

Life Cycle Contracts in the Development of Procurement in the Russian Federation: World Experience

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Abstract

The procurement activity in Russia is in a new phase of its development in connection with the entry into force of the 44-Federal Law of 05.04.2013. "On the contract system in the procurement of goods, works and services for state and municipal needs". Sufficiently serious innovations are required the analysis of international and world experience of procurement and development of the scientific and methodological support of state procurement. One of the innovations is contracts lifecycle. The article reveals the author's approach to identify and justify the conditions of effective implementation of the life cycle contracts in the procurement of the Russian Federation.

Keywords: procurement, life cycle contracts, public-private partnerships, scientific and methodological support, professional training

1. Introduction

In Federal Law of the Russian Federation №44-FZ "On the contract system in the procurement of goods, works and services for state and municipal needs" from 05.04.2013, the contract life cycle is considered as a contract to purchase goods or work, follow-up maintenance, operation during the term of service, repair, recycling, and the goods supplied or created as a result of the object (Baronin, 2014; Yankov, 2013). Key words in this definition are life cycle.

2. Method

The definition of life cycle may vary in relation to different objects. Different products may also have different stages of the life cycle. Unlike stages of the life cycle of different objects can involve a variety of approaches to the conclusion LCC, their pricing and execution.

The process of calculation of life cycle cost is one of the most challenging tasks for the customers. In part 3 article 32 of the Federal Law on the contract system the criteria value of the product life cycle or created as a result of the object:

- expenses for the purchase of goods or performance of work,
- the costs of subsequent maintenance,
- operating costs during their lifetime,
- the cost of repairs,
- the costs of disposal of the goods delivered or created as a result of the object.

The order of the Ministry of Economic Development of Russia № 567 dated 02.10.2013 approved "Guidelines on the application of methods for determining the initial (maximum) contract price, concluded with a single supplier (contractor, executor)" examines the approaches to the definition of IMCP. Section VIII "Calculating the cost of the product life cycle, the object created in the result of the work" is a mere formality. Enough general information about what criteria the cost of the product life cycle or created as a result of the facility include the costs for the purchase of goods or performance, subsequent maintenance, operation during the term of their service, repair and disposal of the goods supplied or created as a result operation of the facility, which does not allow the customer to clearly understand the specific steps to substantiate the purchase of a contract lifecycle. At the same time, it is recommended to make the calculation of the cost of the product life cycle or created as a

result of the object using the methods for the determination and justification of the initial maximum price contract. These methods include:

- Comparable uncontrolled price method, based on an analysis of information on market prices of identical goods, works and services, the planned procurement or, in their absence, similar goods, works and services;
- Normative method, based on the social requirements for procured goods, works and services, designed to provide the functions of public bodies, the management of state extra-budgetary funds, municipal authorities in accordance with Art. 19 of the 44-Federal Law;
- Tariff method used in the case in accordance with the legislation of the Russian Federation, the price of goods, works and services for state and municipal needs, subject to state regulation or established by municipal legislation;
- Design and estimate method used for the construction or renovation of capital construction on the basis of project documentation in accordance with the procedures and standards of construction and specialized construction activities, approved by the federal executive branch responsible for public policy and legal regulation in the sphere of construction; carrying out work on the conservation of cultural heritage (monuments of history and culture) of the Russian Federation;
- The cost method is used in case of inability to use other methods, or in addition to them; is to determine both the amount produced IMCP costs and normal for a particular scope of profit.

It is interesting to take into consideration the point of view of A. Margolin that the life cycle contracts allow:

- Effectively counteract the possible dumping of potential low-quality vendors, who overestimate their actual competence;
- To deal with suppliers who seek access to government orders in the hope of evading responsibility in the event of failure or partial performance of the contract (Sergeeva, 2014).

3. Results

Analysis of legal documents, periodicals suggests that the life cycle contracts in procurement practices Russia are possible, provided that:

- Development and adoption of the federal law governing the issues of public-private partnerships;
- Development of scientific and methodological support of application life cycle contracts in procurement;
- Professional development of personnel in the field of procurement, ready to plan and implement contracts lifecycle.

