

Unlocking the Public-Private Partnerships Deadlock in Indonesia

Andri Wibisono, Jeff Delmon and Hongjoo Hahm



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Abstract

The challenges faced by Indonesia in creating a robust public-private partnership (PPP) program are similar to those faced by many other middle-income countries. This paper provides a gap analysis for Indonesia's PPP framework based on lessons learned and good practice from countries with successful PPP programs. It identifies, in particular, the need for the government to:

1. Select good projects for PPP, rather than only complex ones that are less likely to attract private partners.
 - Establish a list of projects by a limited cabinet meeting and stick to it - issuing different lists of projects and holding showcase summits with open agendas tends to confuse the market.
 - Keep those projects on track for PPP - allowing the contracting agencies to develop prospective projects directly, or to award them without competition leads investors to question the commitment and resolve of the government to its own PPP process.
2. Prepare projects well, using the Ministry of Finance to provide access to:
 - A team of PPP experts to help contracting agencies develop projects.
 - Project preparation funding to help pay the high costs of preparation.
 - Viability gap funding to make projects more affordable and bankable by defraying some of the capital costs.

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Chapter 1

Indonesia's PPP Program

After more than four decades of structured, public-sector-oriented development undertaken through a series of five-year development plans, in the early 1990s the government of Indonesia began to invite private sector investors to participate as partners in infrastructure development. By the end of 1997, Indonesia had attracted over US\$20 billion in public-private partnership (PPP) investments in electricity (\$10.2 billion), telecommunications (\$8.4 billion) and transport (\$2.1 billion). But projects were often awarded based on patronage, and government support was provided in an *ad hoc* manner. Some projects encountered difficulties, such as the lengthy tariff renegotiations between the central government and the country's 27 independent power producers following the Asian financial crisis of 1997–98. Since then, PPP has struggled to take root in Indonesia, despite the government's best efforts to promote and develop a PPP framework. This chapter details the key institutions and mechanisms introduced by the government to mobilize PPP in Indonesia since 2000.

1.1 Legal and Regulatory Framework

Indonesia is changing many of its infrastructure laws (see Table 1.1), dismantling public monopolies and opening the infrastructure sector and market to private sector investors. Under the new legal framework, the private sector can invest in the development and operation of financially viable infrastructure projects, without being obliged to enter into joint ventures with state-owned enterprises (SOEs).



Photo by Hardini Puspasari

Table 1.1: Revision of Infrastructure Laws

| Sector | Old Law (State Monopoly) | New Law (Open Market) |
|--------------------------|-----------------------------|--------------------------|
| Telecommunications | Law No. 3/1989 | Law No. 36/1999 |
| Oil and Gas | Law No. 8/1971 | Law No. 22/2001 |
| Roads & Toll Roads | Law No. 13/1980 | Law No. 38/2004 |
| Railways | Law No. 13/1992 | Law No. 23/2007 |
| Sea Transport & Ports | Law No. 21/1992 | Law No. 17/2008 |
| Air Transport & Airports | Law No. 15/1992 | Law No. 1/2009 |
| Land Transport | Law No. 14/1992 | Law No. 22/2009 |
| Electricity | Law No. 15/1985 | Law No. 30/2009 |
| Geothermal | - | Law No. 27/ 2003 |
| Water and Sanitation | Law No. 11/1974 | Law No. 7/2004 |

Source: Dikun (2010)

In 2001, Keppres No. 81/2001 was issued to establish an inter-ministerial coordinating committee to accelerate infrastructure development through greater private-sector involvement. The KKPPI (Committee for the Acceleration of Infrastructure Provision) is designated to promote and champion infrastructure provision by means of PPP. The KKPPI's main functions include coordination of infrastructure policy and planning, with the line ministries, SOEs and local governments (hereinafter the "contracting agencies") responsible for project preparation and implementation.

In 2005, Perpres No. 67/2005 was issued to replace the outdated Perpres No. 7/1998, and establish the principles, policy and modality of private-sector participation in infrastructure development. Perpres 67 was subsequently amended, in 2010, by Perpres No. 13/2010 to provide better clarity and support for the PPP framework as it applies to SOEs and local governments, and to clarify the provision of government support and government guarantees.

