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# Republic of Chile Country Procurement Assessment Report

August 2004

Argentina, Chile, Uruguay, Paraguay  
Country Management Unit  
Latin America and the Caribbean Region

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## ACRONYMS

Bank	World Bank
CAS	Country Assistance Strategy
CChC	Cámara Chilena de la Construcción (Chilean Chamber of Construction)
CGR	Contraloría General de la Republica (General Controller's Office)
CT-TI	Chile Transparente/Transparencia Internacional Transparency International –Chile Transparent
CPAR	Country Procurement Assessment Report
DAE	Antigua Dirección de Aprovisionamiento del Estado (Former Directorate of State Supplies)
DCCP	Dirección de Compras y Contratación Publica (Directorate of Public Procurement and Contracting)
DIPRES	Dirección de Presupuestos, Ministerio de Hacienda Budget Directorate, Ministry of Finance
EGP	E-Government Procurement
GoCh	Government of Chile
LCR	Latin America and the Caribbean Region
ME	Ministry of Education (Ministry of Education)
MH	Ministerio de Hacienda (Ministry of Finance)
MI	Ministerio del Interior (Ministry of Interior)
MOP	Ministerio de Obras Publicas (Ministry of Public Works)
MINVU	Ministerio de Vivienda y Urbanismo (Ministry of Housing and Urban Development)
MS	Ministerio de Salud
Procurement Law	Law on Procurement of Goods and Services Ley de bases sobre contratos administrativos de suministro y prestación de servicios
PPSSP	Public Procurement System Strategic Plan
SEREMI	Subsecretaria Regional Ministerial Ministerial Regional Subsecretary
SIGFE	Sistema Integrado de Finanzas del Estado
SUBDERE	Subsecretaria de Desarrollo Regional y Administrativo Sub secretariat of Regional Development and Administration
UTM	Unidad Tributaria Mensual (Monthly Tax Unit)

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**REPUBLIC OF CHILE**  
**COUNTRY PROCUREMENT ASSESSMENT REPORT**  
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## Foreword

Implementation of this review was agreed between the Ministry of Finance and the Bank as a piece of sector work aiming at the external knowledge and dissemination of public procurement, and in support of Bank operations in Chile. The review was the result of a joint effort between Chilean public and private sector officials led by the Directorate of Public Procurement Contracting (DCCP) and a Bank team. Preparatory work consisted of the review and discussion of documents with individuals involved in public procurement in May 2003, followed the exchange of information during the initial implementation of the procurement modernization strategy the following year. The Bank team acknowledges the invaluable contribution of the Director and staff of the DCCP, and their considerable logistic support. It further recognizes the equally valuable contribution of staff from the Ministries of Public Works, Finance, Interior, Housing and Urban Development, Health and Education, the General Controller's Office (CGR), Transparency-Chile, the Chilean Chamber of Construction, the University of Chile and other public and private agencies and individuals.

The Bank team consisted of Jaime Roman (LCOPR), Maria Lucy Giraldo (LCOPR), Eduardo Talero (OPCPR) and Enrique Pinilla (Consultant). Also contributing to the CPAR were Alison J Micheli (LEGPR) and Gian E. Casartelli (OPCPR). Agustin Litvak (SARPS), Miguel Mercado and Roberto Panzardi (LCSPS), Aurelio Menéndez (LCSFT) were peer reviewers. Written comments were received from Joao Veiga Malta (IADB), Marta H. Molares (LEGLA), Daniel Fernando Oaks (LCC7C) Pamela Bigart and Knut Leipold (OPCPR). The Bank internal review of this report was chaired by Mr. Felipe Saez (LCC7C).

Following the Bank's internal review a preliminary version of the report was discussed with the DCCP in Chile in December 2003 and June 2004 and subsequently up dated to account for key developments since the initial preparation work review took place, and to incorporate comments from DIPRES, DCCP and MOP to the early version of the report.

By letter of September 6, 2004 Ms. Maria Eugenia Wagner, Undersecretary of Finance conveyed the GoCH's agreement with the findings of this report. She stressed that the ongoing public procurement reform program is comprehensive and entails major changes that should have a direct impact on the country's image, the Government's credibility and economic growth. She also stated that the Bank's views will be a considerable contribution to the reform process. She further commended the joint work between the Chile and Bank teams, which has brought about a highly productive forum for reflection on the reform initiatives.



## EXECUTIVE SUMMARY

### BACKGROUND

1. Chile's public procurement system is considered generally free of corruption supported by probity of the civil servants, decentralization, and good budgetary and control systems. However, it is affected by deficiencies that the government recognizes and is taking action to overcome, particularly with respect to procurement of goods and services. The aggregate value of public procurement by some 200 national government line agencies in 2001 was about \$ 4 billion or 3.4 % of the GDP, of which 58% was public works, 18% goods and 24% services, including consulting services and concessions.
2. There is no unified comprehensive and public procurement system in Chile. The procurement of public works on the one hand, and the purchase of goods and services on the other, have traditionally been carried out under separate legal, procedural and organizational frameworks. A corner stone of legislation is the Organic Law of State Administration (*Ley 18.575 Orgánica Constitucional de Bases de Administración del Estado*) The organic laws of the various ministries, state agencies and municipalities authorize them to set up their own procurement regulations. This is now changing. On July 2003 the President enacted the Procurement Law 19.886 which provides the framework for procurement of goods and service contracts and makes Chilecompra the electronic procurement platform for all agencies of the executive branch, the regional and provincial governments, the municipalities, the Armed Forces, the Central Bank and the CGR. The procurement of public works and concessions continues to be governed by existing regulations. However, the Government is processing a new law that, the same as the Procurement Law for goods and services, would set up a common framework for procurement of studies and construction of public works contracts.
3. On the institutional and operational side, the Ministry of Finance (MH) on the one hand, and the Ministries of Public Works (MOP) and Urban Development and Housing (MINVU) on the other, are respectively the pace setters national agencies on procurement of goods and services and civil works, but each public agency is autonomous to plan and undertake procurement in accordance with its own budgets. The two-tier approach transcends to the operational level.
4. In 1998, the Government established Chilecompra as an information platform for state procurement of goods and services. Chilecompra was a pioneer effort on e-procurement and had been generally considered a model to follow. However, its initial operation did not meet expectations. By 2002 only about 3% of the number of procurement opportunities were being posted and only 577 of the 30,000 potential suppliers were regular users of ChileCompra. An independent study commissioned by the GoCh in 2002 concluded that lack of leadership and inadequate management, cultural resistance and lack of political commitment were the principal reasons for Chilecompra 's inadequate performance. Thus, the Government took a number of policy, institutional and administrative actions designed to introduce transparency to the procurement function and strengthen Chilecompra, which are reflected in the Public Procurement System Strategic Plan (PSSP) for 2000-2004 that is currently under implementation.

## **PUBLIC PROCUREMENT SYSTEM STRATEGIC PLAN, PPSSP (FOR GOODS AND SERVICES)**

5. With the underlying objective of enhancing transparency, efficiency and economy, the PPSSP provides for the establishment of an on-line national information system for all public procurement, while establishing the legal and operational framework for procurement of goods and services. The PPSSP builds on experience, has full support at the highest level of government, and enjoys strong commitment and leadership for its implementation.

6. The PPSSP maintains the procurement responsibility at the agency level but calls for centralization and standardization of the process through Chilecompra, which in addition to transparency, should bring about major operational efficiencies and economies. The PPSP relies on comprehensive public procurement policy, and administrative and institutional reforms, rather than technology, as the fundamental input for the strategic plan. Although implementation of the strategy is still underway, its conceptual approach and design can be considered a best practice. Moreover, so far considerable progress has been made with visible positive results, particularly in regards to disclosure of information, buyers and sellers participation and purchases through framework agreements.

7. The PPSSP comprises work in four major areas as follows: (i) policy and regulation; (ii) institutional change (iii) enhancing capacity and efficiency of Chilecompra and; (iv) technical assistance to government agents and suppliers.

### **THE PROCUREMENT LAW**

8. The Procurement Law 19.886 is a statute of principles that requires development through rules and regulation. A comprehensive draft regulatory decree or *Reglamento* has been drafted and is under review by the CGR. With some exceptions, the Law and draft *Reglamento* provide a solid basis for achieving the PPSSP's objectives in a generally consistent manner with international procurement practices. They focus in general principles and procedures that provide flexibility. However, because of their wording, some articles in the draft *Reglamento* give considerable leeway for change or interpretation, which may in the end result in inconvenient disbursement practices. Thus, achieving the stated policies of uniformity would require strong leadership and guidance by the DCCP in the form of operational manuals and harmonized documentation. The Bank provided detailed comments on the draft to the Government in January 2004.

### **INSTITUTIONAL CHANGE**

9. The establishment of the Procurement Council (PC) as an advisory body in the Ministry of Finance formulation of policy and oversight of the public procurement with the technical support of the DCCP together with the creation of the Court of Public Procurement (CPP) are the main institutional features of the PPSSP. DCCP took over some of the institutional functions of the former *Dirección de Aprovisionamiento del Estado*, DAE (Directorate of State Supplies), but with a completely different strategic and managerial approach. Its operational structure responds to the challenges posed by the PPSSP in respect of client technical assistance and support, procurement policies and procedures, technology development, internal management, and legal.

10. Besides the establishment of the above mentioned institutions, major institutional capacity building on procurement management is necessary at the national, regional and



municipal levels. Chile's institutional strength notwithstanding; it is apparent that the procurement function is relatively weaker than others within the public service sector. Agency managers have traditionally neglected it because many consider it of low strategic value, thus depriving it of adequate resources.

11. Institutional weakness deepens as operational decentralization reaches the regional and municipal levels. In particular, a large number of the 340 municipalities face major issues not only on staffing, but also on availability and access to information technology and connectivity, which if not adequately resolved may hinder implementation of government decentralization in general, and procurement in particular.

12. However the critical issues facing procurement by the municipalities cannot be tackled in isolation, but under the overall umbrella of municipal development. The Under secretariat of Regional and Administrative Development (*Subsecretaría de Desarrollo Regional y Administrativo*, SUBDERE) of the Ministry of the Interior is responsible for fostering and coordinating that endeavor with other state agencies. The Bank could play a key role in this endeavor through existing proposed projects.

#### **ENHANCEMENT OF CHILECOMPRA**

13. Enhancement of the original platform of Chilecompra consisting of basic improvements to capacity, functionality and presentation (more user friendly) as well as, the addition of new features such as purchase orders and e-tendering was completed in 2003. The new platform awarded on the basis of international competitive bidding to a private consortium entered in operation in February 2003. In a subsequent phase Chilecompra will be integrated with other government systems, in particular SIGFE-DIPRES (Integrated Financial Management System of the Budget Directorate in MH).

14. The new electronic platform of Chilecompra was developed on the basis of the experience gained from the operation of the original platform considering the full spectrum of private sector e-commerce facilities that makes possible the use of commercial, off-the-shelf software. Outsourcing to the private sector the technical design, technology selection and acquisition, day-to-day operation of the system and technical support to users on the basis of a four-year output based contract is cost transparent, provides flexibility and guarantees efficiency. A comparative review of Chile's past and current outsourcing experience, and government designed and operated systems should provide valuable lessons about the pluses and minuses of the two approaches.

15. The system has the full complement of disclosure facilities traditionally associated with an electronic government procurement (EGP) system, including: procurement plans, invitations to bid, contract awards, database of past transactions, corresponding search and statistical functions, and a standard product/service coding catalog. Information available at the [www.Chilecompra.cl](http://www.Chilecompra.cl) website includes: the PPSSP in both Spanish and English, the new law and other relevant legislation and regulatory instruments, announcements of all upcoming procurement transactions, and a database of past transactions.

16. The system envisages seven user support facilities: registry of suppliers, reference prices, electronic billing and payments, support for preparation of bidding documents, bid evaluation support and help desk. Of those only two were not operational at the time of this assessment; the

reference price database and electronic payments will be developed in the medium-term. Also, the operation of the registry of suppliers will be outsourced under a separate contract.

17. Chilecompra presents an excellent opportunity to carry out e-procurement under Bank projects in Chile. Every indication exists that Chilecompra provides state-of-the-art electronic procurement capabilities entirely compatible with Bank procurement guidelines, but this would need to be verified when the new electronic platform is fully operational. In particular, the procedure for registration of foreign bidders and the actual implementation of security, integrity, non-repudiation and confidentiality features for one and two-envelope tender transactions would be aspects most interesting to revisit at a later time. Moreover, the on-line procurement facilities of Chilecompra offer more competitive alternatives than those proposed in the Bank Guidelines, particularly with respect to “shopping”.

#### **TECHNICAL ASSISTANCE TO USERS AND SUPPLIERS**

18. Lack of participation by purchasing agencies and suppliers due to a large extent to inadequate knowledge and technical support was one of the main reasons for failure of the initial phase of Chilecompra. Therefore, one of the key elements for success built in the PPSSP is the development and implementation of a immediate and long-term programs of dissemination and technical assistance to users and suppliers; and in particular, regional offices and municipalities. As it is expected that procurement modernization will bring about considerable savings, government agencies are required to cover out of their own resources technical assistance and training expenses which apparently has not been a major problem for national agencies, but it is likely to be a major constraint to implement the program among the small municipalities.

19. Technical assistance includes the following major activities: (i) intensive dissemination and training of state agencies through the Program of Excellency in Procurement Management (*Programa de Excelencia en Gestión de Abastecimiento*) linked to the MH's Program of Management Improvement (*Programa de Mejoramiento de Gestión*); (ii) human resources development through on-the-job and formal training of staff, including the establishment of university courses on procurement management; and (iii) technical support to user agencies on specific issues related to the operation of Chilecompra. Support to suppliers focuses on: (i) establishment of a National Registry of Suppliers; (ii) dissemination of information on the benefits of Chilecompra; (iii) support to PYMEs (Small and Medium Enterprises); and (iv) dissemination of national and international business opportunities.

#### **PPSSP PROGRESS UP TO DECEMBER 2003**

20. It could still be too early to judge the success of Chile's public procurement strategy. However, judging from the results thus far, the prognosis is very positive. The DCCP reports the following progress as of May 2004: (i) participating agencies increased from 144 to 606; (ii) registered suppliers from 6,193 to 70,563; (iii) timely publication of invitations to bid from 5100 to 20,424; (iv) average number of bidders per process from 1.7 to 6.2; and purchase on the basis of framework agreements from 11.5% to 13.2%. This performance exceeds considerable initial expectations, but it has equally caused considerable strain to the electronic platform.

## **PROCUREMENT OF PUBLIC WORKS**

21. Public Works contracts make the largest portion of public expenditures (about \$ 4.0 billion or 58% in 2002). However there is not a unified framework for procurement and contract management of public works. Each ministry and public agency operates on the basis of the principles of the Organic Law of State Administration 18,575 and of their specific organic laws, rules and regulations; It is apparent that the treatment and coverage of procurement and contract matters have not been systematically addressed as they are scattered in various regulations and differ among the various services within the ministries. Also Decree-Law 600 of 1996 establishes a separate regime for concessions of public works services.

