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PUBLIC GOVERNANCE AND TERRITORIAL DEVELOPMENT DIRECTORATE
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Towards OECD Priniciples on the Governance of Public Investments

25th Session of the Territorial Development Policy Committee

15 June and 16 June a.m. 2011
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2 rue André Pascal, 75016 Paris

This document is submitted to delegates for DISCUSSION and APPROVAL.

For further information please contact Dorothee.Allain-Dupre@oecd.org, Tel: +33 1 45 24 82 43.

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25TH TDPC MEETING: STOCKTAKING AND IMPACT OF THE WORK OF TDPC

Proposal to be discussed:

Build OECD/TDPC Principles

for the Governance of Public Investment

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I. Background: Why make the case for an OECD/TDPC instrument related to public investment?

What is the background?

- Guidelines for the governance of public investment have been developed in the Report and forthcoming publication *Making the most of public investment in a tight fiscal environment* (GOV/TDPC(2011)2). They are also reported in the *Regional Outlook*. These guidelines have been elaborated on the basis of the eight country studies included in the project (Australia, Canada, France, Germany, Korea, Spain, Sweden, United States). They also build upon previous TDPC work, in particular *Regions Matter* and *How Regions Grow* – as well as thematic work on multi-level governance (*Performance Indicators* and *Contracts*) and *Territorial Reviews*.

➔ ***Proposal:*** **These preliminary guidelines could be further elaborated and validated by different audiences to form TDPC Principles on the governance of public investment; which could be adopted by the Council as an OECD Recommendation in 2012.**

What are OECD instruments?

- Formal OECD instruments come in two forms. The first are *Decisions*, which are legally binding. The other are *Recommendations*, which are not legally binding, but practice accords them great moral force as representing the political will of Member countries. Recommendations are adopted by the Council of the OECD. Member countries are then expected to do their best to fully implement the Recommendations.

- OECD Recommendations are key tools for policy evaluation and comparisons. OECD Committees rely on these Recommendations – which usually contain a detailed list of *Principles* – to monitor progress achieved and remaining challenges.

- The Council adopts around 5-10 Recommendations per year. These are the result of the substantive work carried out in the Organisation's Committees. They are based on in-depth analysis and reporting undertaken within the Secretariat and cover a wide range of topics from Anti-Corruption to Tax[1].

- Concerning GOV, the Council adopted: a *Recommendation on Principles for Transparency and Integrity in Lobbying* in 2010; a *Recommendation on Enhancing Integrity in Public Procurement* in 2008 and a *Recommendation on Principles for Regulatory Quality and Performance* in 2005. Two new Recommendations are currently being elaborated and will be discussed during the June TDPC: (i) A revised *Recommendation on Principles on Regulatory Policy*; (ii) *Draft Principles for the Use of Public-Private Partnerships*.

- Despite its important work and achievements so far, the TDPC has not yet developed any specific OECD instruments (such as recommendations adopted by the OECD Council).

What would be the value added of a formal instrument for the TDPC?

- It is proposed to produce a Recommendation with detailed Principles that would cover guidelines for the *design and implementation of public investment across levels of government*. This Recommendation would apply primarily to ministries, agencies, sub-national governments, private actors and banks connected to the public investment process.

[1] Other legal instruments are also developed within the framework of the Organisation such as Declarations, Arrangements and Understandings and International Agreements.

- OECD/TDPC principles for the governance of public investment could contribute to:

  → *Provide international instruments commonly agreed among OECD members* in order to help policy makers to better 'govern' public investment across levels of government, which is a critical dimension of stronger, fairer and cleaner economies;

  → *Raise the profile of the TDPC* and further move to enhanced policy evaluation and monitoring in TDPC work, through commonly agreed instruments;

  → *Respond to the in-depth evaluation recommendations for the TDPC*, about the need to raise the impact of the committee's work.

  → *Enlarge the audience of TDPC outputs*, to reach other actors in the national government (such as Ministries of Economy and Finance), and private actors (banks, infrastructure operators or suppliers);

  → *Facilitate the co-ordination with other GOV and OECD committees*, through the use of shared instruments (for example on PPPs, on integrity, on regulation, etc.)

What would be the next steps to design OECD/TDPC Principles?

- OECD Principles need to be *general and flexible* enough to address global challenges in policy-making and help diffuse good practices in different societal, institutional and market conditions; but at the same time be *sufficiently targeted to complement existing international legal instruments and to allow monitoring* as a follow-up.