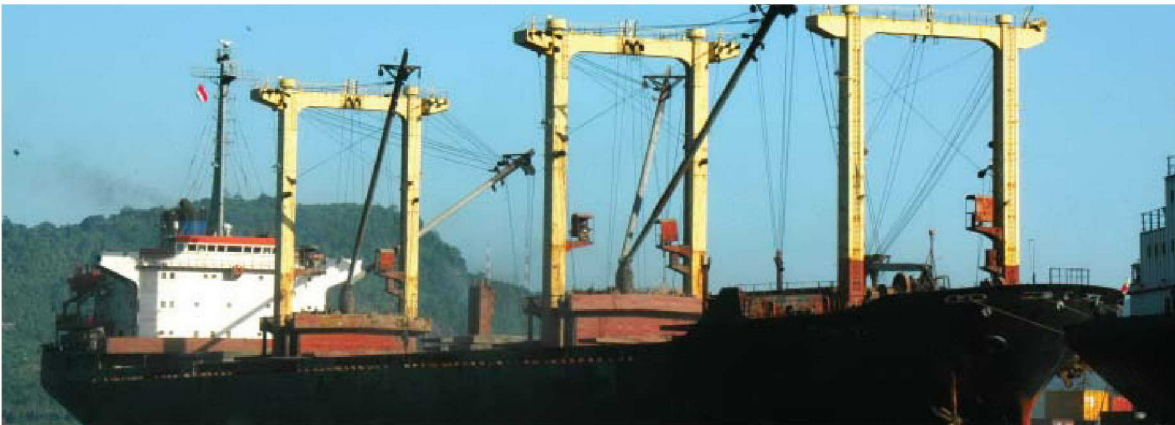


Photo by Hardini Puspasari

Table 1.2: Regulatory Framework that Governs PPP

| Sector | Content | Date Issued |
|--|---|---------------|
| Keppres No. 81/2001 | National Committee on the Acceleration of Infrastructure Development (KKPPI) | June 21, 2001 |
| Perpres No. 36/2005 | Land Acquisition for Infrastructure Development | May 3, 2005 |
| Perpres No. 42/2005 | Renewal of Keppres No. 81/2001 | May 23, 2005 |
| Perpres No. 67/2005 | Public Private Partnership in Infrastructure Provision | Nov 9, 2005 |
| MOF Decree No. 38/PMK.01/2006 | Standard Procedure of Risk Management of Infrastructure Provision by Private Sector. | May 19, 2006 |
| Perpres No. 65/2006 | Renewal of Perpres 36/2005 | June 5, 2006 |
| CMEA Decree No. Per-03/M.Ekon/06/2006 | Procedure and Criteria Concerning of Priority of PPP Infrastructure Projects | June 22, 2006 |
| CMEA Decree No. Per-04/M.Ekon/06/2006 | Procedures for Project Evaluation of PPP Infrastructure Projects Requiring Government Support | June 22, 2006 |
| Perpres No. 36/2005 Amended by Perpres No. 65/2006 | Land Procurement of Development Implementation for Public Interest | June 5, 2006 |
| Perpres No. 91/2007 | Renewal of Perpres No. 86/2006 | Sept 19, 2007 |
| Perpres No. 13/2010 | Renewal of Perpres 67/2005 | Jan 28, 2010 |
| Bappenas Minister Decree No. 4/2010 | Operation Guideline Manual for PPP in Infrastructure | June 21, 2010 |
| Perpres No. 78/2010 | Presidential Decree for Guarantee Application | Dec 21, 2010 |
| MOF Decree No. 260/2010 | Renewal of MOF Decree No. 38 | Dec 31, 2010 |

Source: Dikun, 2010, and other sources

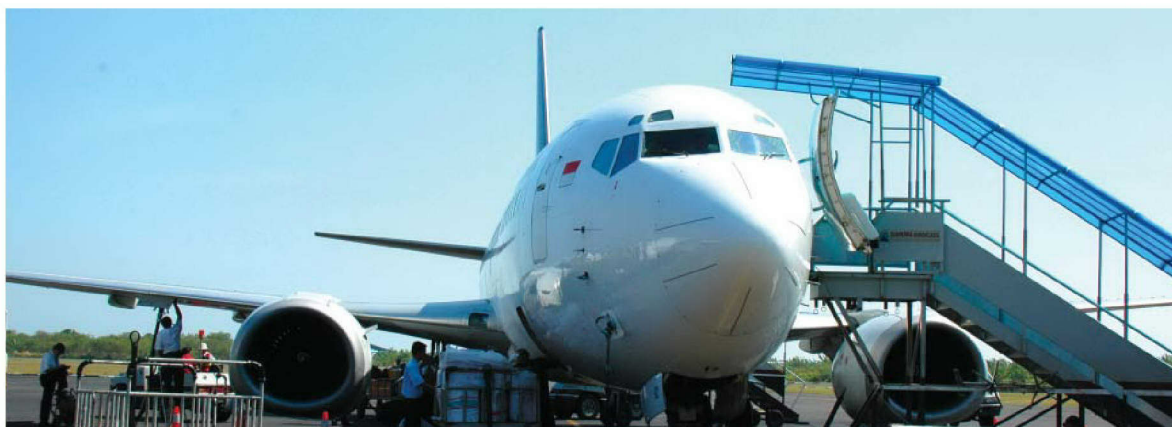


Photo by Hardini Puspasari

The Risk Management Unit (RMU) of the Ministry of Finance (MOF) was formed by Minister of Finance Decree No. 518/KMK.01/2005. The RMU evaluates and determines whether specific infrastructure transactions qualify for public support or any other nonfinancial assistance. In May 2006, the Minister of Finance issued Decree No. 38/PMK.01/2006 on the standard operating procedures for risk management of infrastructure provision by the private sector. With the issuance of Perpres 13/2010, the government issued an amendment of PMK 38 (MOF Decree No. 260/ 2010).