22. Most Chileans share a favorable view of the integrity of the public service. The MOP and MINVU have considerable experience in bidding, contracting and managing civil works, and their practices are generally transparent and competitive. Bid evaluation and contract award procedures are generally seen as undertaken in an open and transparent manner. The agencies exercise an active role during contract implementation and their monitoring staff is generally knowledgeable and fair in their judgments. However, some distinct rules and procedures are not fully consistent with modern procurement practices and should be improved (Paragraphs 72 to 80).

23. In addition to a unified legal framework and harmonized procedures, unification and reform of the existing MOP's and MINVU's. registries are needed in order to reduce transaction costs, avoid excessive specialization and promote bidder participation. A unified registry should aim at simplification of existing information requirements and qualification practices that discourage participation and reduce competition; it should be consistent with and linked to the DCCP's National Registry of Suppliers.

## **SELECTION OF CONSULTANTS**

24. A key issue that deserves special consideration both from the public works and PPSSP Procurement prospective is the absence of special rules and regulation for procurement of services of intellectual nature or consulting services. Consulting services are generally contracted on the basis of open competitive procedures similar to those for public works and goods contracts. Selection of consultants based on a "shortlist" is seldom done. Participation is open to registered firms regardless of numbers. On the other hand, as for construction contractors, the strict registration and qualification procedures may lead to narrow specialization and the predominance of some few firms.

25. Consultants selection in Chile is on the basis of a combined technical and financial evaluation of proposals. Frequently contract award is to the lowest price proposals that meet minimum technical qualifications (Least Cost). Quality and cost based selection is also used, in which case; the weight assigned to the financial proposal is 40% or more., but could be as low as 30% for complex assignments. In the long run the public sector will have to consider a more selective and quality oriented approach to consultant selection with no disregard for transparency and fairness.

## **PROPOSED PUBLIC WORK PROCUREMENT REFORM**

26. The Government is currently processing a draft law for procurement of studies and public works investment projects (*Ley de Bases de Licitación de Estudios y Proyectos de Inversiones*

*Públicas*), agencies, much along the same lines as the Procurement Law, and would establish a unified Registry of Contractors and Consultants managed by the MOP. The proposed Public Works Law would not formally designate a specific agency as the policy leader on the field. However, it should be expected that in practice the MOP would continue to play such a role, particularly regarding the issuance of standard documentation.

27. The proposed public works law, similar to the Procurement Law although very specific on certain matters such as scope of contract amendments, is a statute of principles which would require detailed development through rules and regulations. In fact, the MOP reports that it is considering amendments to the Regulation on Public Works Contracts (*Reglamento de Contratos de Obras Públicas*), some of which apparently coincide with the recommendation's observations of this assessment.

## **THE CONSTRUCTION AND CONSULTING INDUSTRIES**

28. On the supply side, public works and the housing construction industry operating in a local free enterprise environment and state economic intervention is well established, but not eager or equipped for participation in international markets. The *Cámara Chilena de la Construcción*, CChC (Chilean Chamber of Construction) plays a key role in coordinating policy with the government. It also plays a vital role by assisting the industry through a well-established network of social services and by establishing itself as a de facto consultative group for the infrastructure and housing sectors. The chamber's role, the strict MOP and MINVU registry systems, as well as the booming economy of the 1984-1997 period have to a large extent dictated the development of the industry. However, the current more competitive environment may mean that the construction industry begin reviewing its performance and practices, and that both the private and the public sectors should look for ways to reduce transaction costs.

## **CONTROL AND AUDIT – THE ROLE OF THE CGR**

29. On the basis of its constitutional and legal mandates the CGR has broad responsibility and authority, and plays a key ex-ante review role in public procurement. Particularly relevant to the procurement function are the “*toma de razón*”, which in fact is an ex-ante review from the legal prospective of important decrees and resolutions issued by all state agencies, including the municipalities and autonomous agencies. The CGR carries out “*toma de razón*” over bidding documents, bid evaluation reports, award decisions, etc. for all contracts above a certain monetary value, currently about US \$ 80,000. Also, in the absence of comprehensive procurement legislation, the CGR has developed through legal opinions a considerable body of administrative jurisprudence that has de facto become part of the regulatory framework.

30. The role of the CGR is quite controversial in view of its high degree of influence on important government regulations and decisions, but it is generally well regarded and highly respected. Many officials see the CGR as a hurdle difficult to overcome. Moreover, there is an apparent conflict of interest between the ex-ante review function of the CGR and its audit responsibilities that modern practices avoid. Of particular concern is the possible effect of the CGR review process on the effectiveness of Chilecompra.

## **PROBITY**

31. The high degree of integrity of the large majority of civil servants is considered a major strength of Chile's public administration. In 2002 Transparency International ranked Chile 17<sup>th</sup>

on its probity index among 102 countries Also the local chapter of Transparency International: *Chile Transparencia* actively promotes probity and transparency in Chile in a constructive partnership with the Government. CT developed in 2002 a Risk Map on Public Procurement in Chile, and in 2003 signed a cooperation agreement with the MH to carry out joint studies, training activities and development and dissemination of proposals aimed at strengthening Chilecompra.

## **PERFORMANCE OF PROCUREMENT IN BANK PROJECTS**

32. With the exception of the recruitment of consultants, the use of the “two-envelope system of procurement” and restrictive registration practices for construction and engineering firms, national procurement legislation and procedures in Chile are generally consistent with international practice. Therefore, the Bank has relied considerably on the use of local procedures. Implementing agencies generally adhere to Bank policies; recent ICRs and post reviews did not find major problems. There are, however, shortcomings in the application and interpretation of the Guidelines, which give rise to back and forth consultation and delay; also, there have been some instances of abuse, which in two recent cases led to misprocurement. There is also some reluctance to the use of standard bidding documents (SBDs) for international competitive bidding (ICB); and due to the absence of local standard documents for national competitive bidding and because of the autonomy of the executing agencies to carry out procurement, it is necessary to agree to specific documents with each executing agency which is tedious and time consuming. That suggests that, attention should continue to be given to the harmonization of procedures and the use of standard documents consistent with Bank Guidelines and the country’s modernization objectives.

33. The, implementation of common procedures and documentation under the PPSSP gives the opportunity to overcome shortcomings. The goal should be that local procurement procedures are fully acceptable under Bank projects, with no or few exceptions, particularly for NCB.

34. On the basis of previous experience, the strength of the private sector, the openness of procurement legislation, and the expected mix and size of contracts in the portfolio it is recommended to raise in loan agreements the thresholds for ICB and short list of consultants consisting only of national firms, as well as, for prior review. Likewise the thresholds for national competitive bidding should be fixed at the same levels set in the national legislation for public bidding. Higher thresholds should be supplemented with the development of standard documents and realistic and timely procurement planning.

35. Procurement through Chilecompra should be accepted for Bank projects under the premise that Chilecompra is primarily a technology tool that in itself does not set the procurement rules and procedures, but provides the functionalities to carry them out. It is therefore proposed that, as a first step, the use of Chilecompra’s platform be accepted for: (i) advertising NCB invitations to bid and request expressions of interest for short-lists made solely of national consultants as a substitute for the publication in local news papers; (ii) on-line purchasing of goods on the basis of framework agreements.

## **RISK ASSESSMENT**

36. The overall procurement risk in Chile is low, provided that the individual risks are properly managed. There is no concern about the integrity of public officials and the stated

government policy and practice of enhancing transparency and 100% advertisement of public procurement actions. Civil society and the private sector trust the oversight intervention of the CGR at critical stages in the process. Civil society itself keeps a close watch and constructive dialogue with state agencies. However, until the principles in the Procurement Law are developed and operational, a number of potential risks still remain, particularly to bidders and contractors, and they should be addressed. They are: (i) multiplicity and inconsistency of regulation and the lack of clear directives on procurement strategy, planning, bid evaluation, etc, all of which creates uncertainty; (ii) contractor and consultant registration and qualification procedures that restrict participation and limit competitiveness of the construction industry; (iii) relatively low esteem for the procurement function as reflected in low salaries, which have resulted in inadequate staffing and capacity; (iv) strong state authority to interpret and manage contracts and lack of an adequate resolution of dispute mechanisms.

## **CONCLUSIONS AND RECOMMENDATIONS**

37. The overall conclusion of this report is that Chile has adopted a well thought and comprehensive strategy and action plan for procurement of goods and services that is a best practice example to be followed. The strength of the strategy is that it openly recognizes existing shortcomings, builds on past experience and enjoys ownership at the highest levels of government, as well as a committed and competent team responsible for its implementation. Implementation of the plan thus far is on schedule and it is already showing concrete effects on participation of state agencies and suppliers. However, the road ahead is not easy, particularly with respect to strengthening capacity and achieving standardization of procedures at the operational level. On the other hand, there are already well established and generally sound, although not common practices for procurement of civil works that are in the process of being improved. The various sections of this report highlight those strengths. Specific issues and recommendations with respect to implementation of the PPSSP, Procurement and Management of Civil Works Contracts, and procurement under Bank projects are detailed in paragraphs 57 to 62, 95 and 113 to 118 below. The following are the main actions that are proposed:

By Chile:

- Issue a comprehensive regulatory decree to the procurement law and complementary norms and standard documentation;
- Unify and revisit existing regulation for procurement and management of public works contracts;
- Harmonization of procedures and documents of general use by all agencies;
- Provide continued budget support in order to ensure the financial sustainability of Chilecompra, particularly during the initial years of implementation of the new platform;
- Revisit existing registration and prequalification procedures for public works contractors including the unification of MINVU's and MOP's registries and linking them to DCCP's National Registry;
- Provide full support to the DCCP's capacity building and human resources development Program of Excellence

By the Bank:

- Support implementation of the PPSSP and disseminate it as a best practice;
- Promote the involvement of the DCCP in the development of procurement arrangements and capacity building initiatives in Bank projects, particularly at the municipal level;
- Accept the use of the Chilecompra platform for: (i) advertising NCB invitations to bid and request of expression of interest for short-list made solely of national consultants as a substitute for their publication in local news papers; (ii) on-line shopping of goods under framework agreements;
- Until rules and regulations, manuals and standard documents are issues, continue to insist on the need for consistency with Bank Guidelines and procedures and the adequate use of standard documents in project implementation;
- Raise ICB procurement thresholds to reflect local supply capacity and adjust NCB's in line with the thresholds in the Procurement Law;

## A. BACKGROUND

### THE ECONOMY

1. Chile is an upper middle income country of 15.4 million people with the most robust economic performance in the Latin American Region. However, with an economy highly dependent on exports, Chile is considerably vulnerable to regional and global developments. The economy grew steadily in the 1990's but growth slowed considerably to 2.8 per cent in 2001 and 2.1% in 2002, which may be a sign that steady high growth will be difficult to sustain given current global conditions.

2. In the 80s and 90s Chile carried out a series of public sector reforms that resulted in a considerable improvement in public finance, health, education and social security with emphasis on goods and expeditious delivery of services to citizens. More recently the government of President Lagos has turned its attention towards e-government, financial management and e-procurement. Particular attention is being given to increase public access to information, evaluation of results, decentralization of services and resources.

### PUBLIC PROCUREMENT IN CHILE

3. The aggregate value of public procurement by some 200 national government line agencies in 2001 was about \$ 4 billion or 3.4 % of the GDP, of which 58% was public works, 18% goods and 24% services, including consulting services and concessions. Procurement by some 340 municipalities was about 490 millions in 2001<sup>1</sup>. In addition, some 60 state enterprises and independent agencies procured about US\$ 2.5 billion worth of contracts not subject to public procurement regulations. About 82% of the total value of state contracts is procured on the basis of public competitive bidding.

4. Chile's public procurement system is considered generally free of corruption supported by probity of the civil servants, decentralization, and good budgetary and control systems. However, it is affected by deficiencies that the government recognizes and is taking action to overcome, particularly with respect to procurement of goods and services. The multiplicity of administrative rules, insufficient operational capacity, limited information channels, and inadequate attention on the part of high level officials are some of the main shortcomings. The same as for other public sector activities, procurement is decentralized. The *Ministerio de Hacienda*, *MH* (Ministry of Finance) is the leading institution on the purchase of goods and services. The *Ministerio de Obras Públicas*, *MOP* (Ministry of Public Works) and the *Ministerio de Vivienda y Urbanismo*, *MINVU* (Ministry of Housing and Urban Development) are the leaders on procurement of public works and housing. The *Contraloría General de la República*, *CGR* (Office of the Controller General), on the other hand, plays a key role on the interpretation of regulation and setting up of procurement policy.

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<sup>1</sup> Although a large number of infrastructure works are for the municipalities, with the possible exception of large cities, actual procurement of those contracts is by the Central Government



## LEGAL FRAMEWORK FOR PUBLIC PROCUREMENT

5. There is no unified comprehensive and systematized legal statute that governs public procurement in Chile. The procurement of public works on the one hand, and the purchase of goods and services on the other, have traditionally been carried out under separate legal, procedural and organizational frameworks. Several laws and decrees outline principles, many of which have not been developed through regulation and, are to a large extent applied by state agencies on the basis of administrative norms and legal opinions (*toma de razón*) issued by the *Contraloría General de la República*, CGR (General Comptroller's Office). A corner stone of legislation is the Organic Law of State Administration (*Ley 18.575 Orgánica Constitucional de Bases de Administración del Estado*) that sets the principle that administrative contracts should be awarded on the basis of public or private procurement or direct contracting<sup>2</sup>. Otherwise the organic laws of the various ministries, state agencies and municipalities authorize them to set up their own procurement regulations. This has now partially changed. On July 2003 the President enacted the Procurement Law 19.886 which provides the framework for procurement of goods and service contracts and designates Chilecompra as the standard electronic platform for public procurement. (Paragraph 19). The procurement of public works and concessions continues to be governed by existing regulations as will be discussed later. However, the Government is currently processing a new law that, as the Procurement Law for goods and services, would set up a common framework for procurement of consulting services and construction of public works contracts. (Paragraph 66).

## BANK INVOLVEMENT IN CHILE

6. Bank involvement in Chile is selective. While in the past the emphasis was on infrastructure, particularly on highways and ports, nowadays the focus is on supporting poverty reduction, structural reforms and modernization of the state. The current portfolio consists of five investment projects for a total value of \$ 303.2 million, of which \$ 200.6 million had been disbursed as of September 30, 2002. There is also a GEF grant (\$ 6.4 M) under implementation. All projects are rated satisfactory. Procurement is reported to be generally satisfactory, but recent post-reviews have revealed inconsistencies between Chile's practices and Bank procedures (Paragraph 111). Future Bank assistance to Chile is expected to focus on three broad objectives: (i) sustaining economic growth and social progress; (ii) promoting inclusion, especially of rural populations and vulnerable groups; and (iii) modernizing the state, necessary for achieving the previous two objectives. Thus, the FY 03-06 program includes four HD, three FPSI and one PREM projects.