Greater details of these conditions put forward.

As for the public private partnerships, the issue periodically rises sufficiently hard, but, unfortunately, remains unresolved. In most countries, public-private partnership is regarded as the joint implementation of the private partner and the government projects on a risk-sharing between the parties, allowing achieving both economic and social effects. S. A. Sergeeva pointed out that the problem of Russia's life cycle contracts has been rising by the Government of the Russian Federation since 2008, but the lack of legal framework before the 44-Federal Law is not allowed to discuss this issue seriously (Gladilina, 2014).

D. Frimsey and H. R. Lewsi distinguish such signs of public-private partnership based on the contract:

- State transfers to the private partner in the ownership of land or other property for the term of the contract;
- Private partner modifies, remodels or builds an object;
- The state defines the characteristics that should be possessed object;
- Services provided by the private partner, using the object (Koltunov, 2013).

Life cycle contract is a form of public-private partnerships, which are used in foreign countries.

Public-private partnership - one of the most pressing issues of cooperation between government bodies and business - communities. Last years in Russia was presented to the protection of a number of dissertation research on the issue of public-private partnerships in the context of financial and economic instability (Minshina, 2013); on effectiveness evaluation innovation and investment projects on the basis public-private partnership (Berdnikova, 2011), and others. Very idea of interaction between government and business is seen in domestic science for a long time (Amunts, 2005). But the issues of implementation life cycle contracts as a separate line of research is of particular relevance in recent years (Koltunov, 2013; Muratov, 2010, Sokolov, 2011, Yankov,

2013; Dao, 2014). Contract life cycle as a tool for public-private partnerships as presented in scientific articles (Freidin, 2011 by Yankov, 2013 and others.) and in periodicals, on the Internet - sites.

The term “life cycle contract” - is a direct translation of the term “Life Cycle Contract”, which was first used in Finland.

In some countries, such a contract is called the Design - Build - Finance - Maintain (design, build, finance and operation) - the contract the contractor is responsible for both design and construction of the project and financing, and general maintenance and is one of the types of concessions.

This gives the contractor the maximum space for the use of his knowledge and creativity. Payment to the contractor after the construction is done periodically, on the basis of services rendered. If the contract is not fulfilled, come into force penalties. Profit - the goal of the consortium and private donors should ensure that penalties incurred will be kept to a minimum. Company or consortium predetermined conditions assumes responsibility for the entire project (design, construction and financing for 20 or 30 years, the responsibility for maintenance) (Margolin, 2014).

Analysis of the content model “system - exploits – through” (Build, Operate and Transfer) has shown that it provides for limitations on the duration of the concession period of 10 to 30 years. This fact contributes sufficiently serious role of the state, as upon the expiration of the agreement the state may carry out the following steps:

- Leave the right to operate the infrastructure facility to a private company;
- Select another private partner;
- Change management model of the infrastructure (Klëmina, 2014).

PFI (Private Finance Initiative) is a form of public-private partnerships by funding public infrastructure projects with private capital. Initially, this form emerged in the UK. PFI and its variants adopted in many countries as part of a wider neo-liberal program of privatization and financialization, due to an increased need for accountability and effectiveness of public expenditure (Program of the PFI in the UK, 2011).

LCC (life cycle costs) – is the sum of all recurring and non-recurring costs for the entire life or a certain period of service delivery. Includes purchase price, installation costs, operating costs, maintenance and upgrades.

LCCA (life cycle cost analysis) is a tool for determining the most cost-effective option among the various competing alternatives to make the project when one of them is equally appropriate to be carried out for technical reasons. For example, for a highway, except the initial cost of construction, LCCA takes into account all the costs of users, reducing the potential for work areas, as well as the expenses of the agency relating to future operations, including future periodic maintenance and rehabilitation. All costs are usually at a discount and make the value for the current day, known as net present value. This example can be generalized to any type of material, product, or system (Private Finance Initiative, 2011).