Photo by Hardini Puspasari

1.2 PPP Support Facilities

The government of Indonesia has introduced various funds and financing facilities to support PPP transactions. Principal among these are:

Land Fund. In many countries, the public sector acquires the land needed for large infrastructure PPP projects as part of its contribution to project investment costs. This was the practice in Indonesia during the 1970s. However, in the case of toll roads, land acquisition became a major constraint after 1996, when this responsibility was transferred to the private sector. As a result, many toll road

PPP projects were designed without estimates of the cost of land acquisition and without resettlement/social impact assessments. In addition, the land valuation/assessment was not done in a transparent manner, resulting in extended negotiations, distortions, unequal treatment of project affected peoples, and land speculation.

In response, the government sought to provide financial support for private land acquisition and to clarify laws and regulations on both public and private land acquisition. The government's draft Land Acquisition Law, intended to make the process "faster" and "fairer," is now in parliamentary consultation and is expected to be approved and go into effect in 2011. In the meantime, in 2008 the government established a Land Acquisition Revolving Fund (LARF) in the national budget combined with a cost-capping scheme in which the LARF would pay any land costs that exceed by more than 110% those agreed in the concession agreement. The government also established a Rp 6 trillion Land Fund to finance private companies acquiring land for 2010 (Rp 3.8 trillion) and 2011 (Rp 2.2 trillion).

Project Development Facility. A Project Development Facility (PDF) was created to assist in providing needed funds for examining whether a project is indeed viable (feasibility study) before it is brought to tender. The PDF is funded by the Asian Development Bank (ADB) and managed by BAPPENAS. PDF management has encountered numerous problems, and has been relatively ineffective to date. There are currently discussions on requiring the winning bidder to replace the funds expended by making a payment to the PDF. In doing so, the PDF will become revolving and sustainable.

Guarantee Fund. In December 2009 the government established the *PT. Penjaminan*

Infrastruktur Indonesia (PT. PII Persero), also known as the Indonesia Infrastructure Guarantee Fund, (IIGF), with a seed capital of Rp 1 trillion from the state budget (APBN) based on Government Regulation No. 35/2009. The IIGF will provide a single window for guarantees for PPP projects and is now operational.

PT. SMI. A state-owned enterprise called PT. Sarana Multi Infrastruktur (PT. SMI), a nonbanking financial institution dedicated specifically to infrastructure financing, was established in February 2009 through a government regulation.

Infrastructure Financing Facility. PT. Indonesia Infrastructure Financing Facility (PT. IIF) a privately owned subsidiary of PT. SMI, was established in January 2010. PT. IIF will provide local currency project financing in the form of loans, equity, and nonpolitical risk guarantees. PT. IIF has start-up capital from the International Finance Corporation (IFC), ADB, DEG and the World Bank.

1.3 Indonesia's PPP Program – Status and Summary

Indonesia has invested significant effort in developing PPP institutions and financing facilities, yet still has an overly complex PPP framework that lacks a clear lead agency. The main institutional and financing elements developed include:

- KKPPi to assist with high level coordination of PPP issues.
- RMU to manage government contingent liabilities associated with PPP projects.
- PT. SMI and PT. IIF to mobilize long-term, local currency financing for PPP projects.
- IIGF to support the provision of guarantees for PPP projects.

