

Contracting in the Global Market Place

Geoffrey SCHMITT, United Kingdom

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SUMMARY

This paper looks at some of the issues facing contractors, consultants and professionals in their decision to expand their activities into the Global Market Place and thus to hopefully assist them to correctly position themselves in that global market both in the present and in the future.

Before entering any of the Global Markets, a basic understanding of that market, the likely sources of the projects and players, understanding who will be making the decisions on procurement, the role of the multilateral organisations such as the World Bank and a detailed knowledge of the various procurement and funding strategies is essential.

Entering the Global Market can be confusing with participants freely referring to FIDIC, EPC, PFI, PPP, BOT, DBFO, etc.

Making a decision to bid can depend on a number of factors including knowledge of the participants, complexity of the project, period between commencement and award, risk factors and language.

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1. THE GLOBAL MARKET PLACE

1.1 Introduction

This paper looks at some of the issues facing contractors, consultants and professionals in their decision to expand their activities into the Global Market Place and thus to hopefully assist them to correctly position themselves in that global market both in the present and in the future. The Global Market Place includes the building, construction, infrastructure and oil and gas industries.

1.2 The Developing World

The end of the 20th century saw booms in various parts of the world, most noticeably in the Middle East during the 1980's and Asia during the 1990's.

However, the dawn of the 21st century sees booms all over the world including China, the Indian Sub-Continent, Russia and Central Asia, the Middle East and Eastern Europe with Africa and South America waiting in the wings.

The combined 2 billion populations of China and India, the oil and gas reserves in Central Asia, the aim of the Middle East countries to develop from oil producers to finance and tourism centres and the enlargement of the European Union are only some of the reasons for this rapid development.

1.3 Factors and Decisions

This paper looks at some of the factors and decisions facing companies when entering and working in the Global Market and these factors and decisions have been summarised under the following general headings:

- Key Drivers on Global Projects
- Main Types of Contract
- Factors Affecting the Decision to Bid
- Establishing a Local Presence

2. KEY DRIVERS ON INTERNATIONAL PROJECTS

2.1 Introduction

Before entering any of the Global Markets, a basic understanding of that market, the likely sources of the projects and players including the main clients, contractors, specialists and designers, understanding who will be making the decisions on procurement, including political influence, the role of the multilateral organisations such as the World Bank and a detailed knowledge of the various procurement and funding strategies is essential.

2.2 Sources of Projects

2.2.1 Multi-Lateral Organisations

The major Multi-Lateral Organisations are supported either by countries in the region or by international agencies such as the World Bank. The international agencies have, in fact, over the past few years moved from mainly funding specific projects to also supporting institutional strengthening. Thus, for example, the agencies will fund the establishment and running of a Ministry of Highways rather than specific highways projects.

Nevertheless, there are still significant opportunities in institutional strengthening, project support and the supply of services and equipment.

However, the one certain observation is that, unless you know about the project and the agency knows about you, there is no opportunity. Most of the agencies announce their projects on their websites and these websites will often instruct companies on the qualification process.

As with many government type projects, unless you have the specific experience, qualification will be difficult and thus bidding together with other companies, either on a JV or association basis, is a good first step.

The World Bank and the IFC, International Finance Corporation, operate on a global basis; agencies with more regional focus include ADB, the Asian Development Bank, AfDB, the African Development Bank, EBRD, the European Bank for Reconstruction and Development and CDC, formerly the Commonwealth Development Corporation but now Capital for Development.

2.2.2 State Owned Enterprises

Many of the oil and gas resources and facilities and some steel facilities are fully or partly owned by state enterprises. Examples include China, Nigeria and the Sudan where although facilities may be operated by privately owned companies, many of the decisions are made at state level. An understanding of the ownership and decision making processes is vital.

2.2.3 International Corporations

Many of the major corporations have had many years experience in the global market, particularly those in the oil and gas prospecting and processing industries such as BP and Shell, the pharmaceutical industries, the motor industry and the power sector.

The oil and gas sector continues to expand in the Middle East, but Central Asia, Russia and Africa are the main growth areas, both to recover new sources and to lessen the dependence on the Middle East.

The power sector has had a quieter period recently but the focus now on renewable and nuclear energy should re-vitalise this sector.

2.2.4 International Contractors and Consultants

The international EPC contractors who carry out major parts of the oil, gas and power construction work include Bechtel, Fluor and Parsons from the USA, Amec from the UK and a number of major contractors from Korea and Japan.

In the infrastructure field, major contractors with a global presence come primarily from Europe, the USA, Korea and Japan.