- Following initial discussion during the June TDPC, the Secretariat can revise the *draft Principles* to include inputs from the discussion as well as comments received via the TDPC web platform. A revised version with more detailed Principles and explanatory text could then be discussed during the *December TDPC meeting*. Once formally approved by the Committee, the document would then need to be circulated and endorsed by wider audiences.

- The Secretariat would conduct open consultations with other Committees, local and regional actors, private actors (including investment banks and infrastructure suppliers), and civil society representatives. Consultations with Non-Member partners can also be considered. The goal will be to ensure that all interested countries have an opportunity to engage in such work, with particular reference to Enhanced Engagement Countries.

- Once draft principles have been commonly agreed, they will be submitted to the Council for approval. The entire process would last between 12 and 18 months.

- The final document submitted to the Council could include formal principles, to be validated by the OECD Council, and explanations, which can be revised over time without modifying the formal Recommendation.

II. Preliminary list of guidelines on the governance of public investment

These preliminary guidelines constitute a starting point for future Principles. The final format of Principles will include policy recommendations, with detailed text explaining the rationale for each point, as well as illustrative points and background information in boxes and annexes.

An important point concerns the interdependencies across these broad governance principles. In other words, the isolated effect of each of these principles may be significantly reduced compared with a whole-of-government perspective.

Ten preliminary Principles for the Governance of Public Investments

1. Combine investments in physical infrastructure with the provision of soft infrastructure, such as skills and other innovation-related assets, to maximise impact in terms of long-term productivity growth. Infrastructure policy needs to be closely integrated with other sectoral policies such as human capital and innovation as part of a coherent development strategy. Investment funds are likely to work best as part of a multifaceted policy package that makes use of other policy instruments.

2. Exploit the value added of *place-based* investment policies. Investment should be prioritised to address the specific potential and impediments to growth in each region. In addition to national ministries/agencies, regional and local actors have a critical role to play to identify policy complementarities and trade-offs in investment priorities. Clarify the social or growth objectives of investment projects and for the latter, favour selection of projects through competitive procedures. Such calls for tenders should allow local actors to reveal their specific knowledge and development potential. This is particularly needed in times of tight budget constraints.

3. Improve co-ordination mechanisms for the design and implementation of investment strategies across levels of government. The management of the crisis has shown that co-ordination is critical for designing well-informed investment strategies, better targeting them and ensuring policy and fiscal coherence across levels of government. Since the relationship among levels of government is characterised by mutual dependence, countries need to develop co-ordination arrangements to reduce potential gaps or contradictions between policy objectives, fiscal arrangements and regulations across levels of government, which can undermine national strategies for growth. This may imply setting up mechanisms to enhance dialogue across levels of government or specific instruments such as contractual arrangements. Co-ordination takes time, involves a learning curve and has different types of costs (transaction, opportunity, monitoring costs), but when properly designed and implemented, long-term benefits of co-ordination should outweigh its costs.

4. Enhance horizontal co-ordination across local jurisdictions (in particular municipalities) to achieve greater critical mass at functional level and increase economies of scale in investment projects. Fragmented or poorly integrated investment may fail to capture the full benefits. This would avoid the proliferation of small-scale projects with low economic returns.

5. Build transparent management process to improve the selection and implementation of investment projects at all levels of government. Prevent waste and corruption in investment projects from the selection process throughout the tendering until the contract management and payment. Maximize transparency at all stages of the procurement cycle, and establish clear accountability and control mechanisms. Given the complexity of investment decisions and their governance, oversight institutional mechanisms need to be well developed not only for the audit function but also for the relevance of investment choices. Accountability processes should encompass different stakeholder views (citizens, NGOs, technical experts, etc.) regarding the use of funding, without compromising reactivity in the investment decision.

6. Address risks associated to long term investment commitments through robust budget procedures. Because investment tends to involve frequently irreversible projects, it is crucial to ensure that existing stocks are used efficiently before investing in new capacity and further constraining future expenditures. Fiscal space needs to be preserved for key public expenditure programmes for sustainable development. Assessments of the long-term consequences of investment decisions need to be incorporated into budget systems at all levels of government. A multi-year perspective can allow both to look beyond short-term political cycles and to make adjustments over time. Cost-benefit analysis and strategic environmental analysis should be mobilised to help inform and select investment projects. Operational costs of the maintenance of investment over the long-term, which are often under-estimated, should be fully assessed from an early stage in the decision-making process.