## CHILECOMPRA

7. In 1998, within the framework of state modernization, the Government established Chilecompra as an electronic information platform for state procurement of goods and services. Development and operation of Chilecompra was given in concession to a private operator and placed under the authority of the former *Dirección de Aprovisionamiento del Estado*, DAE (State Procurement Directorate). Chilecompra was a pioneer effort on e-procurement and had been

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<sup>2</sup> The principle of public and private bidding is reiterated verbatim in several statutes, including the new Procurement Law.

generally considered a model to follow. However, it did not fully meet expectations. While the system had most e-procurement functionalities, it was not efficient or responsive to client expectations. By 2002, a large number of agencies had registered with Chilecompra, but only about 3% of their procurement opportunities were posted on the site, some of them long after the process had been completed. A similar situation occurred on the supply side. Of around 30,000 potential suppliers only 6,193 had registered and only 577 of them were regular users. As a result Chilecompra was discredited. Both government agencies and suppliers did not trust the system and ranked its usefulness and efficiency very low. Consequently the Concession contract became financially unsustainable and was not renewed.

8. An independent study commissioned by GoCh's in 2002 concluded that lack of leadership and inadequate management, cultural resistance and lack of political commitment were the principal reasons for Chilecompra's failure. Based on those findings the Government took a number of policy, institutional and administrative actions designed to introduce transparency to the procurement function. A key action was the placing of a new and energetic management in DAE. It also issued a Presidential Decree 826 in October 2002, which made it compulsory for all central agencies to post procurement related information, and make use of Chilecompra's e-platform, and established within the MH a Procurement Council responsible for guiding and overseeing the function. DAE's new management developed a Public Procurement Strategic Plan for 2000-2004, which is under implementation, as discussed below.

## **B. PUBLIC PROCUREMENT SYSTEM STRATEGIC PLAN**

### **OVERVIEW**

9. The PPSSP focus almost exclusively on procurement of contracts for supply and goods and services. With the underlying objective of enhancing transparency, efficiency and economy, the PPSSP aims at the establishment of a national electronic public procurement system, while setting up a common legal framework for procurement of goods and services only. It also aims at the promotion of e-commerce to state agencies, and to promote international competitiveness in the Chilean industry. Overall, the PPSSP is highly appropriate and conducive to success. It builds on past experience, has full support at the highest level of government, and enjoys strong commitment and leadership for its implementation. While implementation of the strategy is still underway, its conceptual approach and design can be considered a best practice to be followed. Moreover, two years into its implementation the PPSSP already shows important results, particularly in regards to disclosure of bidding opportunities and user participation.

10. The Plan maintains the procurement responsibility (for goods and services) at the agency level but calls for centralization and standardization of the process through Chilecompra, which in addition to adding transparency, should bring about major operational efficiencies and economies. This principle is applied across institutional, technical, and operational dimensions; examples of that are the centralization of informational and transactional capabilities on the new Chilecompra portal, and the use of a single technology platform for it. Other examples are the adoption of country wide coding standards, the creation of a unique supplier Registry, and the aggregation of demand through framework agreements.

11. While Chile is putting technology at the operational center of its strategy, it is not relying on technology as the fundamental input of its PPSSP. This role is reserved for comprehensive

public procurement policy, procedural and institutional reforms, and support to government users and suppliers spearheaded by Presidential Decree 826 of 2002, and the Procurement Law (*Ley de Bases sobre Contratos Administrativos y de Prestación de Servicios*).

12. The Plan envisions work in four major areas (see **Table 1**) and implementation between November 2002 and June 2004. The major areas are: (i) policy and regulation; (ii) institutional change (iii) enhancing capacity and efficiency of Chilecompra and; (iv) technical assistance to government agents and suppliers. Implementation of the plan entails actions on governance, leadership and human resources, institutional reform, technology and finance, which is consistent with the Bank's Strategic Framework for E-Government Procurement (EGP).

13. The main thrust of the policy actions is transparency, including: 100% timely advertising of procurement opportunities and transactions; the introduction of uniform and efficient procedures that facilitate transparency, including the definition and applicability of procurement methods; rationalization of public procurement through aggregation of demand mechanisms, their applicability and justification.

14. On the institutional and management side the actions included the establishment of a Procurement Council responsible for project formulation and oversight of the public procurement system, with the technical support of the *Dirección de Compras y Contratación Pública* (DCCP), and the creation of a Public Procurement Court responsible for resolution of complaints. The Plan considers finance mechanisms that ensure sustainability of the electronic platform and of a national registry of suppliers, the DCCP and user support through the national budget and cost recovery of some services under the premise of free access to basic information and e-procurement services. It also foresees a concerted dissemination effort of the objectives and achievements of Chilecompra amongst government agencies supplies and civil society.

15. Enhancement of Chilecompra operations consisted in the establishment of a completely new electronic procurement platform more powerful, efficient and user friendly with additional functionalities such as purchase orders. This was carried out under an orderly transition process with minimum disruption of operations, which helped the DCCP to promote the use of the system before than the platform was in operation.

16. In a second phase, following an open competitive process, in July 2003 the Government awarded a contract for development and operation of the new electronic platform for Chilecompra.<sup>3</sup> The technical specifications, the bidding process, the evaluation criteria and the contract form were highly conducive to a successful and economic procurement<sup>4</sup>. Competition was high (11 bids) and the three technically qualifying bids were all from strong consortia and offered reliable technology. In a subsequent phase Chilecompra will be integrated with other government systems, in particular SIGFE-DIPRES (Integrated Financial Management System of the Budget Directorate in MH).

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<sup>3</sup> The contract for the electronic platform of Chilecompra was awarded to a national consortium SONDA-ICONSTRUYE. SONDA operated the original platform.

<sup>4</sup> A few features, notably the payment scheme and the combined price/quality evaluation formula used are in fact worth considering not just for other projects but also for adoption as part of Bank standard bidding documents for IT.

**Table 1. Overview of Chile's Public Procurement System Strategic Plan 2002- 2004**

<b>ACTION TRACKS</b> → <b>INPUTS</b> ▼	<b>GOVERNANCE</b>	<b>LEADERSHIP &amp; HUMAN RESOURCES</b>	<b>INSTITUTIONAL CHANGE</b>	<b>TECHNOLOGY</b>	<b>FINANCING</b>
<b>POLICY &amp; MANAGEMENT</b>	<ul style="list-style-type: none"> <li>♦ Pass New Procurement Law.</li> <li>♦ Issue Regulatory Decree.</li> <li>♦ Authorize government agencies to issue RFQ's/RFP's and enter into contracts electronically.</li> <li>♦ Define new procurement methods/thresholds.</li> <li>♦ Legislate framework agreements</li> <li>♦ Make mandatory the publication of all procurement transactions</li> <li>♦ Establish publication time standards.</li> <li>♦ Introduce single goods/service coding standard.</li> </ul>	<ul style="list-style-type: none"> <li>♦ Establish Public Procurement Council as leading policy making body.</li> <li>♦ Establish a Technical Secretariat to the Council to draft plans and evaluate policy implementation.</li> <li>♦ Provide special support to anchor clients to achieve critical mass in system use.</li> <li>♦ Consult and communicate broadly with system users.</li> </ul>	<ul style="list-style-type: none"> <li>♦ Establish Public Procurement Tribunal.</li> <li>♦ Replace DAE with DCCP.</li> <li>♦ Create unique, government-wide supplier Registry.</li> <li>♦ Simplify/standardize procedures across government</li> <li>♦ Promote framework contract mechanism.</li> <li>♦ Facilitate large user (MOP, Health) participation in e-system ().</li> <li>♦ Achieve 100% user participation in e-system.</li> </ul>	<ul style="list-style-type: none"> <li>♦ Provide online, public access all procurement legislation, policies, regulation and standards.</li> <li>♦ Provide online, public access to 100% transaction announcements, timetables and awards.</li> <li>♦ Use e-system to enforce publication time standards.</li> <li>♦</li> </ul>	

<b>ACTION TRACKS</b> → <b>INPUTS</b> ▼	<b>GOVERNANCE</b>	<b>LEADERSHIP &amp; HUMAN RESOURCES</b>	<b>INSTITUTIONAL CHANGE</b>	<b>TECHNOLOGY</b>	<b>FINANCING</b>
<b>TECHNOLOGY PLATFORM</b>	<ul style="list-style-type: none"> <li>◆ Require single technology platform.</li> <li>◆ Adopt full private sector outsourcing policy for system operation.</li> <li>◆ Pay operator for service received, not for investment or operating costs.</li> </ul>	<ul style="list-style-type: none"> <li>◆ Emphasize local public procurement experience in operator selection.</li> <li>◆ Appoint high-level evaluation committee for operator selection.</li> </ul>	<ul style="list-style-type: none"> <li>◆ DCCP to manage operation contract with private sector, establish and monitor service level agreement.</li> <li>◆ Operator to be responsible for technology, user training, system deployment and operation, system promotion, technical support and user support.</li> </ul>	<ul style="list-style-type: none"> <li>◆ Require world class e-commerce software platform.</li> <li>◆ Systematically learn from strengths and weaknesses of Chilecompra l.</li> <li>◆ Adopt industry standards (e.g. web services).</li> <li>◆ Interoperate with legacy government and supply chain mgmt systems.</li> <li>◆ Require high availability, security, reliability, scalability standards.</li> </ul>	<ul style="list-style-type: none"> <li>◆ Government pays for full system operation; no transaction fees to users.</li> <li>◆ Fees may be adopted for value added services.</li> <li>◆ Operation contract assigned competitively using 40% price weight.</li> </ul>
<b>USER SUPPORT</b>	<ul style="list-style-type: none"> <li>◆ Manage “procurement Excellency” program as incentive and recognition mechanism for agency adoption of new procedures and e-system.</li> </ul>	<ul style="list-style-type: none"> <li>◆ Promote “service mentality” among DCCP staff, system operator, and public procurement staff.</li> </ul>	<ul style="list-style-type: none"> <li>◆ Provide comprehensive training program to all system users.</li> <li>◆ Provide comprehensive “Help Desk” facility.</li> <li>◆ DCCP to provide technical support to agencies on procurement process redesign and system adoption.</li> </ul>	<ul style="list-style-type: none"> <li>◆ Provide value-added services (electronic payments, selective notification, etc.) as incentive for system adoption.</li> <li>◆ Make available data base of model bidding documents to purchasing agencies.</li> </ul>	

17. On technical assistance to government agencies, the Plan gives considerable emphasis to increasing participation and development of institutional capacity including: (i) intensive dissemination and training of state agencies through a Program of Excellency on Procurement Management (*Program de Excelencia en Gestión de Abastecimiento*) linked to the MH's Program of Management Improvement (*Programa de Mejoramiento de Gestión*); (ii) human resources development through on the job and formal training of staff in local universities and other entities, including the establishment of diploma courses on procurement management; and (iii) technical support to user agencies on specific problems related to the operation of Chilecompra.

18. Support to suppliers focus on: (i) establishment of a National Registry of Suppliers; (ii) dissemination of information on the benefits of Chilecompra; (iii) support PYMEs (Small and Medium Enterprises); and (iv) dissemination of national and international business opportunities.

#### **THE PROCUREMENT LAW AND DRAFT REGULATORY DECREE (*REGLAMENTO*)**

19. The Procurement Law 19.886, (*Ley de Bases Sobre Contratos Administrativos de Suministro y Prestación de Servicios*) provides the legal framework for procurement of goods (with the exception of war materials) and services by agencies of the executive branch, the regional and provincial governments, the municipalities, the Armed Forces, the Central Bank and the CGR. Contracts financed under credits provided by international organizations, e.g. procurement under Bank projects are excluded from its application. Procurement of public works and concession contracts that constitute about 58% of public investments continues to be ruled by separate legislation as discussed in Paragraph 66. Moreover, the Law establishes mandatory electronic procurement of all goods, services, public works and housing contracts through Chilecompra.

20. The Law aims at increasing transparency and participation in public procurement, including unrestricted participation of foreign bidders. It consists of thirty-nine articles grouped into six chapters dealing with: (i) General provisos on jurisdiction and applicability; (ii) bidder eligibility; (iii) procurement procedures and contract provisos, including procurement methods and applicability, cancellation of the bidding process contract award, bid and contract securities, contract amendments, accession and termination, and registry of contractors; (iv) electronic procurement and information systems; (v) creation of a Court of Public Procurement including its composition, competence, terms and procedures; and (vi) creation of the Directorate of Public Procurement and Contracting (DCCP), with responsibilities including advising public agencies, managing Chilecompra and the Registry of Contractors, assets and staff roster. The Law became effective 30 days after publication for agencies of the central government and on January 2004 for the municipalities, and will take effect on January 1, 2005 for the armed and security forces.

21. With the exception of the chapters dealing with the Court of Public Procurement and the DCCP, which are very detailed, the Law is primarily a statute of principles with considerable latitude for interpretation. Therefore, it requires the issue of detailed rules and regulation, bidding and contract documents. As of July 2004 a comprehensive draft regulatory was under review by the CGR for subsequent enactment by the President. The

Bank provided to the Government detailed comments to the draft in January 2004. The following paragraphs review some key topics in the law and draft regulatory decree.

22. **Procurement Methods.** The Law establishes public bidding as the default procurement method for contracts valued at 1000 UTM <sup>5</sup> (about US\$ 46,000), and provides for private/limited bidding and direct contracting/quotations (*Trato Directo*) as exceptional methods applicable under specific circumstances defined therein. It prohibits the breakdown of contracts with the sole purpose of avoiding public bidding. It also requires that resolutions authorizing direct procurement of contracts be published in Chilecompra within 24 hours of their issuance.

23. The Law identifies the concept of “the nature of the negotiation” (*naturaleza de la negociación*), as one of the circumstances justifying the use of exceptional procedures, based on criteria to be defined in the regulatory decree. However, the draft *Reglamento*, partially defines this concept by given examples of its applicability, such as contracting of consulting services.

24. **Bidding Period.** The draft *Reglamento* prescribes a 10-day minimum advertising period for public procurement (for contracts costing 1,000 UTM or more), subject however, to the requirements of trade agreements signed by Chile. Likewise, the minimum bidding periods for international and national competitive bidding required by the Bank should be consistent with this requirement in the *Reglamento*. For contracts valued between 100 and 1.000 UTM the minimum bidding period is five days.

25. **Two-Stage Bidding vs. Two-Envelop System.** The draft *Reglamento* provides as an option a two-stage system of procurement of goods and services involving the submission of proposals in two digital or physical “envelopes”. The envelope containing a technical proposal is opened and evaluated first; the second envelop containing a bid price is opened only for the qualified technical proposals. This is akin to the two-envelope system of bidding which the Bank does not favor, in part due to concerns about the confidentiality and integrity of the process. The *Reglamento* prescribes specific security requirements for paper and digital proposals, but the Bank recommends against the use of this bidding procedure for international competitive bidding.

