/financial-services/project-finance/key-issues-for-lenders-in-project-finance-agreements/>

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## Conclusions – Questions

- Is it really true that one-sided Contracts avoid claims and disputes?
- Do banks & funding institutions underestimate the management component in successful projects?
- Do banks and funding institutions have a comprehensive understanding of the advantages of Dispute Boards?
- Is there hope?

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## JICA observes:



Construction work is susceptible to many external influences such as variable subsurface and, metrological conditions as well as social, economic and environmental factors. It is impossible to eliminate all uncertainties from construction work and unforeseen events are likely to occur during any lengthy construction period.



Under Red Book, the Contractor has an entitlement to extensions of time for completion of the work if he suffers delay from specified events and payment of qualifying additional cost he incurs as a result of such events. The Red Book sets out, in detail, a claims and dispute settlement procedure to cope with uncertainties involved in construction works.

**JICA CHECKLIST HOW TO AVOID "ONE SIDED CONDITIONS OF CONTRACT"**

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JICA Test\*:  
**Appointment of the  
Dispute Board**

Is the deadline for  
the establishment of  
a DB set in the  
Contract Data written  
as “28 days after the  
Commencement  
date”?

**\*JICA CHECKLIST HOW TO AVOID "ONE SIDED CONDITIONS OF CONTRACT"**

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What can we (the DRBF) do?



Promoting best practice!



Striving for balanced and manageable Contracts!



Emphasizing the management approach implying Dispute Boards!



Thus: Following a holistic approach!