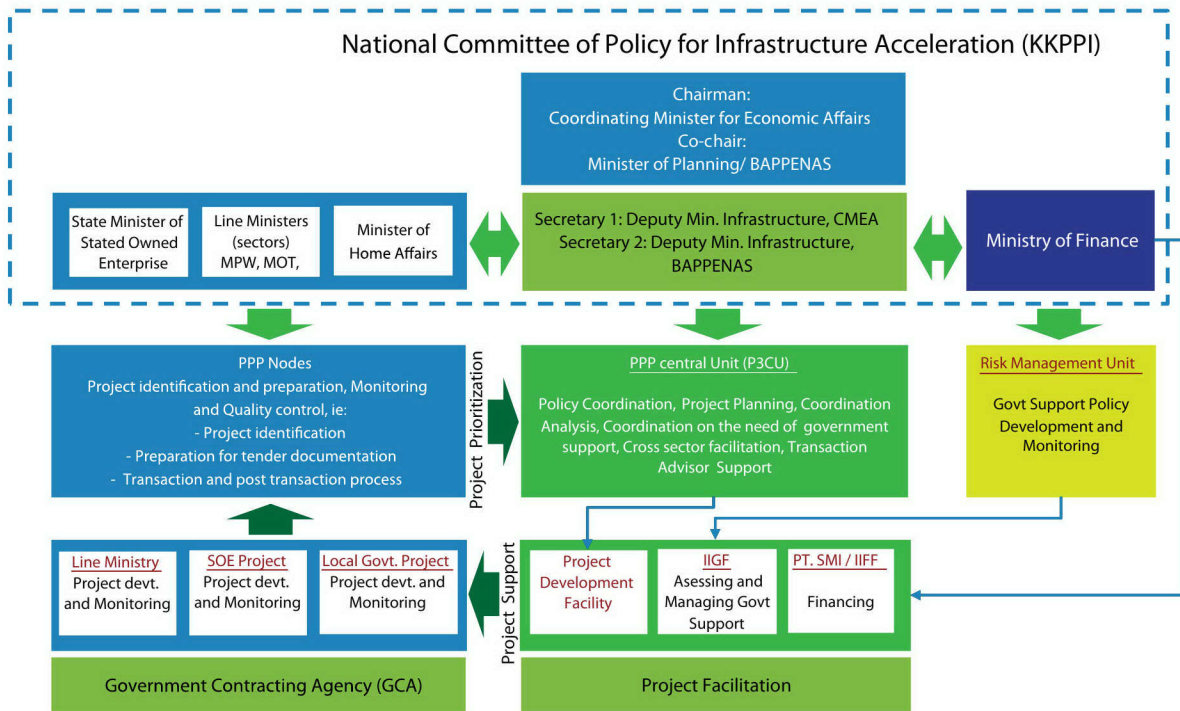
- PDF to fund project preparation.
- Public Private Participation Central Unit (P3CU) to support selection of well-developed PPP projects.
- MOU between the Ministry of Finance, BAPPENAS and the Coordinating Investment Board (BKPM) to define their roles and responsibilities and accelerate the PPP process.

Figure 1.1 shows the PPP institutional structure in Indonesia. This structure was intended to empower the Risk Management Unit at the Ministry of Finance as the single decision making authority to provide public support for any PPP investment. This arrangement has successfully moved Indonesia away from the practice of individual line ministries or agencies issuing government guarantees, and consolidated such guarantees in a single agency that will only provide government support for projects that are in accordance with government PPP laws.

However, while Indonesia has many PPP project proposals, most are not well prepared, and to date no successful PPP project has been developed within the current framework. The line contracting agencies do not place sufficient priority on selecting good PPP projects, nor do they invest the resources needed to develop the available projects on a best practice basis. The RMU has not given any financial assistance to contracting agencies to support a PPP transaction. The government has on many occasions identified lists of “priority” projects, but these are rarely well developed or financially viable. Indonesia lacks a pipeline of financially viable, technically feasible, legally reliable projects to attract strong private investors.

The complexity of this current framework is exemplified in the following diagram.

Figure 1.1: Current Indonesian PPP Institutional Framework



Source: BKPM Presentation



Photo by Hardini Puspasari

Chapter 2

Benchmarking and Lessons Learned

Indonesia's PPP program has struggled compared with those in other countries. Indonesia's difficulties lie in the many subtle but important differences in the areas of project selection and preparation, leadership and effective coordination, integration of fiscal decisions in the PPP process, and the quality and type of transaction advisors being hired.

2.1 Political Leadership

In most countries with successful PPP programs, the program and initial projects were strongly and personally backed by the president or prime minister. For example, in both Colombia and the Philippines, the president chairs the inter-ministerial committee responsible for PPP projects. In the Netherlands, Australia and the United Kingdom, decisions on major PPP projects, as well as the overall PPP program, are made by the cabinet, which is chaired by the prime minister. In India, the Cabinet Committee on Infrastructure (CCI) decides on infrastructure sector projects and

monitors their performance. This 12-member committee is headed by the Indian prime minister.

By contrast, while the president of Indonesia supports PPP and has made high-profile statements about its importance, he does not formally select projects. In a bureaucracy as large and fragmented as Indonesia's, this formal level of executive leadership can be essential to achieving effective coordination.