26. **Consulting Services.** The Law makes no distinction between procurement of services of non-intellectual nature and contracting of consulting services. This reflects current practice in Chile (see paragraph 92 on engineering consultants), which differs from internationally recommended and Bank required practice of competitive selection of consultants on the basis of invitation to a limited number of qualified firms. This in the end may discourage participation of qualified consultants and negatively affect the quality of consulting services. It would, thus, be highly desirable that Chile considers a separate methodology for procurement of consulting services based on proposals requested from a limited number of qualified firms, and evaluation procedures that give quality preponderance over price (Quality and Cost Based Selection, or QCPBS). In fact the proposed *Reglamento* would allow for the use of such methodology as it lists consulting services as an example of contracts whose award may not be subject to public

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<sup>5</sup> The UTM (Unidad Tributaria Mensual) is a constant value monetary unit nominated in Pesos, valued monthly and in which some government transactions are measured.

bidding because of the “nature of the negotiation” (paragraph 23). This proviso; however, would not apply to consulting services for public works and housing, which fall under different legislation. Moreover, the Law provides for special procedures for service contracts of intellectual nature with individuals.

27. **Electronic Public Procurement System.** The Law makes Chilecompra the standard tool for public procurement of goods, services and works contracts. It requires that all invitations to bid, bidding documents, inquiries and responses thereto, bid prices, administrative resolutions on award decisions, contract documents and other relevant documents for all state and municipal contract, including public works contracts be posted on Chilecompra platform. Moreover, all procurement transactions for goods and services should be carried out through Chilecompra. State agencies are not allowed to award contracts tendered outside Chilecompra. The functionalities of Chilecompra are discussed in detail below (Paragraph 34).

28. **Framework agreements.** An interesting feature of the Law is the formalization of framework agreements as a tool for consolidating the purchase of certain goods and services, such as office supplies, vehicles, air tickets, etc. for efficiency, and better prices. Under framework agreements (awarded on the basis of public bidding), the DCCP agrees with suppliers to unit prices for specific and well defined goods or services. The DCCP develops and posts on Chilecompra catalogues containing those goods, prices and suppliers. Government agencies are required to purchase through purchase orders goods and services posted in the catalogues, unless they can obtain more advantageous conditions elsewhere. However, the *Reglamento* is not specific on the process that purchasing agencies may use to obtain prices better than in the catalogues. In practice public bidding is the only way to obtain better prices, but the draft *Reglamento* seems to preclude that option.

29. **Contractual Provisos.** The Law and draft *Reglamento* prescribe selected contract provisos covering bid and performance securities; subcontracting and accession, amendments and early termination and compensation. However, force majeure and fortuitous events are not specifically mentioned as a ground for contract amendment or early termination event, as they are ruled by civil legislation, are part of the legal framework, and are applied to Law 19.886 in a supplementary manner. The draft *Reglamento* does not include provisos regarding the use of INCOTERMS and payment conditions, which are particularly relevant in international trade.

30. **National Electronic Registry of Suppliers.** The stated objective of this registry is to establish a national database to document the legal and financial status as well as the technical capacity of suppliers, with the purpose of avoiding the repetitive submission of information each time they bid, which is reasonable. Operation of the Registry is the responsibility of the DCCP, but it will be outsourced to private operators. However, government agencies may establish their own registries, and are free to require or not to require bidders to register in the national Registry; also, the administrative and operational linkages between the national and agency registries are yet to be developed, except that the latter must be authorized by decree. The draft *Reglamento* develops in detail the requirements and operation of the Registry that give the impression that its scope and operation may be more ambitious and complex than its stated objective. If that was the case, the Register could end up discouraging participation of suppliers,



particularly foreign suppliers. For example, the formalities for periodic renewal of information and certification appear to be overly rigid; also the draft *Reglamento* proposes four categories of qualification, but it does not determine the nature or value of goods and or services that bidders may be allowed to bid for under each category.

31. Sustainability and usefulness of the Registry will depend on the amount of information to be requested, the intended and potential use across government agencies, and easy submission and updating of information. Evaluation of information and classification of suppliers is generally contract specific and costly, and is better left to the contracting agencies. Registrants, should be able to submit information on line; and electronic links with government agencies should be established for automatic update of suppliers' performance and compliance with fiscal and other obligations.

32. ***The Court of Public Procurement***. The responsibility of this court is to hear and resolve complaints related only to administrative actions or omissions in the bidding process and award of all contracts by government agencies covered by the procurement law (the draft public works procurement law reiterates the jurisdiction of the Court to public works). The Court's responsibility does not include the resolution of contractual disputes. The Law defines in detail the composition of the Court and the proceedings and time-periods for processing complaints under operational rules set up by the Supreme Court (Resolution AD-19.775), and with technical and logistic support by the DCCP. The Court, which is in the process of being established, is expected to shorten the lengthy complaints resolution process by the regular courts, thus expediting the bidding process. That notwithstanding, the judiciary proceedings and time periods defined in the Law, (although apparently short), when coupled with the authority of the Court to suspend the bidding process could lengthen the bidding period considerably. Administrative mechanisms for resolution of contractual disputes are established in Law 18.575.

33. ***Institutional Responsibility***. The Law created the Directorate of Public Procurement and Contracting, DCCP, in the Ministry of Finance. The DCCP takes over the DAE as the agency responsible for supporting implementation of public procurement policy, including: the proviso of technical assistance to government agencies, managing Chilecompra and the Registry of Suppliers, and awarding framework agreements. The Law gives DCCP the authority to impose fees to users for the services it provides. The DCCP is expected to be a lean and efficient agency operating on the basis of limited technical and managerial staff, and the outsourcing of specific tasks to the private sector.

## **THE NEW ELECTRONIC PLATFORM OF CHILECOMPRA**

### **CONCEPTUAL DESIGN**

34. The new electronic platform of Chilecompra was designed on the following premises based on the experience gained from the operation of the original platform:

35. Adoption of the full spectrum of private sector e-commerce facilities that makes possible the use of commercial, off-the-shelf software and focuses operator resources on conversion, deployment, testing, promotion, technical support and maintenance of the system, rather than on bespoke software engineering.

36. Outsourcing to the private sector technical system design, technology selection and acquisition, day-to-day operation of the system and technical support to users, where comparative advantage for these activities clearly resides. The DCCP retains system specification, contract management and client management responsibilities, and is not encumbered with responsibility for operation of complex and fast changing technological facilities.

37. Financing for the operation, initially, is being provided entirely from fiscal resources through direct payments to the operator at least through 2006. This means that neither purchasers nor suppliers will pay transaction fees to the operator. This is a bold decision creating ideal circumstances for system adoption. It is also a fully justified decision, since the government-wide efficiency and cost benefits expected from an electronic procurement system are well documented and sufficient to cover the costs of system operation. However, the Government and the Law allow for Chilecompra to generate income in the form of fees.<sup>6</sup> to replace fiscal resources.

38. Based on the lessons learned from the first contract, payments to the operator are on an output basis, as follows: (i) monthly base payment for the duration of the contract for: making the basic services of the platform available and operating it, providing user support and migration from the original system; (ii) monthly base payments from the date that specific functionalities, grouped in three phases, are made available; (iii) transaction based fees. Base payments declined by 33% during the second and third year/phase and remain constant thereafter, which ensures financial sustainability to the operator. However, the contract ensures no transaction based income.

#### **FUNCTIONALITIES.**

39. The functional capabilities of an electronic government procurement (EGP) system can be broadly categorized into disclosure, transaction, user support and integration facilities. These facilities are described and compared among various countries in the EGP Concepts and Country Experience paper available in the key documents section of [www.worldbank.org/eprocurementforum](http://www.worldbank.org/eprocurementforum). The capabilities of the Chilean system are examined below using that conceptual framework.

#### ***Disclosure Facilities.***

40. The system has the full complement of disclosure facilities traditionally associated with an EGP system. Most of these facilities are already available and DCCP has been successful in increasing the level of compliance with publication requirements by purchasing agencies even before the new electronic platform went online. Information available at the [www.Chilecompra.cl](http://www.Chilecompra.cl) website includes: the PPSSP in both Spanish and English, the new law and other relevant legislation and regulatory instruments, announcements of all upcoming procurement transactions, data base of past transactions and corresponding search and statistical functions. And standard product/service coding catalog. DCCP's objective is to achieve timely publication of close to 100% of public procurement transactions at the end of CY 2003. It is already over 50% and growing.

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<sup>6</sup> Value-added services, particularly those provided to suppliers, may be subject to fees.

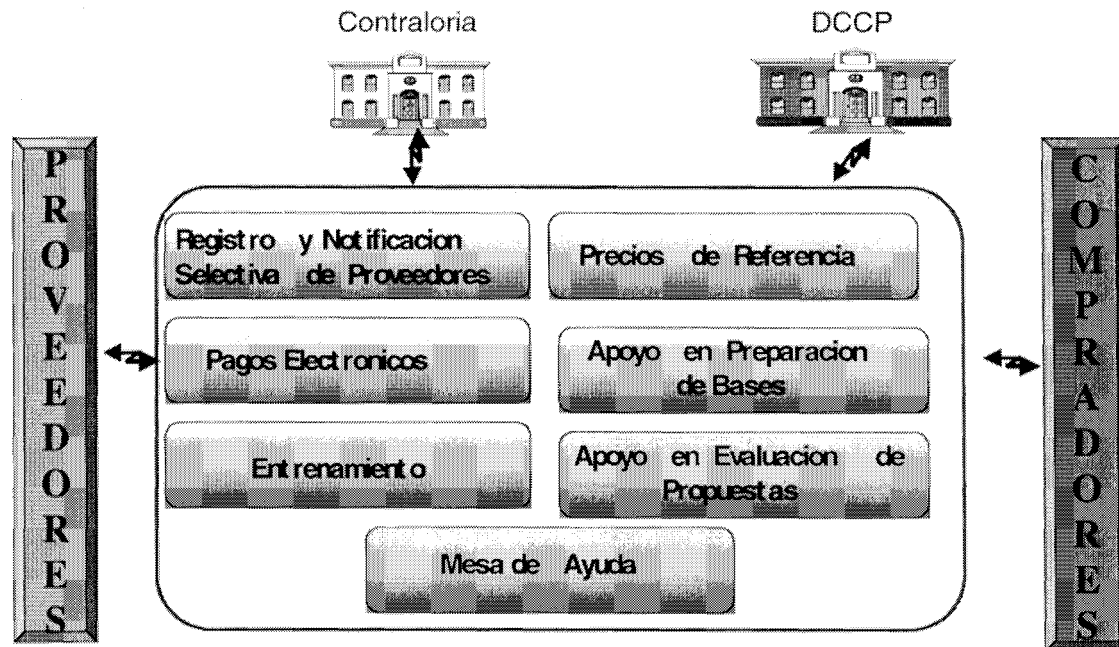
### ***User Support Facilities.***

41. Comprehensive user support and service orientation are essential aspects of Chile's EGP strategy. DCCP already operates a very busy help desk where current Chilecompra users can get both technical and procedural issues resolved. An active training plan is ongoing with extensive participation from government agencies and curriculum determined as a byproduct of issues resolved by the help desk. The user support facilities available in Chilecompra are depicted in Figure 1.

42. Of the seven user support facilities depicted in only two were not yet available at the time of this CPAR, namely the database of reference prices and the electronic payment facility. The Registry of Suppliers will be outsourced to a private vendor on a competitive basis.

### ***Transaction Facilities.***

43. The new platform supports the full spectrum of commercial B2B e-commerce transactions. However, since public procurement transactions differ from private transactions in many respects (procedural requirements, contracting approach, evaluation method, approval and audit requirements, etc.) the platform has configuration capabilities to tailor the system to the requirements of public procurement. The main transaction types are those depicted in **Figure 2** and explained below:



**Figure 1. User Support Facilities in Chilecompra**

44. *Purchase Orders (PO)* These are direct purchase transactions made through the system by authorized buyers, on the basis of electronic supply catalogs. Their volume is expected to increase with the adoption of framework agreements (see below). PO's are equivalent to direct contracts under Bank procurement guidelines. When made in the context of framework agreements, they can be equated to local shopping transactions

under Bank guidelines, since purchasers benefit from a readily accessible choice of suppliers through electronic catalogs.

45. *RFQs ("Cotizaciones/Quotations")*. The vast majority of transactions (those for value less than 1000 UTM or about \$ 46,000) will be processed as competitive electronic proposals due on a stated date and evaluated on the basis of price. RFQ's are subject to standard contracts and tight processing cycles (current standard is two days advance publication and 4 days for submission of proposals). RFQ's may refer to detailed technical specifications and require special delivery or service terms. These transaction-specific elements are provided to potential bidders through downloadable electronic documents. RFQ transactions may be suitable for shopping under Bank guidelines.

46. *RFPs ("Licitaciones/Tenders")*. These are higher value (over US\$ 1000 UTM) electronic transactions subject to longer bidding periods (up to 60 days), combined price and quality evaluation, non-standard technical specifications and potential ex-ante review by the Controller General office (when over US \$80,000). RFP's may refer to packages of goods and services where price proposals are derived from the sum of several price components for goods, incidental services, maintenance and technical support components. The system provides a clarification and specification amendment mechanism and allows merit evaluation through any kind of point and weight scoring scheme. RFP's may be suitable for public NCB and ICB procurement under the Guidelines.

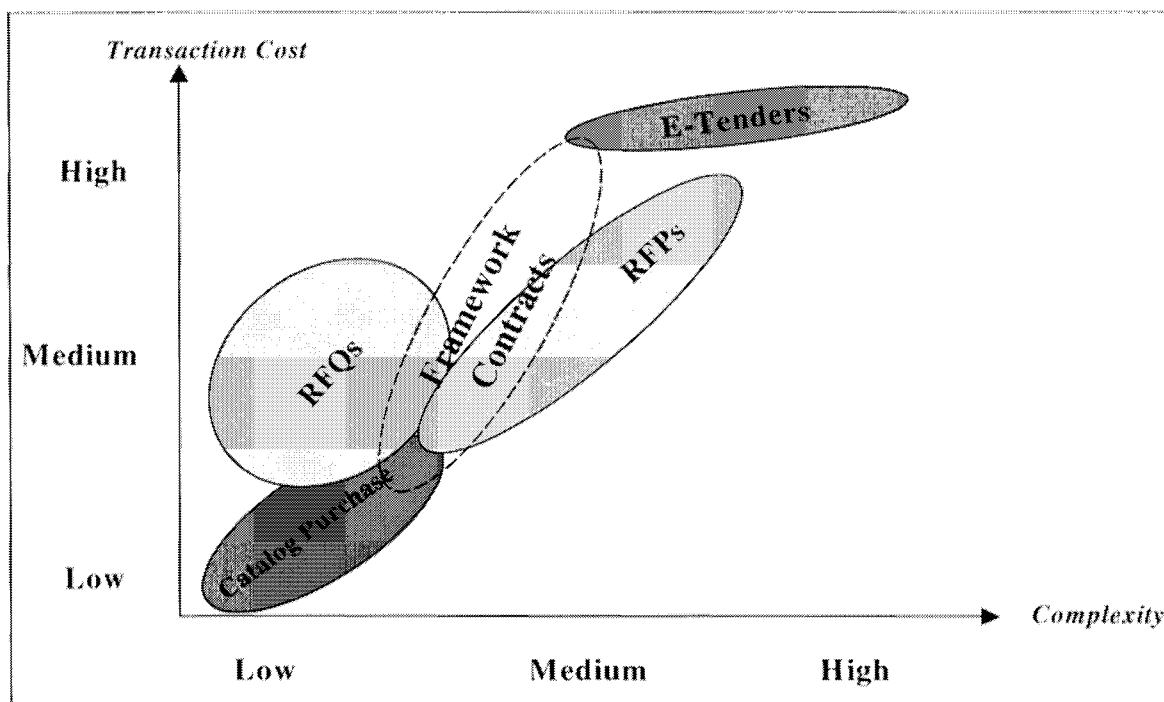


Figure 2 Transaction Capabilities in Chilecompra

47. *Electronic Tenders.* This is a special kind of RFP for procurement of complex contracts. Its characteristics are: (i) different opening dates for the technical and financial proposals; (ii) bid evaluation off-line by evaluation committees; (iii) flexible processing timetable to allow for adequate time for bid evaluation.