In addition to the contractors, some of the major consultants operate on a global basis including the USA firms above, all now very strong in all markets. In addition companies including Jacobs and AECOM are increasing their presence by purchasing UK and European companies. In addition to these US firms, consultants from the UK, German, Denmark, the Netherlands and Japan operate worldwide.

2.2.5 Utility Companies

The utility companies are a major source of projects in the power, water and waste sectors and therefore an understanding of the ownership and operation of these facilities is vital for companies entering the global market.

Many of these companies are now owned and operated by non-indigenous companies with French and German companies particularly active in this market.

An understanding of the procurement methods is also essential where for example framework agreements are the chosen method.

2.2.6 Governmental Agencies

In all countries, governmental agencies similar to the NHS, Network Rail and Local Authorities in the UK are a major source of work and countries in the European Union are

required to advertise these projects in the OJEU journal, Official Journal of the European Union. Whether all countries conform to the strict rules is another question.

2.2.7 Private Companies

Finally, but initially with more difficulty, work can be sourced through the private sector.

2.3 Main Players – Roles and Relationships

The Main Players are described above but in summary entry into any Global market will require a local knowledge of:

- End Users
- Clients
- Funding Agencies
- Funders
- Contractors
- Consultants
- Specialist Contractors
- Suppliers

2.4 Strategic Role of Specifiers/Designers

Understanding the role of specifiers and designers in the various projects, and whether they are the decision makers, is fundamental in any entry into the local market.

Many clients, contractors and have developed supply chains and partnering programmes, whether formally or informally, and your inclusion in these is vital.

As a specialist in your field, you can enter these programmes by offering your expertise and track record by the way of innovation, new products, research and development and the provision of resources.

2.5 Various Procurement and Funding Strategies

Many companies try to enter the Global Market without any knowledge of the various procurement and funding strategies used on specific projects. This knowledge is fundamental in understanding your entry point in the market as well as assessing the risks involved. These strategies are described in more detail below but they can be summarised generally under five main headings:

- Traditional
- Design and Build
- Turn Key EPC
- Financed

– Cost Plus (Management/CM/Target Cost)

3. MAIN TYPES OF CONTRACT

3.1 Standard Forms of Contract

Entering the Global Market can be confusing with participants freely referring to FIDIC, EPC, ICE, JCT, PFI, PPP, ECC, BOT, DBFO etc.

You have been invited to an international meeting as an expert in your field, and it does not give the right impression to be asking the meaning of DBFO !! So...

FIDIC - Federation Internationale des Ingenieurs Conseils

EPC – Engineering Procurement Construction

ICE – Institution of Civil Engineers

JCT – Joint Contracts Tribunal

PFI – Private Finance Initiative

PPP – Public Private Partnership

ECC – Engineering and Construction Contract

BOT – Build Operate Transfer

DBFO – Design Build Finance Operate

3.2 Main Types of Contract

As set out above, the five main generic types of contract can be summarised as:

- Traditional
- Design and Build
- Turn Key EPC
- Financed
- Cost Plus (Management/CM/Target Cost)

3.2.1 Traditional

The Traditional approach is the appointment by the client of an Engineer or an Architect to design and administer the contract.

The FIDIC Forms of Contract have developed over the years as the contract of choice for many of the multi-lateral organisations and the Red Book is the FIDIC traditional form of contract. Regular users of the ICE forms of contract, and particularly the earlier editions, will recognise much of the wording in the FIDIC Red Book.

This has now been developed into an additional version referred to as the MDB Harmonised Edition for use on projects funded by the listed Multilateral Development Banks.

Throughout the countries in the world where the United Kingdom has had a presence, the influence of the JCT and ICE forms of building and civil engineering contracts can often be seen.

The Website www.fidic.org gives good advice for choice of contract

3.2.2 Design and Build Contracts

The FIDIC form of contract for Plant and Design Build is the Yellow Book and in the UK the JCT Design and Build has developed as the contract of choice for Design and Build building projects.

In the Design and Build format the Employer and his Consultants decide on a design outline, the extent of the design outline varying from project to project.

The detailed design is carried out by the Contractor and its design team, and the Contractor takes overall responsibility for design. The contract is based on the employer's requirements and the contractor's proposals.

A number of contractual issues arise on design and build contracts which have to be understood to manage the additional risks arising. These include the responsibility for design, professional negligence, fitness for purpose and in some instances novation.

3.2.3 EPC Turnkey Projects

The FIDIC form of contract for EPC/Turnkey Projects is the Silver Book and is mainly used for projects in the power, process, oil and gas and industrial sectors.