2.2 Lead PPP Agency

All countries with a strong PPP tradition have a single, powerful agency that coordinates PPP decisions, creating a unified government approach that ensures consistency in policy and project development. In the Netherlands and South Africa, as well as the United Kingdom and Australia, the lead agency is housed within the ministry of finance. This works well in these countries because the finance ministry has significant influence over fiscal expenditure decisions, as well as

a culture of scrutinizing major infrastructure projects carefully. Finance ministries also tend to bring a value-for-money mind-set to decisionmaking and can exert influence over other agencies through their control of the budget. In Colombia, South Korea and the Philippines, PPP policy and decisionmaking is coordinated by the national planning agency. In South Korea, PPP is led by the Ministry of Planning and Budget, which chairs the Private Investment Project Committee. In Colombia, the National Council on Economic and Social Policy (Conpes) is responsible for major decisions involving economic and social development, and the National Planning Department (DNP) acts as its executive arm.



Photo by Hardini Puspasari

In Indonesia, there is no clear lead agency for PPP. The KKPPI is co-chaired by the Coordinating Minister for Economic Affairs and the State Minister for National Development Planning/Chairman of BAPPENAS. The result of this dual chairmanship structure is that coordination at the committee level is more difficult than in the benchmark countries with a similar central planning agency structure. In addition, the dual chairmanship deprives Indonesia's PPP program of institutionalized high-level political support, and blurs control and accountability. The KKPPI's Secretariat comprises staff from CMEA and BAPPENAS, creating unnecessary

duplication and coordination problems. In the benchmark countries, one single agency has the responsibility for promoting PPP. Moreover, governments in the benchmark countries manage to combine the decision on whether to do a PPP with a decision on what fiscal support to provide, since most PPPs need some fiscal support to be viable. The Indonesian approach results in a decision to proceed with a PPP on a theoretical level, but real progress is not possible until the fiscal support decision is made.

2.3 Direct Fiscal Support

In the Netherlands and South Africa, the amount of direct fiscal support to a project can be as much as 100 percent of the cost of the project—usually in the form of an availability payment made over the life of the facility. Such high levels of direct fiscal support are common for education and health facilities and government accommodation PPPs. In India, the Government provides direct fiscal support of up to 40 percent of cost or the amount needed to make them commercially viable (whichever is less), provided the project is justified on a cost-benefit basis. In contrast, many Indonesian government officials believe that PPPs should be largely self-funded, with infrequent and strictly limited use of direct government support. The unintended consequence of this approach is that opportunities to stretch public funds and increase their impact are lost, time is wasted in preparing projects that never proceed because direct fiscal support is unavailable, and projects still continue to obtain hidden subsidies through contingent support anyway.

2.4 Regulation

While many important new regulations are in place in Indonesia, these reforms have not yet

gone far enough in terms of establishing clear and consistent rules, policies and guidelines for PPPs. Of course to put expectations in perspective, it should be recognized that many countries, including PPP leaders such as the United Kingdom and Australia, also made mistakes in connection with their early PPP projects and used the lessons from these experience to improve their subsequent efforts. Such ongoing enhancements are often achieved through issuance or revision of detailed implementing rules and procedures. In Colombia, Conpes (the equivalent of the KKPPPI) has issued more than 100 written policy decisions building on and improving the PPP legal framework as it gains experience implementing PPP projects across multiple infrastructure sectors and with evolving approaches to financing.



Photo by Hardini Puspasari

The PPP framework in Indonesia is not supplemented by such a detailed and helpful body of implementing rules and procedures as used in the benchmark countries. In addition, many of Indonesia's regulations conflict with each other, are ambiguous, or in some way hinder rather than help PPP projects. In particular, there appear to be significant conflicts between the PPP framework established by Perpres No. 67/2005 and Perpres 13/2010, the sector regulations

that represent a higher level of government regulation, and the plethora of other rules. Not surprisingly, when processes are unclear, rules contradictory, responsibilities blurred, and fiscal support limited, implementing agencies are reluctant to propose PPP projects and serious investors are even more reluctant to spend valuable resources on project assessment.

2.5 Project Selection

The inter-ministerial committees that make PPP decisions in other countries are chaired by the president or prime minister. These committees have a value-for-money ethos, viewing PPPs primarily as a way to increase the total value of services to the public, and not as a substitute for public finance. For example, in the Philippines, the National Economic Development Agency (NEDA) runs a process that brings together the Department of Finance and the sector agency, and presents all relevant information to a powerful committee of ministers, who decide simultaneously on whether a project should go ahead, whether it should be a PPP, and what fiscal support it should be given. In contrast, the criteria and priorities on which BAPPENAS selects PPP projects are not always sufficiently clear or formally defined. Furthermore, the selections are made without a concomitant decision by the MOF to provide financial support to the projects. As a leading institution in the selection of PPP projects, BAPPENAS still has an engineering and physical-planning mentality, viewing PPPs primarily as a way to obtain physical infrastructure using private rather than public funds.