48. Electronic tendering under Chilecompra is equivalent to the “two-envelop system” of procurement, which is not acceptable under the Bank’s Procurement Guidelines (for goods and works). However, this functionality can be used for selection of consultants as provided for in the Consultants’ Guidelines.

49. The new Chilecompra platform has repudiation proof encryption and electronic bid submission capabilities, security features ensuring the integrity and confidentiality of bids and safeguards to ensure that bids are opened only under proper authority and only on the published dates for bid opening. These features were not in operation at the time of this review, therefore, were not be evaluated.

50. Regarding the registration of foreign bidders, DCCP intends to establish a special procedure to facilitate their registration and exempt them from automated verifications against the taxation and treasury management systems, or validation of academic titles as required for national suppliers.

#### **TECHNICAL ASSISTANCE TO USERS AND SUPPLIERS**

51. Lack of participation by purchasing agencies and suppliers due to a large extent to inadequate knowledge and technical support was one of the main weaknesses of the initial version of Chilecompra. Therefore, one of the key elements for success built into the PPSSP is the development and implementation of immediate and long-term dissemination and technical assistance activities to users and suppliers. Management of these activities is under a separate line unit within the DCCP (*Gerencia de Clientes*). Considerable work has been done in this area since inception of the strategy. When the *Reglamento* and specific guidelines are issued this program will play a key role in their dissemination and the training of procurement staff. As it is expected that procurement modernization will bring about considerable savings, government agencies are required to cover technical assistance and training expenses out of their own resources. Following are the main features and achievements thus far on this area:

52. ***Program of Excellence on Procurement Management.*** This program aims at assisting government agencies on improving procurement efficiency and transparency, and promoting networking for knowledge transfer. Its focus is on technical assistance on the legal framework and new practices, procurement planning, inventory management, use of technology and development of suppliers. By the end of 2003 the program was implemented and evaluated on a pilot basis in ten agencies. Lessons learned from those pilots are being considered for subsequent country-wide implementation of the program.

53. ***Program of Improvement of Public Management, Procurement System.*** The Public Management Improvement Program (*Program de Mejoramiento de Gestión, PMG*) is a national program run by the Directorate of Budgets (Dirección de Presupuesto, *DIPRES*) of the MH on the field, human resources, customer assistance, planning and implementation, internal audit, financial management and quality of service. The PMG aims at attaining measurable improvement on each field in five steps. It includes agency

and staff incentives linked to the attainment of each of the five stages; salary increases are tied to achievement of PMG goals. Public procurement goals are included in the field of financial management. The DCCP is the agency responsible for fixing goals and evaluating improvement results on par with the Program of Excellence. By the end of 2003 some 131 agencies had included procurement in their PMG plans, out of which 99 and 30 respectively reached stages five and four of achievement. That means that those agencies have obtained a higher degree of understanding of the procurement function, and their managers are committed to implementing and financing the actions required under the PPSSP.

54. **Staff Training.** This program focus on the implementation of short courses and workshops for staff and managers at the regional level on the use of the Chilecompra platform and other specific topics. Thus far the achievements have been eighty-two courses on the platform and 157 workshops for some 7,900 individuals. While the emphasis has been on central and regional agencies, work has started with the municipalities, which make up a clientele with the largest needs. In addition DCCP promoted the establishment of intermediate courses on procurement management in the University of Chile. Some sixty individuals have completed those courses.

55. **Support and Information Services.** This activity consists primarily of the operation of an online help desk in cooperation with the operator of the platform (Paragraph 41). It also entails information and promotion through the platform and a periodic news letter from the director of the DCCP to a select audience.

56. **Integration of Suppliers.** Consists of the carrying out of business encounters with supplier organizations and automatic e-mailing of business opportunities tailored to the preferences of individual suppliers. It also includes coordination with and support to Internet kiosks (*Infocentros*)

## ISSUES AND RECOMMENDATIONS

57. **The Legal Framework and Operational Procedures.** One of the major operational deficiencies of public procurement in Chile has been the lack of consistent practices procedures and documentation among purchasing agencies, which contributed to inefficiencies, and the fragmentation of supply as bidders tended to specialize in bidding for agencies they are familiar with. The Procurement Law and *Reglamento* provide the tools to overcome that weakness, in particular through the mandatory use of Chilecompra and the authority of the DCCP. However, as it reads now, the *Reglamento* would apparently give purchasing agencies considerable leeway for interpretation and change of the requirements therein, which in the end could result in the continued proliferation of procedures and documentation. Thus, it is recommended that for common procedures and requirements the *Reglamento*, while providing flexibilities sets up mandatory boundaries within which purchasing agencies should operate. Moreover, it would be advisable that the standard bidding documents, forms of contract and other documents containing commercial practices and procedures and other documents are of mandatory use.

58. **Registry of Suppliers.** The Registry of suppliers is a necessary tool, particularly for on-line transactions. However, if overloaded with requirements it could become a

deterrent for participation and would thereby limit competition. Therefore, the information required should be confined to aspects related to the legal status of the applicants, their experience and capacity to contract with the state, and whether they meet minimum requirements of purchasing agencies. As foreseen in the Procurement Law, state agencies may establish their own registries designed to meet specific requirements, such as for construction of public works. However, it should be expected that those individual registries will be linked to the National Registry, so as to relieve applicants of the burden of filing and updating the same information in several registries

59. **Consultative Mechanism.** Creating a consultative mechanism with Chilecompra's government clients will go a long way to ensure that system users participate in decisions and enhance their perception that the new electronic platform is a tool to facilitate their work, rather than a bureaucratic requirement. DCCP has already convened the first meeting of the procurement executives of anchor government agencies and invited the executives of any other agency to join

60. **Financing.** While it is a sound objective that Chilecompra eventually becomes financially self sufficient, it is very positive that fiscal resources are made available to fund operation of the platform until 2006 to ensure that it is fully accepted and in operation. Besides, adequate resources should be made available for implementation of the system at the agency level and the training of staff. Otherwise, its rapid and wholesale adoption, as well as its strategic stability, may be compromised. In the meantime, the DCCP should study self-sustaining financial mechanisms for eventual implementation in a later phase.

61. **Framework agreements.** As framework agreements are awarded on a competitive basis by the DCCP, government agencies can directly purchase through those contracts through purchase orders not subject to competitive bidding. This has been particularly the case in the purchase of medicines and big ticket items such as vehicles. However, as Chilean officials traditionally closely adhere to established regulation and practice, buying under the umbrella of framework agreements has encountered some resistance particularly because of price obsolescence.

62. Solution of this issue require practical and innovative approaches that provide real economies of scale for purchasers and suppliers and recognize changing prices. For example, price obsolescence can be dealt with by denominating bid prices in the tender transaction in terms of discount margins over commercial price lists, or by dynamic pricing mechanisms such as reverse bidding when large lots are being procured.

## **C. PROCUREMENT OF PUBLIC WORKS**

### **OVERVIEW**

63. Public Works contracts make the largest portion of public expenditures (about \$ 4.0 billion or 58% in 2002). The Ministries of Public Works (MOP) and Housing and Urban Development (MINVU), which are the pace setters in the sectors, procure and manage contracts in a manner consistent with the general principles of transparency, efficiency and economy, but each one uses its own procedures. Other agencies' public works contract procedures are modeled along the same lines as of the two ministries, but

are not necessarily the same. Public works contracts are different in nature from Goods and Services, therefore, the issue is not the existence of a separate regime for civil works, but uniformity and modernization of processes across ministries, departments within ministries and municipalities. Accordingly, this chapter aims at taking a critical look at public procurement of works and consulting services.

64. Most Chileans share a favorable view of the integrity of the public service. The MOP and MINVU have considerable experience in bidding and contracting civil works. The MOP's bid evaluation and contract award procedures are generally seen as undertaken in an open and transparent manner, although they do not conform to Bank guidelines in several aspects, such as contracting of consulting services and selective bidding of construction contracts based on a registry system. The agencies exercise an active role during contract implementation and their monitoring staff is generally knowledgeable and fair in their judgments. Still, there is room for improvement particularly in the unification of the registry system, bid submission and evaluation procedures, recourse, claims and resolution of disputes mechanisms.

65. On the other hand the public works and housing construction industry operating in a local free enterprise environment and state economic intervention is well established, but not eager or equipped for participation in international markets. The *Cámara Chilena de la Construcción*, CChC (Chilean Chamber of Construction) plays a key role on concerting policy with the government. It also plays a vital role by assisting the industry through a well-established network of social services and by establishing itself as a *de facto* consultative group for the infrastructure and housing sectors. The chamber's role, the strict MOP and MINVU registry systems, as well as the booming economy of the 1984-1997 period have to a large extent dictated the development of the industry. The less favorable current situation in the economic environment means that the construction industry should start to question its performance and practices, and that both the private and the public sectors should look for ways to reduce transaction costs..

#### **LEGISLATION, RULES AND REGULATIONS, PROCEDURES AND PRACTICES**

66. As mentioned before (Paragraph 5) the Organic Law of State Administration 18,575 and the individual organic laws of state agencies and municipalities provide the basic regulatory framework for public works contracts. Otherwise each ministry and municipality follows its own procedures and uses documentation issued through presidential administrative directives. Decree-Law 600 of 1996 establishes a separate regime for concessions of public works services. As Chile is a civil law country, regulation subordinates the contractor to the employer, who has a prominent role in the administration and interpretation of the contract. The role of independent supervisors in the administration of the contract is limited to advising the employer. Concession contracts, however, while allocating a lion share of contract risk to the concessionaire, include proviso for compensation of events due to changes by the employer, or by changes in demand, as well as mechanisms for resolution of disputes.

67. The Government is currently processing a draft law for procurement of studies and public works investment projects (*Ley de Bases de Licitación de Estudios y Proyectos de Inversiones Públicas*), by public agencies. This bill spouses the same principles of transparency and efficiency, covers the same agencies and includes similar



provisos as the Procurement Law. It would: (i) establish a Registry of Contractors and Consultants managed by the MOP; (ii) confirm public competitive bidding as the default procurement method and establish strict requirements for other exceptional procedures; (iii) confirm Chilecompra as the electronic platform for public works procurement; (iv) highlight some contractual provisos such as securities, amendments, termination and subcontracting; (v) confirm the jurisdiction of the Court of Public Procurement to public works contract procurement. In contrast with the Procurement Law, the Public Works Law would not formally designate a specific agency as the policy leader on the field, as the DCCP is for procurement of goods and services. It is expected, however that in practice the MOP would continue to play such a role in coordination with the DCCP, particularly regarding development of model documentation and procedures.

68. The same as the Procurement Law, the proposed public works law, although very specific on certain matters such as scope of contract amendments, it is an statute of principles which would require detailed development through rules and regulation. However, in contrast with the procurement of goods and services, the various branches of the MOP have developed a considerable number of rules and regulations that should be revised and integrated into a single consistent set for general use throughout the MOP, other ministries and municipalities. In fact the MOP reports that it is currently revising the regulation on public works contracts (*Reglamento de Contratos de Obras Publicas* hereto after *Reglamento de Contratos*). The objective and scope of the existing Registry of Contractors managed by the MOP would also provide the basis for the national registry of consultants and contractors, but it would have to be overhauled in consideration of its extended role, as well as for increased efficiency and participation in the procurement of works and engineering consulting services; it should also be made consistent with the National Registry of Suppliers. The general views on the Procurement Law and the draft *Reglamento* stated in this report apply to the proposed public works legislation; additional comments specific to the existing laws and regulation works are discussed in the following paragraphs.

69. From the review of a sample of MOP's documentation for a road construction contract it is apparent, as shown in *Table 2*, that the question of where in the regulation and contract documents specific matters should be covered has not been systematically addressed. For example, topics such as performance security, price adjustment, claims, and termination by the agency are not addressed in the general conditions, as it is practiced in most countries. Also, the specific requirements related to different topics are scattered in the different regulations and are some times inconsistent. The general conditions should contain the basic proviso affecting the rights and obligations of the parties involved, which are typical of the contract implementation phase in most projects. A separate directive should set forth exclusively the bidding procedures for selecting the contractor.

**Table 2. Location of Selected Procurement Topics in the Legal Documents**

	Law 15875	Law 5840	Decree 15/92	Gnrl. Cond.	Partlr .Cond.
<b>General</b>					
Authority to contract	x	x			
Contract method	x	x			
<b>Instructions to bidders</b>					
Registration			x		x
Bid security			x		x
Contract award			x	x	x
Contract acceptance		x		x	x
Recourse	x				
<b>Contractual matters</b>					
Contractor's general obligations			x	x	x
Site		x	x	x	
Performance guarantees		x	x		x
Retention money			x	x	x
Payments		x	x	x	x
Advanced payment		x	x	x	x
Price adjustment			x		x
Variations			x	x	x
Claims			x		
Disputes					x
Works insurance			x	x	
Third party insurance			x	x	x
Termination by agency			x		
Penalties			x	x	
Handing over			x	x	x

#### **PRE-CONTRACT PROCESSES AND PRACTICES.**

70. *Procurement Methods.* The acceptable procurement methods for public works contracts are substantially the same as for goods and services prescribed in the Procurement Law (paragraph 22). In the MOP public bidding is mandatory for contracts valued at 1000 UTM (about \$ 46,000). The bidding period should be at least 40 days (Decree 826/2002). However, this is not a standard requirement for all public works contracts. Also, public bidding, with no limit in the number of potential bidders, is considered expensive, risky and time consuming in Chile. Accordingly, participation in public bidding for all contracts is preceded by a registration and pre-qualification process. Contracts below the public bidding threshold are subject to a competitive process and mandatory advertising, but the minimum tender period is only 10 days. Contracting on a sole source basis is allowed in case of emergency, for works maintenance and repair, community works, works in the Isla de Pascua, and when no bids are received in a previous competitive process. Registration and prequalification are not in themselves objectionable practices, but the manner that the process takes place, as discussed below, apparently restricts competition and increases cost.