7. Diversify sources of financing for infrastructure investment, by making more and better use of user fees and creating mechanisms for securing long-term financing for infrastructure. Carefully assess the benefits of public-private partnerships (PPPs), as compared to traditional procurement. Consider setting up joint investment pools across public agencies/ministries, to help prioritise investment and overcome any tendency by spending agencies/ministries to consider only a limited set of investment options. Care is needed in the financing of such funds, as they risk becoming pro-cyclical.

8. Conduct regular reviews of the regulation with potential impact on public investment decisions and strengthen regulatory coherence across different levels of government. Contradictory regulations across government levels, as well as obsolete and excessive regulations, may impede public investment. Enhance coherence across sectors in regulation targeting cross-cutting outcomes such as green growth, innovation and risk management. Ensure independence of regulators; which helps establish a stable, credible and transparent framework for public investment.

9. Focus on capacity building at all levels of government. Investment projects may fail or engender significant waste or corruption in the absence of adequate or sufficient support services and credible leadership. Robust local public employment systems, with transparent recruitment and remuneration rules, are needed. Developing the ability to manage relations with banks and private actors is crucial for the implementation of public investment. Local capacities to design appropriate investment strategies must be sufficiently developed, in particular regions' capacity to diagnose their competitive advantages and challenges.

10. Bridge information gaps across levels of government. More work is needed in most countries to better track investment at regional and local levels in terms of spending and overall impact. Pursue the efforts made during the crisis to enhance the use of e-government tools for performance monitoring of investment funding and the access of citizens, private firms and government services to shared databases.

For further details on the discussion and rationale of these principles see OECD(2011a), *Making the most of public investment in a tight fiscal environment: multi-level governance lessons from the crisis*.

III. Issues for discussion

- Are these principles adapted for: different national situations (developed as well as developing countries); different territorial contexts (urban, rural); different economic environments (growth and recession)?

- To what extent could these principles be complemented to prompt commitment from a variety of stakeholders (central, regional, local governments, private actors, investment banks, public monopolies, citizens, NGOs, etc.)

Annex 1. List of OECD instruments per Committee

- Public Governance Committee (5 instruments)
- Chemicals Committee (5)
- Committee for Agriculture (8)
- Committee for Information, Computer and Communications Policy (15)
- Committee for Scientific and Technological Policy (10)
- Committee on Consumer Policy (11)
- Committee on Financial Markets (9)
- Committee on Fiscal Affairs (20)
- Committee on Industry, Innovation and Entrepreneurship (1)
- Competition Committee (11)
- Council Working Party on Shipbuilding (1)
- Development Assistance Committee (9)
- Education Policy Committee (3)
- Employment, Labour and Social Affairs Committee (4)
- Environment Policy Committee (70)
- Insurance and Private Pensions Committee (15)
- International Energy Agency Governing Board (1)
- Investment Committee (19)
- Maritime Transport Committee (5)
- Steel Committee (1)
- Steering Committee for Nuclear Energy (8)
- Steering Group on Corporate Governance (2)
- Tourism Committee (3)
- Trade Committee (5)
- Regulatory Policy Committee (1)

- Working Group on Bribery in International Business Transactions (2)
- Working Party on Chemicals, Pesticides and Biotechnology (2)
- Working Party on Export Credits and Credit Guarantees (3)
- Working Party on Private Pensions (2)
- Working Party on SMEs and Entrepreneurship (2)
- Others (1)

Source: http://webnet.oecd.org/oecdacts/Instruments/ListByCommitteeView.aspx

Annex 2. List of OECD instruments adopted in 2010

- C(2010)143/REV1 - Recommendation of the Council on Good Practices for Mitigating and Financing Catastrophic Risks
- C(2010)119 - Recommendation of the Council to Facilitate Co-operation between Tax and Other Law Enforcement Authorities to Combat Serious Crimes
- C(2010)61 - Recommendation of the Council on Information and Communication Technologies and the Environment
- C(2010)41 - Recommendation of the Council on Good Institutional Practices in Promoting Policy Coherence for Development
- C(2010)16 - Recommendation of the Council on Principles for Transparency and Integrity in Lobbying
- C/MIN(2010)3/FINAL - Declaration on Propriety, Integrity and Transparency in the Conduct of International Business and Finance

Source: http://webnet.oecd.org/oecdacts/Instruments/ListByInstrumentDateView.aspx