In the benchmark countries, before being considered as a PPP candidate, a project must be shown to be both technically and economically feasible. PPP value drivers will be identified and risks allocated efficiently as

part of designing a PPP contract structure, and this work is typically completed before the procurement phase. Contracts will be drafted to international standards. Implementing agencies will be assisted by world-class transaction advisors to prepare the contracts and other bid documentation, market the transaction and run the bid process. In contrast, Indonesia frequently prepares PPP projects before there is anything approaching a feasibility study. Indonesia has not yet implemented an appropriate process for dealing with unsolicited proposals. Risk modeling or risk allocation is still weak and contracts fall well short of international standards for clarity and robustness. For example, compensation on termination is often poorly defined in PPP contracts and fails to consider lenders' exposure sufficiently.

In successful programs, the lead agency is focused on maximizing the value achieved from government expenditures. This mind-set is rooted in the agency's role in economic policy development and project selection (in the case of the planning agencies) or safeguarding and optimizing the use of public resources (in the case of finance ministries). The activities of the British, Dutch and South African ministries of finance illustrate this point. They review

financial models that compare the PPP option with the public-sector comparator to confirm that value for money is being achieved. In the Netherlands, the burden of proof has actually been switched because the PPP option is assumed for projects above a certain size. It is then up to the implementing agency to demonstrate affirmatively why a conventional approach would deliver better value for money than the PPP approach. In Colombia and the Philippines, the planning agency staff are responsible for PPP coordination with a mind-set driven by economics and maximizing value for money for government expenditures. Staff in the PPP unit are qualified in economics and finance, and supported by external advisors with strong transaction and project finance experience.

In Indonesia, project selection is based on political imperatives to fill PPP books, showcase PPP at infrastructure summits, or otherwise demonstrate progress where there is little. BAPPENAS approaches project selection with a planning and engineering, rather than value for money mind-set. Feasibility studies are rare, in particular in relation to commercial and financial viability, subjects less familiar to BAPPENAS staff. The RMU, where such a value-for-money mind-



Photo by Hardini Puspasari

set is more common, does not get involved in project selection, preferring to play a reactive role once projects are submitted to it for allocation of government support. This is a critical shortcoming—without a viable pipeline of feasible projects, other PPP reforms initiated by the government will achieve little.

2.6 Structure for Project Development and Implementation

Flexible, multi-agency, multi-disciplinary teams are the best way to develop and implement PPP projects. Government officials initially lack the specialized skills needed for successful PPP transactions, so they need to bring in experienced advisors if they are to perform their roles effectively. In Colombia and the Philippines, the planning agency

officials work closely with their finance ministry colleagues on multi-agency teams. Both also utilize sector specialists during the project development phase. The Netherlands and South Africa form similar working groups, but seem to rely more on the implementing agencies for the needed sector specialists. The United Kingdom arranges for secondment from commercial banks and law firms of staff with expertise in project finance. South Africa and Egypt initially hired long-term consultants to work in their PPP units to improve access to global best practices. In Indonesia, capacity at the implementing agencies to structure, procure and manage PPP contracts is limited. PPP experts are difficult to hire at government salaries, and when specialist consultants are hired, they are expensive and need to be managed accordingly. There has been limited success in using such consultants to date.