71. *Advertising.* As required by the Procurement Law bidding documents, invitations to bid, contract awards and related documents are to be advertised in Chilecompra, and the MOP in particular has taken decisive action to meet that requirement using standard templates. Chilecompra features an exclusive and prominent page for MOP contracts. Advertising in local newspapers is optional, but is a practice that would be gradually discontinued, which may be an issue for Bank finance contracts.

72. *Registration of Bidders/Prequalification* Registration of prospective bidders is a standard feature in Chile. There are currently two major registries of public works and housing of the MOP's and MINVU's. All construction and consulting firms must register to participate in bidding for contracts with these ministries. The MOP's registry encompasses a wide range of civil works and engineering contractors while the MINVU's registry focuses on housing and urban development works (see **Box 1**). Other contracting agencies use either registry at their discretion. The registries were developed in the early nineties to protect public funds, prevent contractors' defaults, and ensure quality of construction. They have contributed to the unification of standards and forms for pre-qualification of contractors and to discipline the construction industry in its initial stages of development. However, its current objective and scope should be revisited as an input to the proposed new national registry.

### ***Box 1. Registries of Contractors***

#### **MOP Registry**

The MOP's civil works comprises two main categories: major and minor works. The registry for major works is managed centrally by the DGOP through a committee and classifies the construction companies in thirteen work specialties and in three categories based on the prospective value of works, personnel and experience. The registry for minor works is managed by the thirteen MOP regional offices and divides the construction companies in two value categories and nineteen specialties. The MOP's registry is open to international contractors. Applicants that wish to be registered in a particular category should show a minimum financial capacity equivalent to 15% of the upper limit of the works budget assigned to that category. The experience of a firm is allocated on the basis of its own and that of its professional staff. The MOP's General Directorate of Public Works (DGOP) manages the registry, within the framework of fifty-eight articles on the subject included in MOP's decree 15/92, which allows the government to shape the industry. As of May 2003, there were 376 contractors registered in the MOP's registry for larger works and about 600 registrations for minor works.

#### **MINVU Registry**

The fifty-two articles of decree DS127 of 1977 regulate the MINVU's registry, which is simpler than the MOP's and gives more flexibility to joint venture applicants. A national coordinator manages it centrally, but the applications are handled at the regional level. It classifies the contractors in nine specialties and four categories based on prospective bid value, minimum capital and experience. As of May 2003, there were 2000 firms registered.

73. Both registries entail a rigorous classification and qualification procedure requiring a full assessment of the financial standing of the applicant and of its technical credentials. Information in the registry is updated and assessed every year. When their staffing situation changes, firms must inform the registry. Managerial and technical competences as well as experience are assessed through certification from clients, supplemented by a detailed review of the number and qualifications of the staff.

74. The MOP's registry requirements and evaluation criteria are complex and strict as they intend to make an objective process out of one which is essentially subjective. However, the decision on an applicant's registration, which is final, is made by a

committee that “will consider and evaluate, at its own discretion, the applicant’s documentation and will decide on his registration”(article 34 of MOP’s decree 15/92). The strictness of the system also works to the detriment of more effective competition as it may reject qualified applicants because of insignificant formalities. Reportedly the revision of the registry’s rules currently under consideration would introduce elements to increase objectivity and transparency to the classification of contractors.

75. Maintaining independent registries by state agencies is redundant, possibly inconsistent and costly for the state. Moreover, filling out and maintaining applications by contractors and suppliers requires money and effort that likely discourage participation, particularly among smaller firms. The cost to contractors and government agencies of running the registries has not been quantified but is likely to be considerable, particularly for small companies. Also, there is some duplication of effort in completing the registration for each ministry, since the basic requirements are similar.

76. Fortunately the proposed public works law would establish an unified national registry for works contractors and consultants (Paragraph 67). Such an unified registry would result in significant savings for the state and the industry. For it to be effective, however, development of the proposed registry should be carried-out concurrently, on the same general principles as the DCCP’s Registry of Suppliers, including basic information on the legal, fiscal, and commercial situation of contractors as well as general information on their capacity and experience. However, the assessment of bidders’ capacity for specific contracts, including their financial and technical qualifications, should be the responsibility of the contracting agencies on the basis of the information in the registry. Management of such a registry should be independent and neutral within the MOP. Also consideration should be given to the establishment of an registry advisory board made up of the users and the industry.

77. ***Bid submission and qualification of bidders.*** Only registered firms are eligible to bid. In addition, eligible bidders are required to submit, five days before the deadline for bid submission, documentation updating key registry information along with a formal declaration about knowing the site conditions and scope of the works (Articles 68 and 70 of the by-laws of Public Works Contracts issued through Decree 15 of February 1992) . On the basis of that information eligible bidders are further prequalified and issued a bid form only three days before the deadline for submission of bids. Pre-qualified bidders submit proposals in two sealed envelopes, one with technical data and proposed work program; the second with the bid price and back up information. This procedure entails a tight schedule to complete the preparation of bids. It also implies unnecessary expenses to prospective bidders who are at the last minute disqualified. In the end these unusual requirements discourage participation, reduce competition and ultimately increase costs, let alone rising potential compromise on transparency. Also, this is a “two-envelope” system of procurement, which is not acceptable under Bank financed projects.

78. ***Bid Opening and Evaluation.*** At the time of bid opening the envelop containing technical data is opened first. The information therein is reviewed for completeness. Proposals with incomplete documentation are rejected on the spot and the respective envelopes containing the bid are returned unopened. There are no defined criteria for bid evaluation, but in general the evaluation focuses on ensuring that the letter of the instructions to bid is closely met. Therefore, there is little flexibility and discretionary

judgment, which is generally seen in Chile as an open and transparent manner of carrying out the evaluation.

79. Rejection of bids at opening is a undesirable and non reversible practice that should be discontinued. Substantial responsiveness plays an essential role in bid evaluation. It is not a simple matter that cannot and should not be hurriedly resolved at bid opening. Otherwise, there is a risk of rejecting responsive and good proposals because of formalities that in some case may be amendable without substantive change to the proposal. Besides, incomplete proposals can always be rejected later in the evaluation process. This practice would reportedly be reconsidered under the revised *Reglamento de Contratos*.

80. **Compensatory unit prices.** This MOP practice consists of modifying the winning bidder's unit-prices in proportion to the contract's official cost estimate while maintaining the total bid prices unchanged, with the apparent purpose of preventing front-end loading of bids (article 4 of decree 15/92). This practice contravenes the very essence of unit-price contracting that contract payment is on the basis of unit prices proposed by the bidder. Risk and cost are closely linked and bidders should be entitled to price risk according to its own business condition. The procedure should be abolished. In case of an unbalanced priced bid, the contracting agency may request an increase in the amount of the contract performance guarantee. In fact, the draft *Reglamento* to the Procurement Law provides for this kind of mechanism for goods and services contracts. Alternatively, whenever possible, contracts could be awarded on a lump-sum basis and paid in accordance with well-defined progress indicators. The revised *Reglamento de Contratos* would reportedly phase out this proviso.

81. **Bid evaluation and Contract award.** Article 81 of the public works directive (decree MOP 15/92) authorizes the contracting agency to accept any offer, except when the conditions of contract spell out the evaluation system. The Directorate for Public Works' conditions of contract however, establish that "the agency will award the contract to the bidder whose offer complies with all the requirements of the bidding documents and that is evaluated as the most convenient for the interest of the state." Although in practice, the lowest bid price is probably the most frequently used criteria for awarding the contract, the evaluation criteria is not explicit and may be subjected to different interpretations. In this regard, the policy should be more explicit in its economic intent. Bid evaluation criteria should be fully disclosed in the bidding documents. A commonly used criteria is that the contract is awarded to the bidder submitting a responsive bid at the lowest cost, provided that it has the capacity to execute the contract. When factors other than price are considered in the evaluation, they should be, to the extent possible, valued in monetary terms. The revised by-laws would apparently adopt this procedure.

82. **Contract formation.** Contract award is formalized through administrative resolutions or decrees. The award resolution is then submitted to the CGR for no-objection (*toma de razón*), after which the bidder subscribes and notarizes the resolution to formalize the contract deed. A copy of the notarized resolution is forwarded to the contracting agency's documents office. The contract is perfected on the date it is received at the documents office.

## CONTRACT ADMINISTRATION

83. **General conditions of contract.** There is not a set of standard general conditions of contract used through government agencies. Contracting agencies have developed their own conditions frequently modeled on their organic laws and on MOP's or MINVU's general conditions of contract. These conditions are based on the civil law approach, which assigns an active role to the employer in the interpretation and administration of the contract, but requires that he exercises his role in accordance with good governance principles. The development and implementation of standard conditions of contract to be used by any government agency should be sought. It will benefit both the contracting agencies and the contractors.

84. **Contract supervision and implementation.** While MINVU's contracting system is decentralized and implemented by the regional offices of the Ministries (*Subsecretarias Regionales Ministeriales*, SEREMI); contracting in the MOP is more centralized because of the importance and size of the works. The employer who appoints one of its professionals as its representative holds responsibility for contract administration. If a consultant is hired, his role is limited to assist the employer representative and he/she has a duty of skill and care in exercising this function. Monitoring staff are generally knowledgeable, experienced, and fair in their judgments.

85. In practice, there is reliance on the contractor's self-control, as the parties tend to rely more on trust and credibility to ensure that the work is completed and reimbursed appropriately. Although compliance with the specifications is very important, attention to the issue of what can be done to improve the efficiency of the construction process should not be overlooked. For example, consideration could be given to the concept of strategic supervision of the construction operation, where an independent group audits, inspects, and monitors the financial, technical and performance aspects of the contracting agency, the contractor, and the supervision team with regard to the contract implementation aspects.

86. The basic employer obligations of enabling the contractor to execute the works and of paying for such execution are well established. Payments are normally made within 30 days. The more sophisticated agencies have developed and maintained good track records of contract performance indicators, which help them to evaluate whether the objectives of quality, time, and cost are being achieved.

87. **Recourse, claims and disputes.** The Chilean constitution states the person's right to make requests to the public authority regarding any private or public issue (article 19.14) and to sue the administration in case of non-compliance with the law (article 38). However, with the exception of concession contracts, topics such as recourse, claims, and disputes do not have in the Chilean regulation the same relevance as it does in other countries. This may be so because of the prominent role of the contracting agency in the contract. In fact, other than the courts, the only proviso for recourse that a bidder has, in case of the procuring agency's non-compliance with the law, is given in article 10 of law 18,575. This article allows for impugning the acts of the government.

88. Contractors' claims and disputes during contract execution are submitted to the contracting agency's director for his summary resolution. An informal dispute resolution

panel is sometimes provided for in the particular conditions of contract. It is made up of three persons, one named by the contractor and the other two by the employer. The panel submits its recommendations to the agency's director who is not bound to accept them. Because of the agencies' active role in the implementation of the contract, the resolution of issues is often anticipated before they become disputes. In spite of this, the contractor is in a weak legal situation with respect to the employer and, in practice, the system appears to be rather paternalistic. Certainly for the sake of transparency and equity principles, the regulation should include explicit provisos regarding recourse, the processing of claims, and independent resolution of disputes mechanism.

89. **Securities.** The provisos for contract performance guarantees are prescribed in different parts of the regulation. Article 109 of law 15,840 establishes the bank guarantee (boleto bancaria) as the preferred security to guarantee contract performance but allows the option of guarantees issued by insurance companies, provided the instruments are of the same type as those issued by the banks; the requirements for the amount and duration of the guarantees are prescribed in articles 53 and 90 of the MOP's 15/92. These articles are confusing and lack consistency; therefore, deserve revision.

#### **SELECTION OF CONSULTANTS**

90. There are no public sector standard procedures for recruitment and employment of consultants. Consulting services are generally contracted on the basis of open competitive procedures similar to those for public works contract and goods. Consulting firms are required to register, and are classified and qualified in the relevant registries. Requests for proposals are publicly advertised. All registered and qualified firms are eligible to submit proposals. Technical and financial proposals are submitted in two separate envelopes. Proposals are evaluated on the basis of criteria spelled out in the request for proposals (RFP). The technical proposals are opened and evaluated first, subsequently the financial proposals of those passing a minimum qualifying mark (MQM) are opened, and the combined evaluation is carried out assigning weights to the technical and the financial proposals. Some agencies award the contract to the proposal the MQM and offers the lowest price. Most consulting contracts are on a lump sum basis but include a variable portion to allow for unforeseen work.

91. The weight assigned to price can be 40% or higher. In the case of complex assignments the financial proposal may be assigned only 15%. In certain circumstances, to allow for more selectivity, additional qualification requirements are added in the request for proposals and the MQM set at very high levels. In this manner the number of qualifying firms and proposals may be reduced to a very small number.

92. Selection of consultants based on a short list is seldom done. Participation is open to all registered firms. On the other hand, as for construction contractors, the strict registration and qualification procedures lead to narrow specialization and the predominance of some few firms. Therefore, in practice the number of proponents is generally low. Single source selection in the public sector is practically unknown, except for certain entities such as universities.

93. The Association of Consulting Engineers (AIC) promotes the Quality and Cost Based Selection (QCBS) method of selection, and is against using least cost as a selection

method. Private sector institutions and state owned enterprises such as CODELCO and ENAP follow selection procedures similar to those World Bank. On the other hand public sector institutions tend to consider the hiring of consulting services similarly to the procurement of goods, therefore, using price as the main evaluation and contract award factor.

94. In view of the above circumstances, the best qualified consultants may find working for the private sector more attractive than for the public sector. In the long-run the public sector should consider a more quality oriented selection approach on the basis of shortlist procedures.

### **Issues**

95. The transaction costs to both the public and private sector in the procurement process for large civil works contracts can be significant. This is particularly so in a decentralized service system driven by a regulatory approach, based mainly in probity principles, as is the case of Chile. This transaction cost includes the cost of bidding and the internal administrative costs involved in such processes as preparation of bidding documents, advertising, registration and qualification of bidders, bid evaluation and contract award, performance monitoring and feedback. An indication of the magnitude of these costs may be inferred from the comments made by some of the contractors and consultants interviewed that, bidding for government contracts is at least twice as expensive as bidding for similar projects in the private sector because of the greater number of government requirements and more time involved. However, the return to a modest economic growth has brought a concern for increasing the efficiency of the processes involved in the different stages of a project. In this context, the government agencies should revise the internal administrative cost of their procurement activities to ensure they remain competitive. The proposed revision should pay particular consideration to measures such as:

- Enacting national Public Works Procurement Law, rules and regulations along the same lines as and consistent with the Procurement Law; the proposed draft law on this subject is an excellent good step in this direction;
- Inclusion in the proposed law of specific competitive procedures for selection of Consultants based on invitation to a short-list of qualified firms, and evaluation criteria that gives to quality of the technical proposals much higher weight than to price;
- Establishing a single and simple national registration system for civil works contractors and for consultants on the basis of an independent review and lessons learned from the existing registries, and should be consistent with DCCP's National Registry of Suppliers
- Adopting the use of electronic bidding through Chilecompra to replace and expedite paper based transactions;
- Developing standard bidding documentation to be used by all government agencies;



- Making more use of design and build type of contracts to create incentives for contractors to perform better, and for contracting agencies to seriously consider the risks involved
- Implementing a systems conducive to monitoring and measuring procurement and contract management transaction costs.