Currently, the State Duma is considering a package of amendments adapting legislation to contract life cycle. Also the Federal Law “On Public-Private Partnership and on Amendments to Certain Legislative Acts of the Russian Federation” is now in the process of adoption. This bill should become a system act in PPPs. One advantage of the emergence of this bill is a significant expansion of the contractual forms of public-private partnership, which will be applied in Russia. Given the fact that the list of shapes is assumed to make open conclusion LCC will also be possible, even if the form is not directly fixed bill.

Implementation of LCC in the public sector today is possible to Law N 115-Federal Law “On Concession Agreements”, for example, the construction and operation of toll roads. But the lack of regulatory support LCC and potential competition rules of law 44-FL and 115-FL leads to legal uncertainty which creates additional risks for potential investors and reduces their interest in long-term contracts of this type. Deep enough, this process is considered in the study of problems of the life cycle in modern organizational and management studies (Klëmina etc., 2014).

4. Discussion

Thus, it is necessary to secure the contract life-cycle regulatory setting common features of such contracts and the possibility of their implementation in the various legal forms, whether it be a concession, procurement contracts or other models.

The second condition for the effective implementation of the procurement activities of Russian contract life cycle is development of scientific and methodological support of the use of LCC in procurement. For the

development of scientific and methodological support necessary to examine the application of LCC existing world experience. In the UK in 1981 was obtained by the first experience in projects of public private partnership. Initial projects public private partnerships were seen as a way to attract resources, knowledge and expertise of the private business sector of public services (Bromund, 2009).

In the result of the changes in procedures of PFI in 1997 new criteria for government support for public private partnership projects were created. The use of PFI possible after the analysis carried out using the methods of economic analysis and with the guarantee that the use of PFI for this sector (institutions). Government also estimated profitability of the price, which is determined by the rule of optimum value for money, best matched the goals and criteria meet the needs of the end user. In the future, a full assessment of costs and revenues, including the assessment of the risks will take place. It should be noted that a similar method is used in the evaluation of projects traditional funding budget projects the UK (Theodore, R. Bromund, 2009).

By analogy implemented a number of projects, including the construction of schools in Bridgeport and Dorset, an integrated waste treatment system on the Isle of Wight police building in Ilkeston, nursing homes in Surrey, Northern Ring Birmingham and Croydon railway network, etc. Every year in the UK for about 80-conclude new agreements on private finance initiative and provide about 17% savings for the state budget.

At the present moment the methodological and data base assessment of qualitative and quantitative criteria specific projects by the ratio of the value and cost – Value for money. When deciding whether to use the Public-private partnership, the results achieved with traditional approaches are considered to be critical and compared with estimates of VfM.

Preparation of projects takes a sufficient amount of time, resources, and does not depend on the scale of the project (there are fixed costs in the form of the costs of raising legal, financial and investment advisors, and operations according to the calculations, etc.). Large sums are spent on the negotiation and signing of contracts. Earlier most of the projects it was necessary to attract the fixed assets in the amount of not less than 20 million pounds. Currently the rule was adopted that for the implementation of PFI schemes are necessary the projects worth more than 20 million pounds. However, the development of new schemes in which small projects are combined in order to justify the time and cost.

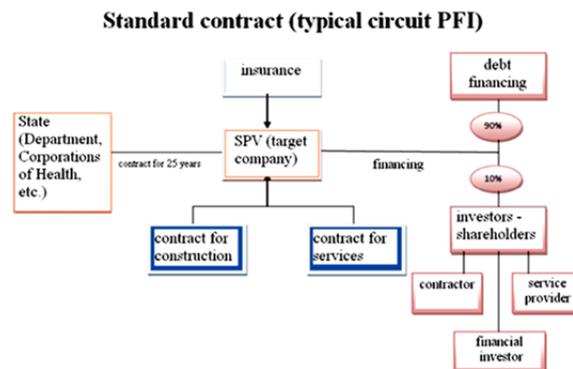


Figure 1. Typical scheme of the PFI in the UK
(based on site [www.pppinrussia.ru/userfiles/upload/files/events/kafedra_2011/11\(3\).pdf](http://www.pppinrussia.ru/userfiles/upload/files/events/kafedra_2011/11(3).pdf))

The main distinguishing features of PFI projects, according to the experts are:

- The need for a large volume of capital investments related to the need for effective management, risk management in construction;
- Relevant experience and resources, which are represented by the private sector;
- Selection of segments that need renovation and for which PFI is an effective way to “restore” with the possibility of redistribution of risk between the private and public sectors;
- Investments in the long term;
- Long-term payback period;
- High probability of cost recovery and cost of the project;
- Modernized technology sector is not sensitive to sudden changes.