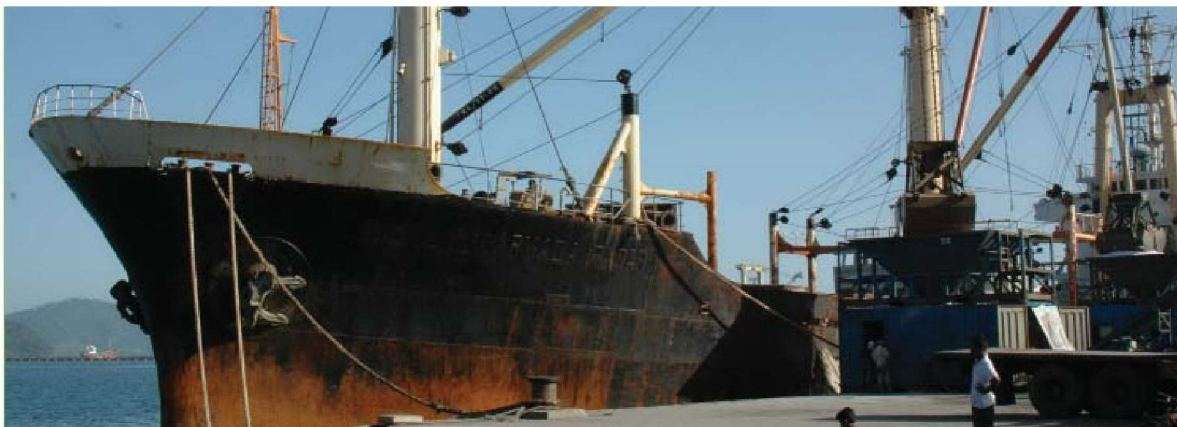


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Chapter 3

Indonesia's PPP – The Way Forward

As a general observation, the Indonesian authorities need to improve their overall understanding of PPP and not view it simply as a budget substitute—free infrastructure funded by the private sector. In this regard, a concerted effort is needed to **build capacity** in government departments and contracting agencies (local government and SOEs alike) to help improve their understanding of PPP and how to implement PPP projects. This capacity building program should be implemented centrally, perhaps under the auspices of BAPPENAS or CMEA. The government (perhaps BKPM) should also develop a **road map** for its PPP framework, to provide clarity and transparency for investors to understand how PPP projects are selected, prepared, procured and implemented in the Indonesian context.

This chapter summarizes the key challenges currently faced in the development of PPP in Indonesia and provides a list of recommendations to address the most critical gaps in the Indonesian PPP framework.

Challenges

Poor Project Selection—too many projects, too few of them viable. Project selection in Indonesia currently tends to focus on “strategic” projects that are less viable and more difficult to implement. BAPPENAS has a “PPP Book” that lists more than 100 PPP projects, only one of which has RMU approval for government support and few of which have been demonstrated to be potentially viable. Other government agencies have different lists of PPP projects. CMEA had at one point identified a list of ten “model” projects. The IIGF has a list of six guarantee “priority” projects, while BKPM has released a list of five “showcase” projects. Local and provincial governments also have their own list of PPP projects. And all of them are different! These multiple lists create confusion among investors. The government—across agencies and ministries—must agree and be able to articulate a priority list of Indonesia’s PPP projects in a single voice.

The selected PPP projects should be priority projects identified by and agreed across government on the basis of their strategic importance as well as their demonstrated financial viability and value for money. These projects need to be developed using global best practices. A pipeline of credible projects is critical to the success of the PPP reforms and institutions established by the government. It is also critical for the reputation of the country. Once such a list is identified and announced, the government PPP project list should not change at whim. In the past, viable and attractive projects have been announced as PPP only to be taken out and implemented directly by the SOE or allocated directly to a concessionaire on a business-to-business or government-to-government basis. This damages Indonesia's reputation and creates a perception of disorganization and lack of discipline. There must be greater accountability for project selection, viability, and implementation.



Photo by Hardini Puspasari

Poor Project Preparation—too fast and then too slow. Contracting agencies need assistance from experts experienced in PPP to structure projects in a manner that will attract investors, understand best practice, and share know-how for other projects. To date, there

has been no project preparation support within government. The one exception has been the Central Java IPP project, which was prepared by PLN with involvement by the IFC, using international good practices and as a result successfully attracting global bidders. BAPPENAS, P3CU, CMEA, the RMU and government entities have not provided any support to contracting agencies in developing a best practice PPP. A center of expertise on PPP (transaction support unit, or TSU) needs to be developed to support line ministries, SOEs, and local governments in their PPP efforts. In addition, during project preparation, the RMU-IGF is not sufficiently involved at an early stage with the contracting agencies in developing PPP projects. The MOF through the RMU plays a reactive rather than proactive role, waiting for projects to be developed and submitted for consideration. This is far too late in the process. In addition there is still a lack of clarity regarding the specific roles of the IIGF and the RMU and the requirements for accessing government financial support.

Recommendations

Recommendation 1: Select only the most strategic and viable PPP projects, and support them across government with a unified voice. This can be achieved through the following steps:

- **Establish a PPP selection process.** BAPPENAS should work with the contracting agencies (line ministries, SOEs, local governments) to identify potential PPP projects and to do a preliminary review of those projects with the support of MOF/RMU, CMEA and BKPM. Criteria need to be established to ensure that these projects are viable, with the kind of characteristics that will facilitate implementation as PPP. This due diligence

process must be properly funded and staffed, with experts intimately familiar with PPP investment (not just theory) and able to propose projects not currently contemplated in BAPPENAS' PPP Book. The shortlist of proposed PPP projects should then be submitted for final selection to a limited cabinet meeting of the MOF, BAPPENAS, CMEA and BKPM, chaired directly by the president (rather than being selected by the KKPPI, which is not functioning effectively for purposes of coordinating PPP). This meeting should select a few projects that will be undertaken through PPP on the basis that they are implementable, viable, represent "value for money," and are likely to receive government support (direct and/or contingent). The shortlist could include short, medium, and long-term PPP projects to ensure the creation of a sustainable PPP pipeline. Priority PPP projects could include a well-prepared geothermal IPP or mini-hydro IPP to promote green energy, the Bali cruise terminal, the Lampung PDAM investment, the Jatilahur water transmission project, and the Medan toll road, all of which could be implemented in the short- to medium-term. For the long-term, consideration could be given to developing projects requiring more preparation, such as the Trans-Java Expressway, the Soekarno-Hatta Airport Railway, Umbulan Water Supply, and a new deepwater port for West Java. The decision to provide government support must be a fundamental part of the initial project selection process. The Figure 3.1 illustrates the proposed project selection process.