## **D. INSTITUTIONAL FRAMEWORK, CONTROL, PROBITY**

### **INSTITUTIONAL RESPONSIBILITIES**

96. While the Procurement Council (Paragraph 6) and DCCP, and the MOP/MINVU are respectively the leading national agencies on procurement of goods and services, and of public works and consulting services there under, each state agency is autonomous to plan and undertake procurement in accordance with its own requirements, and up to now under their own rules. The two-tier approach transcends to the operational level. Within each ministry, central agency, and municipality procurement is the responsibility of separate and independent units: one for goods and services, generally attached to administrative departments, and the other for public works attached to engineering departments or the like. Moreover; in general, each operational department has its own procurement units. However, some individual ministries rely on the MOP for design and construction of infrastructure works, such as school buildings for the Ministry of Education. Overhauling this compartmentalized institutional structure is a key element of modernization that deserves to be revisited with the goal of facilitating implementation of the PPSSP.

97. Consistent with the emphasis on a gradual decentralization strategy, the central ministries are generally responsible for setting priorities and policy, and for procurement of large contracts, while the SEREMIs are responsible for implementation of investment plans drawn by the Regional Councils and *Intendentes Regionales* upon consultation with the *Consejos* and *Intendentes Regionales* and funded out of the National Budget, as well a most works contracts for the municipalities. Expenditures and procurement thereto by the municipalities themselves are generally limited to operating expenditures, including goods and services, and public utility services.

98. Under the PPSSP, individual agencies of the central administration maintain their investment and procurement autonomy, but are required to use Chilecompra as the transaction and information tool for all procurement. Moreover, they are required to purchase certain standard items through framework agreements subscribed by the DCCP (Paragraph 28) with the objective of reducing prices and increasing efficiency. There, is however concern among agencies that the DCCP may gradually return to past practices where the former DAE carried out procurement for all the central agencies with mixed success.

99. No different from other LAC countries, it is apparent that the procurement function has been relatively weaker than others within the public service. Agency managers have traditionally neglected the function as they give it no strategic value, thus, depriving it of adequate resources. Most critical of all is staffing. In general the heads of

procurement units, let alone other staff, have not had the expertise and training in modern techniques to perform the function. Moreover, there is no procurement career stream in the civil service.

100. The PPSSP, therefore gives considerable emphasis to dissemination of information and knowledge transfer of modern procurement techniques and the use of Chilecompra's platform through the programs of Excellence on Procurement Management and Improvement of Public Management (Paragraphs 52 to 55). The DCCP has aggressively pursued implementation of these programs with positive response from managers and staff, particularly among national agencies at the central and regional levels.

101. Institutional weakness deepens as operational decentralization reaches the regional and municipal levels. In particular, a large number of the 340 municipalities face major issues not only on staffing, but also on availability and access to information technology and connectivity, which if not adequately resolved, may hinder implementation of government decentralization in general, and procurement in particular. This is reflected in the fact that, while application of the principles and procedures in the Procurement Law by the municipalities became effective on January 1, 2004, the mandatory use of Chilecompra's information and on-line procurement platform has been postponed. Starting on June 1, 2004; the municipalities will be gradually incorporated into the platform in three phases by December 31, 2004. Accordingly, the DCCP is focusing technical assistance efforts to ensure that the municipalities meet the new targets. However, since the municipalities are strapped for cash, they would not have the funds to pay for technical assistance services and investments that the central government agencies are required to fund out of their own resources. In addition there are political factors that affect the process, while some majors have welcome the advent of Chilecompra with a positive and open mind, others see it as intromission on their autonomy. Therefore, meeting the proposed target is going to be a considerable challenge for the municipalities and the DCCP, particularly considering that about 250 of the 340 municipalities would be incorporated in the last quarter of 2004.

102. The critical issues facing the municipalities on procurement, however, cannot be tackled in isolation, but under the overall umbrella of municipal development. The Sub secretariat of Regional and Administrative Development (*Sub secretaria de Desarrollo Regional y Administrativo*.(SUBDERE) of the Ministry of the Interior, is responsible for advancing decentralization in cooperation with other ministries agencies, including the DCCP for procurement. The Bank funded and SUBDERE implemented Second Municipal Development Project (PROFIN) piloted procurement training for the municipalities in 2003 with positive results. The proposed third PROFIN and Infrastructure for Territorial Development projects would be excellent vehicles for the Bank to support modernization of public procurement and for the use of Chilecompra, within the general framework of decentralization and municipal development.

#### **CONTROL AND AUDIT – THE ROLE OF THE CGR**

103. On the basis of its constitutional and legal mandates the CGR has broad responsibility and authority, and plays key ex-ante review and regulatory roles on public procurement. While the CGR shares its control function with the Chamber of Deputies

and the judiciary, it is an autonomous body independent from all branches of government. But more importantly, its role and authority goes beyond the mere control function. The responsibilities of the CGR comprise a variety of activities unlike similar entities in LCR. The CGR : (i) carries out ex-ante control of legality (*toma de razón*); (ii) issue legal opinions on the interpretation of matters of its competence; (iii) conducts audits, inspections and prosecutions; (iv) control compliance of statutory rules by public servants and keeps a registry of those personnel; (v) keeps the national accounts and reviews financial statements issued by state fiduciary agents; and (vi) reviews and keeps a database of laws, treaties and regulations. In connection with those activities the CGR is particularly concerned with the administrative probity of public officials, and carries out extensive training therein.

104. Particularly relevant to the procurement function are the “*toma de razón*” and legal opinions. The “*toma de razón*” is in fact an ex-ante review from the constitutional and legal prospective of supreme decrees and resolutions issued by all public agencies, including the municipalities and autonomous agencies. With respect to procurement the CGR carries out “*toma de razón*” over draft rules and regulation, bidding documents, bid evaluation reports, award decisions, etc. for contracts above a certain monetary value (currently about \$ 80,000). Also, in the absence of comprehensive procurement legislation, the CGR has developed through legal opinions emanating from the “*toma de razón*” a considerable body of administrative jurisprudence that has de facto become part of the regulatory framework. In fact, the CGR is charged with the compilation of laws, decrees, rules and regulation and a bulletin on administrative jurisprudence. It is not clear if said jurisprudence is integrated into the draft *Reglamento* to the Procurement Law.

105. The role of the CGR is quite controversial in view of its high degree of influence on important government regulations and decisions, but it is generally well regarded and highly respected institution. On public procurement the CGR plays a critical role as it monitors and contributes to transparency and probity on the procurement and contract award of large contracts, and provides legal and regulatory guidance. However, many officials see the CGR as hurdle difficult to overcome in particular because of the time that often it takes to carry out the “*toma de razón*”. While, by law the CGR is required to issue its opinions within 15 days of reception, it apparently takes longer because the CGR also has the option of extending the review period for grave reasons. This problem is highlighted by the fact that, existing legislation notwithstanding, Article 33 of the proposed public works law would specifically require the CGR to carry out “*toma de razón*” within fifteen working days. The proposed article apparently does not add anything to what is already provided for in Article 10 of the CGR Law 10.336, but is symptomatic of the problem. Moreover, the effectiveness of Chilecompra’s electronic procurement facilities could be seriously hampered if CGR’s actions are not carried out timely and on-line. It should be expected that an ongoing CGR modernization project supported by IADB would address this potential issue.

106. Besides, there is an apparent conflict of interest between the ex-ante review function of the CGR and its audit responsibilities that modern practices avoid. However, this is a general subject which is outside the scope of this review, which should be looked

into in more detail under the Financial Management Accountability Assessment FMAA for Chile.

## **PROBITY**

107. The Government's policy to prevent corruption is guided by Law 19653 on Probity in State Administration that aims at establishing an environment in which transparency and irreproachable, honest and loyal behavior are the norm for public officials. In fact, the high degree of integrity of the large majority of civil servants is considered a major strength of Chile's public administration. In 2002, Transparency International ranked Chile 17<sup>th</sup> on its probity index among 102 countries. It ranked above industrialized countries such as France, Germany, and Spain, and well above the other Latin American and the Asian nations, except for Singapore and Hong Kong.

108. The Government established in January 2003 a Presidential Probity Commission (*Comisión Asesora Presidencial para el Fortalecimiento de los Principios de Probidad y Transparencia Pública*), but its role and achievements so far are not apparent. On the other hand, the local chapter of Transparency International: *Chile Transparencia* (CT), and its Executive Secretariat FORJA (*Acción Ciudadana para la Justicia y la Democracia*) actively promote probity and transparency in Chile in a constructive partnership with the Government. The emphasis of CT has been on the promotion and dissemination of the norms and procedures that rule the acts of public officials. It has also pursued the objective of making probity and transparency part of the agenda of civil society organizations.

109. The CT prepared in 2002 a Risk Map on Public Procurement Chile highlights existing shortcomings, which to a large extent are confirmed by this assessment (Paragraph 119). Also, in July 2003, CT and MH signed a cooperation agreement to carry out joint studies, training activities and development and dissemination of proposals aimed at the strengthening of Chilecompra. Among others, the agreement calls for: (i) research and compilation for consideration in the drafting of the regulatory decree to the Procurement Law; and the carrying out of a workshop to review the draft decree with wide participation of government officials and representatives of civil society; (ii) cooperate on the dissemination of procurement regulation; (iii) develop a ranking that reflects the use of Chilecompra by state agencies; and a reward mechanism therein; (iv) develop and validate methodology to measure transparency in public procurement; and (v) promote the use of Integrity Pacts.

110. The Government's stated policies and effort for probity notwithstanding, there have been recent incidents of alleged misbehavior by public officials, which although not of extreme gravity, give reason for concern. It has been determined that the MOP signed contracts with the University of Chile and a private company with the purpose of topping up salaries of high level professionals, whom otherwise would be difficult to retain in public service. Several high officials of the ministry were indicted. The scandal had a great impact in professional circles because of the relatively high ethical and professional standards observed so far at MOP and its contractors. The Government has acknowledged the facts, but maintains that its intention was not to defraud the taxpayers. As expected, these events caused a great deal of political controversy and questions about how the Ministry was managed. On the other hand it was also apparent that the Chileans

were proud of the great achievements of the Ministry and were not willing or prepared to undermine its effectiveness. So far, the scandal does not appear to have deterred foreign investors. Nevertheless, it is expected that in addition to punishing the culprits, the operation of the Ministry would be subject to scrutiny.

## **E. PERFORMANCE OF PROCUREMENT BANK PROJECTS**

### **OVERVIEW**

111. The Bank's portfolio in Chile is small and selective (paragraph 6). While in the past the emphasis was on infrastructure, particularly in highways and ports, more recently the focus has been on supporting poverty reduction, structural reforms and state modernization. Therefore, procurement under Bank projects largely consists of relatively minor civil works, and small goods and particularly consulting services contracts, this approach is expected to remain unchanged. Given the strength of Chile's public sector, the Bank has relied considerably on the use of local procedures and documentation. However, it is apparent that the lack of national standards and some institutional weaknesses have also led to a multiplicity of procedures specific to each project implementing agency, and not always consistent with best practices. That suggests that, attention should continue to be given to the harmonization of procedures and the use of standard documents consistent with Bank Guidelines and the country's modernization objectives.

112. As shown in Annex A, local procurement legislation and procedures in Chile are generally consistent with Bank policies. Moreover, the Procurement Law and the Public Works bill exempt Bank financed contracts from their jurisdiction. Implementing agencies generally adhere to Bank policies, and use of standard bidding documents (SBD) for international competitive bidding (ICB), as well as modified version thereof for national competitive bidding (NCB). Two ICRs, two agency capacity assessments and two mid-term reviews which were completed between the second half of FY01 and FY03, as well as recent procurement post reviews and supervision reports did not find major problems. There have been; however, shortcomings in the application and interpretation of the Guidelines, which have given rise to back and forth consultation and delay. Also, there have been some instances of abuse, which in two cases led to misprocurement. Those reports have also identified deficiencies in procurement planning, monitoring and filing. The weakness are due in part to lack of staff experience and training on Bank policies and procedures, which are often linked to the quality of Bank support and supervision. They are also linked to the overall institutional shortcomings on procurement noted elsewhere in this report.

113. Given the lack of national standards, deviations from Bank Guidelines are agency specific; therefore, it cannot be said that they occur across all projects. The implementation of common procedures and documentation under the PPSSP gives the opportunity to overcome those shortcomings. The goal should be that local procurement procedures are fully acceptable under Bank projects, with few or no exceptions, particularly for NCB. In doing so, attention should be given to ending the following practices: (i) submission of information and bid securities in advance of the deadline for

bid submission; (iii) rejection of bids at the opening ceremony; (iii) contract award on the basis of bracketing procedures; and (iv) compensatory pricing, or adjustment of bid unit prices on the basis of the official price estimate, in works contracts (Paragraph 80). An aspect that deserves special consideration is the selection of consultants on the basis of open bidding and price, which is inconsistent with the Bank Guidelines; likewise there is a tendency among some agencies to sole source consulting services contracts particularly with universities, which may run counter to both Chilean legislation and the Guidelines and should be avoided (Paragraph 26 and 90).

114. A fact that deserves attention is that, the Government still establishes project implementation units (PIUs) for management of Bank projects, and in some instances also hires international institutions such as the UNDP to manage Bank projects. The PIUs in turn include small procurement teams (usually one or two specialists) responsible for procurement, sometimes operating independently from agency procurement offices. This practice does not speak well of Chile's public sector strength and should be reconsidered. Moreover, special implementation arrangements should not be used as an excuse to circumvent sound national regulation and practices under the pretense that Bank projects are exempt from them.

#### **PROCUREMENT THRESHOLDS AND BANK REVIEW**

115. The current thresholds in Chile for ICB procurement of works and goods are \$ 5.0 M and \$ 350,000 respectively; the thresholds for NCB are respectively fixed at \$ 350,000 and \$ 100,00, which are well above what the Procurement Law (\$ 46,000) allows. Given the composition of the current portfolio, the value of works contracts generally falls below the ICB threshold; goods contracts, on the other hand, are generally above the threshold, but in most cases bids are submitted by local companies only. Shortlists of consultants consisting of local firms only are allowed for contracts costing up to \$ 500,000; most consulting services contracts are awarded to local firms.

116. On the basis of previous experience, the strength of the private sector, the openness of procurement legislation, and the expected mix and size of contracts in the portfolio (Paragraph 111) it is recommended to raise the thresholds for ICB of civil works and goods to \$ 10.0 M, and \$ 1.0 M respectively, and for short lists made exclusively of national consultants to \$ 1.0 M. Also, as the national legislation makes NCB the default procurement method, for consistency, the NCB thresholds should be fixed at the same levels of 1000 UTM or about \$ 46,000 as in the legislation. It is also recommended to set the prior review thresholds for civil works and goods contracts at \$ 1.0 M and for Consulting services at \$ 500,000. Higher thresholds should be supplemented with the development of standard documents and realistic and timely procurement planning.

