

Article category: PROCUREMENT

BUILD - OPERATE - TRANSFER

The way forward

**By Ian McKechnie*



Infrastructure establishment, refurbishment and/or maintenance in many developing parts of the world, including Africa, have been restricted in the past through many reasons. One of the major reasons has been access to finance. Internally-generated funding is often not an option, and many countries have not always seen development aid as the desirable alternative. It is therefore important to consider alternative means of funding infrastructure provision in the developing world. One of these is a concession-type project model, referred to in various guises such as Build-Operate-Transfer (BOT), Build-Own-Operate (BOO), etc. For the sake of this article, we will refer to BOT as a generic term encompassing the different variants.

The basic concept

In a typical BOT-type project, a concession is awarded to a successful bidder (the concessionaire). The concessionaire then establishes the required infrastructure, as well as operation and maintenance systems. Financing is provided through the concessionaire, and is typically a mix of debt and equity finance. Finance is typically limited or no-recourse financing, and is provided on the merit of the project and security of the project revenue flow.

Once the concessionaire has established the required infrastructure and systems, he is entitled to a revenue flow generated through the use of the infrastructure, and his ongoing operation and maintenance thereof. This is recovered throughout the concession period, either directly from users or indirectly through government. The revenue stream and concession period are calculated to ensure repayment of capital and an acceptable level of return to the concessionaire and his financiers. Due cognisance of project risks and complexity is taken into account.

At the end of the concession period, the infrastructure is transferred free of charge to the host government. Whilst this is a simplified description, and there are also many variants, it serves to illustrate the basic concept.

Attractive method of implementing projects

The BOT project concept is becoming an increasingly attractive alternative method of implementing projects. It is particularly suited to the African context, including South Africa, where financing is limited. It is also often more politically acceptable to establish infrastructure through concession-type projects than through full privatization models.

Although it is currently probably a more prevalent contracting model in the civil and built environment, the BOT project model is also particularly applicable to projects in other engineering and technology areas. These include electricity supply and distribution, communications and computer/IT-related systems. At a toll road, for example, a toll-fee or levy is placed on users, and paid to the concessionaire as the principal revenue stream.

In these sectors, it is also possible to identify users and use-related tariffs from which a revenue stream or streams can be generated. Such tariffs can then be directly or indirectly recovered from end-users by government or the concessionaire. These tariffs could, for example, be transaction based, surcharge based or simply based directly on usage/availability, and can also be a combination of these.

Traditionally, these types of concession projects have usually been dealt with on a tender and contracting basis, with the contractor playing a reactive role. Although it is usually regarded as a fair method, it can be a very time-consuming and expensive process for all concerned. However, in addition to this reactive approach, the BOT project model also allows a more proactive approach to be followed by the contractor. In this respect, provision can be made for unsolicited proposals to be

objectively considered by governments, without going through the formal tender process. Such proposals may, for example, be accepted either through a direct negotiation process, or through a counter-bidding process. The system should, however, offer an incentive to contractors to make unsolicited proposals. Examples of various methods of dealing with unsolicited proposals can be found in different countries around the world.

The return on a BOT investment and project is financed through a revenue stream generated through a concession contract, together with related "take-off" contracts. For example, in the case of electricity supply and distribution, take-off agreements may be signed with various local or regional authorities, to purchase certain quantities of power at agreed tariffs, etc.

As BOT projects are funded as limited or no-recourse financing, an essential part of any BOT project is therefore securing access to a reliable and predictable revenue stream. This revenue stream also needs to be protected against outside factors, such as environmental, economic and political events.

Different risk profile

It is important to take cognisance of the different risk profiles relating to a BOT project. From a contractor's perspective, the risk is significantly greater than with a traditional type of contract. For example, project delays and/or unforeseen costs can significantly alter the investment potential of the project. This places significant emphasis on the project planning and project management aspects of the project, in addition to the technical capacity and ability of the contractor.

The integrity of the project contracts is also of vital importance in ensuring the success of these types of projects. Contracts are referred to in the plural, because a BOT project typically incorporates a number of contracts. Examples include the basic concession contract, take-off contracts, joint venture contracts, supply/service agreements with subcontractors, etc. It is also essential that these be harmonized.

The legislative situation in the country is also of vital importance in ensuring that concession projects can be successfully implemented. It is often the case that specific legislation must be amended to ensure not only that the service can be provided on a concession basis, but that the necessary revenues can be diverted to the concessionaire (either directly or via government entities). This is a particular problem area in countries that do not have a well-developed BOT policy and project history, and is certainly typical of many African countries.

The alteration of legislation can be a time-consuming task, and it is therefore essential that the legislative and legal implications of the intended project and contract are carefully investigated. This is of particular importance when considering the preparation and submission of unsolicited proposals.

Importance of planning and management

As discussed earlier, BOT or concession-type projects have often been considered only in terms of civil engineering-type projects, such as toll roads, bridges, etc. In fact, other sectors such as electricity supply, telecommunications, and IT also offer excellent opportunities to establish BOT projects where other forms of project finance are restricted. Numerous successful examples can be found around the world of such projects. However, the project planning and management implications are of particular importance in ensuring the success of such projects, and minimizing the associated project risks.

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This article was first published in ProjectPro magazine Vol 8 No 5, September 1998

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