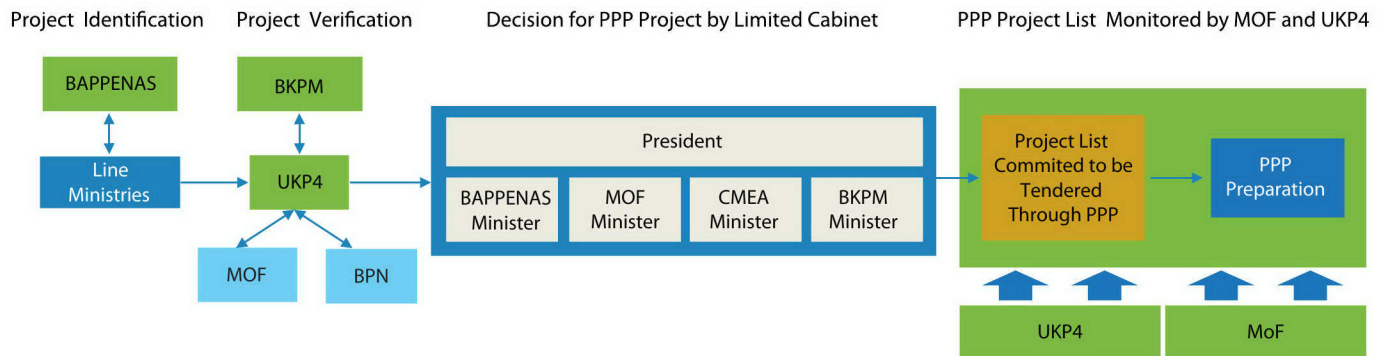
- **Mandate the Vice President's Office (UKP4) to monitor project preparation and implementation** to ensure they are undertaken in a timely manner.

- **Stop contracting agencies from implementing the chosen PPP projects by any means other than through PPP.** There has been a tendency for the government to announce that a project is to be undertaken through PPP, only for the contracting agency to then pursue other methods of financing, often B-to-B or G-to-G. Such leakages from the formal program should be penalized and the contracting agency should be held responsible for all costs incurred in PPP project preparation in such cases.
- **Stop issuing PPP project lists other than those announced by the limited cabinet meeting, and avoid announcing new and different PPP projects** until there is real progress on any already announced PPP projects and until viable projects are ready for market. There is a risk that holding additional Infrastructure Summits or similar events in the absence of these prior actions may actually lower Indonesia's credibility with prospective PPP investors.



Photo by Hardini Puspasari

Figure 3.1: Proposed Project Selection Process



Recommendation 2: Prepare better PPP projects involving MOF and its affiliate agencies early and throughout the process. This can be achieved by adopting the following:

- Establish a Project Task Team to develop each individual PPP project**, led by the contracting agency and made up of specialists from different government bodies. Currently, the contracting agency has only limited interaction with key government counterparts (MOF/RMU, BAPPENAS/P3CU, the National Land agency/ BPN). The Project Task Team needs
- to be a proactive, mutually supportive team that is chaired by the contracting agency and reports on progress regularly to the Vice President’s Office (UKP4).
- Create a team of PPP experts** to help the contracting agencies and the Project Task Team to develop the PPP projects according to international best practice. The PPP Expert Team, comprised by and large of investment bankers and lawyers, could be hired by an SOE such as SMI, given its ability to carry out procurement more quickly than government agencies



Photo by Hardini Puspasari

and to pay market salaries. The cost of the PPP Expert Team would need to be shared by the contracting agency, possibly through the revolving project preparation funding discussed below.

- MOF should provide financial incentives to the contracting agencies to pursue PPP to ensure that their interests are aligned with the government's PPP policy. In particular, **project preparation funding and viability gap funding** should be provided, possibly by creating a revolving fund that would charge success fees to winning bidders or fine contracting agencies that fail to fulfill their PPP obligations. These mechanisms could also be used to pool donor funds and support, thereby avoiding fragmentation of the
- **Resolve land issues before commencing project procurement.** Land acquisition in Indonesia is extremely difficult and poses serious challenges to private investors. PPP land acquisition should be supported by government, in particular through PIP, in close coordination with BPN. **It is always better to resolve land acquisition** issues as early as possible, since land acquisition in Indonesia can take many many years.



Photo by Hardini Puspasari

The diagram below illustrates the proposed preparation structure.

Figure 3.2: Proposed Project Preparation Process