#### **USE OF CHILECOMPRA FOR PROCUREMENT UNDER BANK FINANCED PROJECTS**

117. This subject should be considered under the premise that Chilecompra is primarily a technology tool that in itself does not set the procurement rules and procedures, but provides the functionalities to carry them out. Thus it should be expected that Chilecompra does not preclude the application of Bank procurement policy or of bidding documents. Therefore, on the basis of the review of the technical platform it can be concluded that Chilecompra presents an excellent opportunity to carry out e-

procurement under Bank projects in Chile. Every indication exists that Chilecompra will provide state-of-the-art electronic procurement capabilities entirely compatible with Bank procurement guidelines, subject to verification once the new electronic platform is fully operational. In particular, the procedure for registration of foreign bidders (see paragraph. 50), and the actual implementation of security, integrity, non-repudiation and confidentiality features for one and two-envelope tender transactions (see paragraph. 49) would be aspects to revisit at a later time. Moreover, Chilecompra's functionalities offer more competitive procedures for shopping than the minimum required in the Bank Guidelines.

118. It is therefore proposed that the following practices are fully acceptable procedures for procurement under Bank financed projects:

- Advertising of General Procurement Notices, NCB Invitations to Bid and Requests for Expression of Interest for consideration for shortlist national firms in Chilecompra as a substitutes for advertising in newspapers of national circulation in Chile;
- On-line shopping through Chilecompra and DCCP's catalogues of goods and services.

## **F. RISK ASSESSMENT**

119. The overall procurement risk in Chile is low, provided that the individual risks are properly managed. There is no concern about the integrity of public officials and the stated government policy and practice of enhancing transparency and 100% advertisement of public procurement actions. Civil society and the private sector trust the oversight intervention of the CGR at critical stages in the process. Civil society itself keeps a close watch and constructive dialogue with state agencies. However, until the principles in the Procurement Law are developed and operational, a number of potential risks still remain, particularly to bidders and contractors, and they should be addressed. Those risks have been highlighted in this report and coincide with the findings of a survey carried out by Transparency International in 2002 <sup>7</sup>. They are: (i) multiplicity and inconsistency of regulation and lack of clear directives on PPSSP, planning, bid evaluation, etc, all of which creates uncertainty (ii) contractor registration and qualification procedures that restrict participation and limit competitiveness of the construction industry; (iii) relatively low esteem for the procurement function as reflected in low salaries, which have resulted in inadequate staffing and capacity; (iv) strong state authority to interpret and manage contracts and lack of resolution of disputes mechanisms therein.

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<sup>7</sup> Mapa de Riesgo sobre licitaciones publicas en Chile, Transparencia Internacional, Enero 2002

## G. PRIVATE SECTOR

### PROCUREMENT PRACTICES

120. The present legal and business climate is of a free enterprise society operating within a generally broad environment of state intervention in the economic sphere. The private sector tends to rely on two approaches when sourcing contractors. Appointments are usually on the basis of a long-term relationship, or through shopping depending on the characteristics of the project. Projects normally proceed on a design and build basis and the works are of good quality and to an agreed lump sum price. Contracting by the private sector is guided by the civil and commercial codes initially written in the nineteenth century.

### THE CONSTRUCTION INDUSTRY

121. The output of the construction industry in 2002 was US\$ 9,180 million representing about 7.9 percent of the country's GDP. Some 60 percent of the construction demand is currently attributed to private sector clients and about half of this is in the housing sector. Most of the public sector demand is for civil engineering projects mainly in the transportation sector. The public sector however, is a less dominant client than it used to be. In 2003, some US\$ 8,100 million would be invested in construction, of which less than 40 percent would come in the public sector, compared with the about 80 percent participation of twenty years ago. Table 3 provides an indication of the relative size of the demand distribution for the year 2002.

Table 3. CONSTRUCTION INVESTMENT BY TYPE OF WORK		
	US \$m	%
Civil works	3,829	42
Housing	2,782	30
Building	1,560	17
Repairs & demolition	1,010	11
Total	9,181	100

122. Most people in the contracting sector work in small firms or as sole traders, particularly in housing, but a limited number of large firms undertake a substantial proportion of the work. There are approximately 4,000 contractors; the large construction firms (several of them foreign) representing 20 percent of the civil works contractors carry out some 60 percent of the workload, while in the housing and building sectors five percent of the firms carry out about 40 percent of the work.



123. The Chilean Chamber of Construction (CChC) is the trade association for the construction industry representing some 2,000 firms (*Box 2*). The chamber plays a vital role by assisting the industry through a well-established network of social services and by establishing itself as a de facto consultative group for the infrastructure and housing sectors. The chamber's role, the strict MOP and MINVU registry systems (Paragraph 71), as well as the booming economy of the 1984-1997 period have to a large extent dictated the development of the industry. During this period there was a regular and relatively high demand for construction because of the increasingly successful private sector and government privatized agencies.

### **Box 2. The Chilean Chamber of Construction (CChC)**

Created in 1951, the CChC is a trade association representing the interest of over 2,000 member firms, ranging from sole practitioners to large multidisciplinary practices. Its members include building and heavy civil works contractors as well as suppliers. The chamber's objectives are to improve the well being of the construction workers and to contribute to the development of the construction sector. The particular circumstances of the construction work, including its temporary labor, induced the chamber to create nonprofit organizations to take care of the workers' needs such as pensions, health, training and insurance. To date, the CChC has some 17 entities worth US\$ 900 million; some of them profit enterprises, which take care of the needs of about seven million people.

The chamber is managed by a president, appointed by a 15-member board and supported by seven working committees on real state, housing, general contracting, public works, subcontracting, manufacturing, and suppliers. In addition, the chamber has advising committees on concessions, economics, ethics, infrastructure, labor, legislation, housing, environment, and urban development. The chamber is well connected in the political circles, and is a the de-facto consultative agency in the infrastructure and housing sectors.

## **PRODUCTIVITY IN THE CONSTRUCTION INDUSTRY**

124. The less favorable current situation in the economic environment means that the construction industry should start to question its performance and practices, and that both the private and the public sectors should look for ways to reduce their costs. In this regard, (Table 4) has been prepared to crudely compare productivity data of several

**Table 4. CONSTRUCTION PRODUCTIVITY**

Country	Chile (2002)	Taiwán (1999)	USA (1993)	UK (1993)	Nicaragua (2002)*
Number of construction workers (thousand)	425.3)	300	7,000	1,400	3.15
% of Work Force	15.7		6.0	6.7	
Construction Output (US\$ m)	9,181	20,000	464,800	67,900	54.3*
Productivity (Thousands \$)	21.6	66.6	66.4	48.5	17.2
* Nicaragua data refers to the Ministry of Public Works					

countries. This rough comparison shows that Chilean workers are only half to one third as productive as construction workers in more industrialized countries. Also, contracting agencies should look for ways to reduce the transaction costs of procurement including the registration cost, the cost of bid preparation, and the cost of contract administration and supervision.

125. Other prevailing views regarding the industry's problems include:

- The reduction of the construction demand in the late 90s;
- The excessive documentation, processes and bureaucracy involved in the bidding and contract implementation stages;
- Incomplete engineering designs and changes of the contracting agency's requirements once the work is underway.

### **CONSULTING SERVICES**

126. Consulting engineering. The Chilean economy is strong in mining, energy, forestry, transportation, water and sanitary services, software development and communication services. The size and sustained growth of these sectors have resulted in extensive and broad local engineering know-how. Furthermore, the open market policy of the country has allowed the establishment of several foreign consulting firms competing or collaborating with local consultants. A rough estimate of the consulting annual billings amounts to about US\$ 300 million; this represents approximately three to five percent of the construction activity which seems to be a low figure compared with the eight to ten percent in more developed countries. Some 40 to 50 percent of the demand for consulting work comes from the public sector, mainly the MOP

127. The market of consulting services is formed by a small number of large multidisciplinary firms that derive their profitability mostly from the private sector and a large number of small firms that work mainly for the public sector. These engineering consulting firms are either private limited companies or sole proprietorships. The directors, partners, and associates of the firms are generally engineers that have worked in the public sector for a number of years and; therefore, are familiar with government practices. Most firms consist of a core of four to six professionals and a pool of individual freelance specialists. These firms find it difficult to grow because of the fierce price competition that they confront serving the government. The Association of Consulting Engineers (AIC) founded in 1968, has over 60 member companies and claims to represent about 75 percent of the consulting engineering capacity of Chile. Furthermore, a total of 210 firms and 540 individual consultants are Registered with the MOP. The MINVU's registry also records 700 entries.

128. There appears to be in Chile, due to budget limitations, less involvement of independent consultants in procurement and contract implementation services than in other countries, as shown by the relatively low percentage of the construction output represented by the consulting services. Therefore, it seems that there is a case for more use of consultants services for feasibility studies designs and construction supervision of works design engineering, that would reduce the high incidence of construction cost overruns due to inadequately undefined works, as well as those related to strategic

supervision of construction to identify areas where improvements in performance can be achieved.

#### **INSURANCE AND GUARANTEES**

129. The insurance industry in Chile is well developed. According to the Chilean Association of Insurers, which was founded in 1899, 19 out of its 23 member companies provide services to the construction industry. The surety market, including bid and performance guarantees represents less than one percent of the general insurance market and five of the insurance companies handle about 90 percent of the business. The industry is regulated by the Ministry of Finance's decree DFL 251 of 1981 through its Superintendence for Insurance. Also, the MOP is considering including the surety in its registry system, which may restrict the supply of surety providers. (paragraph 89)

### **H. CONCLUSIONS AND RECOMMENDATIONS**

130. The overall conclusion of this report is that Chile has adopted a well thought-out and comprehensive strategy and action plan for procurement of goods and services that is a best practice example to be followed. The strength of the strategy is that it openly recognizes existing shortcomings, builds on past experience, and enjoys ownership at the highest levels of government, as well as a committed and competent team responsible for its implementation. Implementation of the plan thus far is on schedule and it is already showing concrete effects on participation of state agencies and suppliers. However, the road ahead is not easy, particularly with respect to strengthening capacity and achieving standardization of procedures at the operational level. On the other hand, there are already well established and generally sound, although not common practices for procurement of civil works. The various sections of this report highlight those strengths. Specific issues and recommendations with respect to implementation of the PPSSP and Procurement and Management of Civil Works Contracts are detailed in Paragraphs 57 and, 115

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**ANNEX A - CHECKLIST COMPARING NATIONAL COMPETITIVE  
BIDDING PROCEDURES AND BANK POLICY**

	Yes	No	Bank Policy
1. Are there eligibility restrictions based on nationality of bidder and/or origin of goods (other than primary boycotts)?		<b>x</b>	Not allowed
2. Are there primary boycotts which are established by law?		<b>x</b>	Only primary boycotts are acceptable
3. Are bidding opportunities advertised in the local press?	<b>x</b>	<b>x</b>	Required <i>Advertising in Chilecompra is compulsory. Advertising in newspapers is optional.</i>
4. Are prospective bidders allowed at least 30 days for bid preparation (except for commodities/small goods contracts)?		<b>x</b>	Required
5. Are contractors/suppliers prequalified for large/specialized contracts?		<b>x</b>	Required
6. Are minimum experience, technical and financial requirements (for pre- or post-qualification) explicitly stated in the documents? Registration should not be used as a substitute for advertisement when open competition is required. However, when advertising for civil works, borrowers could indicate the required minimum category of contractor specified in the registration system.		<b>x</b>	Required  Required
7. Is an invitation to prequalify advertised for each procurement involving large or complex potential contracts?		<b>x</b>	Required
8. Are joint ventures with local firms required for foreign firms' eligibility?	<b>x</b>		Not allowed
9. Are joint venture partners jointly and severally liable?		<b>x</b>	Required
10. Are there set limitations to the number of firms who can bid for a contract?		<b>x</b>	Not allowed
11. Are parastatals allowed to bid?	<b>x</b>		Acceptable only if they (i) are financially autonomous, (ii) operate under commercial law, and (iii) are independent from

			borrower and its purchasing/contracting authority.
12. Are bidders required to register with a local or federal authority as a prior condition for bidding?		<b>X</b>	Should be discouraged. Acceptable only if registration criteria, process and cost reasonable/efficient and qualified foreign firms are not precluded from competing.
13. Are extensions to bid validity allowed?		<b>?</b>	Acceptable only if justified by exceptional circumstances.
14. Are there restrictions on the means of delivery of bids?		<b>X</b>	Not allowed, except when bidders have to submit physical samples. Then they can be required to deliver bids by mail, by courier, by hand, etc.
15. Is preference given to suppliers or contractors based on region or locality of registration, small size, ethnic ownership, etc.?		<b>X</b>	Not allowed
16. Are there restrictions on sources of labor and material?		<b>X</b>	Not allowed, except for unskilled labor, if available locally.
17. Is public bid opening required? Does it occur immediately or closely following the bid submission deadline?	<b>X</b>		Required
18. Is a "two envelope" bid opening procedure permitted for procurement of goods or works? <sup>111</sup>	<b>X</b>		Should be discouraged. Allowed only if (i) domestic law precludes use of one envelope and (ii) provided adequate safeguards against retaining second envelope unopened are incorporated in the two envelope procedures and effective bid protest mechanisms are already in place for the due processing of bid complaints.
19. Is automatic rebidding required if too few bids are received?		<b>X</b>	Acceptable, provided all responsive bidders are allowed to bid, the process is efficient and no serious delays result.
20. Is "bracketing" used in bid evaluations? <sup>121</sup>		<b>X</b>	Not allowed Only if quantified in monetary terms

Are bid evaluation criteria other than price allowed?			monetary terms
21. Is award made to lowest evaluated qualified and responsive bidder?		<b>X</b>	Required Award is to the bidder submitting the most convenient bid, which in practice is the lowest evaluated.
22. Are price negotiations conducted with "winning" bidders prior to contract signature?		<b>X</b>	Not allowed, except where the bid price is substantially above market or budget levels and then only if negotiations are carried out to try to reach a satisfactory contract through reduction in scope and/or reallocation of risk and responsibility which can be reflected in a reduction in Contract Price. (See Guidelines para 2.60)
23. Are price adjustment proviso generally used?	<b>X</b>		Not required, but recommended for works contracts of one year or more in duration when domestic inflation rate is high.
24. Are the terms and conditions used in goods and works procurement generally appropriate for the size and nature of contract intended?	<b>X</b>		Required (to be acceptable they should be balanced, reasonable, and clearly address the most important issues that lead to problems during performance, e.g. risk allocation, payment, inspection, completion/acceptance, insurance, warranties, changes, contract remedies, force majeure, governing law, termination, etc.)
25. Are contract scope/conditions modified during implementation?	<b>X</b>		Acceptable, but the Bank's approval is required for changes in those contracts that were subject to prior review under the Loan Agreement.

<sup>[1]</sup> All technical envelopes are opened first and, after review, price envelopes of all or only qualified/responsive bids are opened in the second round.

<sup>[2]</sup> Rejection of bids outside a range or "bracket" of bid values.