Experts identify the following benefits of PFI projects for the UK government:

- The ability to maintain high standards of service provision of services;
- In connection with investor interest in quick start projects, their payback and profitability - increasing the timeliness of commissioned projects;
- Efficient use of public funds;
- The money is returned to the investor gradually and the investor has an interest to ensure that improving the quality of services as it affects their final profit and the need to eliminate defects at its own expense;
- Private investor determines the cost of services, which includes the cost of construction, reconstruction and the cost of maintaining the object in proper condition;
- New approaches to the provision of services and to work (public sector determines which service will be provided, and a private investor determines how it will be implemented, for example use of innovations, etc.)

The projects of public-private partnership in the United Kingdom are based on a contractual procedure. However, the EU Commission did not agree with the interpretation of the directives of the United Kingdom to establish and later projects of public-private partnerships have become competitive dialogue procedure provided.

The initiator of the project is the company of the public sector. There are many areas of PFI: education, police, health, security, roads, courts, prisons. The draft presence of new construction is not necessary; it may be services or IT-service. Project Agreement to be entered into the enterprise with Single (Special) Purpose Vehicle (SPV) established to ensure appropriate infrastructure project, and not involved in any other projects.

Funding for the project may be provided by:

- Treaty between the shareholders (Memorandum) (Shareholders' Agreement) between different companies (joint ventures) on the basis of equal participation.
- On the basis of the Loan Agreement (Credit Agreement) - ordinary loans.

Under the terms of the project agreement, SPV is able to hire other companies to enter into a contract with a major construction company. The main construction company is one of the circles of belonging to the SPV. It also contracts with FM - companies (Facilities Management companies) for long-term management of the facility project (real estate, services, etc.).

The structure of the project may consist of a large number of contracts, and FM - the company can hire a variety of organizations, in particular to address the issue of design and engineering in the construction, as well as the hiring of staff to service government offices. In the event of a possible failure of the project SPV, each participant enters into contracts directly with the public sector enterprises. In practice, in special projects contractual arrangements are more complex.

For the design and implementation of public policy objectives in the planning of infrastructure projects has established a number of institutions, such as:

- "Partnerships UK" - launched as a public-private partnership and "Local Partnerships", which is a joint venture with the Association of local government, supporting public bodies to provide improved services and infrastructure.
- "The Infrastructure Finance Unit", which considers applications for loans for projects PFI, is negotiating the terms of any such loans and provides monitoring and management of loans.
- "Infrastructure UK" created for the development of infrastructure strategy of the United Kingdom.
- Authority for major projects (Major Projects Authority) (MPA) in the framework of the Group's efficiency and reform (ERG) Cabinet Office was established in 2001 and is aimed at the success of the major projects of the central government by working with departments to ensure consistency and quality of major projects during the period of their validity (PFI, 2011).

Thus, the experience of Great Britain has a fairly serious scientific and methodological support.

The third condition is the development of professional training in the field of procurement, ready to plan and implement contracts lifecycle. I. P. Gladilina notes that professional customers - a multidimensional professional - personal quality with a complex structure consisting of functionally interrelated motivational, cognitive, and reflective components of the activity (Federal Law of 05.04.2013 N 44-FL, 2014). Working with contract lifecycle requires customers seriously expand their professional functions, as well as extensions of the corresponding operations of these functions.

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Necessary to note that the professionalism of the customer as a necessary condition a good result of the contract life cycle is considered by the Department of the Moscow City Competition Policy and from the standpoint of methodological support for procurement activities. This approach allows theoretically justifying the existing world experience life cycle contracts and developing management approaches to practical implementation of this experience in the development of procurement activities in Russia.

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