An EPC contract, Engineering, Procurement and Construction contract, is a direct agreement between the Employer and EPC Contractor and the Employer is not involved with the detailed design process, except in the event of variations and the Quality Control procedures.

The fundamental difference between Design and Build and EPC contracts, is that in the case of Design and Build, the client normally has an input into the outline design of the building. In the case of EPC the client normally only has a decision in the output e.g. megawatts of power or tonnes of cement and will not be involved in the detailed design process.

3.2.4 Financed Projects

The UK has been in the forefront of these types of projects and the various formats are spreading rapidly worldwide. Financed projects normally entail the formation of Special Purpose Vehicles, SPV, to carry out not only the construction but also the operation and maintenance of the project. Many SPV are therefore a combination of contractors and facility managers

The Private Finance Initiative, PFI, used in the for hospitals, schools and in the Ministry of Defence is a model where all of the finance is provided by the private sector. The client purchases its requirements based on an output requirement e.g. number of bed or school places.

Public Private Partnerships, PPP, are being used for example for light rail and tram projects, were proposed for the stadium project in Ireland and most famously is being used on the London Underground. PPP uses a mixture of public and private money and as can be seen on the London Underground complicated targets can lead to pointing of fingers.

Build Operate and Transfer, BOT, often used for Toll Highways and Bridges entails the private sector providing all of the finance and then receiving receipts, sometimes subsidized, over a period of say 25 years. At the end of the 25 year life of the project the ownership is transferred back to the central or local governmental authority.

Design Build Finance Operate, DBFO, used on the Channel Tunnel but unlike BOT does not transfer back to the authority.

3.2.5 Management Contracts

Construction Management, CM, type contracts have been the norm for many years in the USA, and two of the main proponents in the UK, Bovis and Mace, have made a specialty of this type of contracting.

The Construction Manager effectively acts as the overall manager and specialist contracts are entered into, often directly with the client. The system has been criticised as leaving the CM with an open cheque book and Holyrood House in Scotland is not a very good example. However, experience in the USA does point to Construction Managers and clients building up good working relationships. This results in the CM demonstrating his expertise for future projects.

The CM system in the USA is also influenced by the widespread use of 100% surety bonds whereby the bond holder steps in, in the event of the default of the Construction Manager.

3.2.6 Target Cost/Cost Reimbursable

Target cost and cost reimbursable contracts are widely used in the utilities sector. The client and contractor set a target cost and then share the profit or loss, often referred to as the Pain/Gain formula.

As with Construction Management there would seem to be less incentive for contractors to control the costs but the incentive of steady workloads appears to result in efficient working practices.

4. DECISION TO BID

4.1 Introduction

Making a decision to bid can depend on a number of factors including knowledge of the participants, complexity of the project, period between commencement and award, risk factors and language.

However, you may wish to consider a more precise form of decision making by considering a number of factors and then using a scoring system. I haven't tried to determine the actual scoring, as this will differ so greatly, but have suggested some headings which I am sure you will be able to add to.

The headings can be summarised as:

- Client Relationship
- Third Party Relationships
- Sources of Funding
- Countries of Origin
- Competitors
- Guarantees
- Legal Framework
- Payment Terms
- Local Business Requirements
- Local Customs
- Agents/Representatives
- Design Responsibility
- Risk Profile

4.2 Client Relationship

This can be considered based on previous projects, knowledge of the client and any partnering and framework agreements. These considerations can be made for yourself or associated and JV companies.

4.3 Third Party Relationships

Knowledge and previous experience of working with the various funders on the project whether they be funders, contractors, consultants or specialist contractors

4.4 Sources of Funding

Determination of where the money is being sourced is a further consideration and this can include aid agencies, inter-government, soft loan, governmental, bank or corporation. Certain

types of funding come with strings attached, restricting the nationality of the prospective bidders.

4.5 Countries of Origin

The countries of origin of the possible parties to the project, whether they be the client, partners, funders, contractors, consultants and competitors.

For example, dealing with participants from the USA brings all types of new laws relating to unions, whistle blowing and agents; participants from the Middle East bring the Sharia law; certain countries have a less than favourable record regarding corruption etc.

4.6 Competitors

A review of the likely competitors is essential; bidding against companies from a country providing a soft loan to the project may be a high risk

4.7 Guarantees

Whether the project is attracting export guarantees from, for example, the UK or USA which both have sophisticated export guarantee schemes.

4.8 Legal Framework

This can be a source of confusion with the:

- form of contract;
 - law of the contract, be it Common Law, Civil Code or Sharia;
 - language of the contract; and
 - location for dispute resolution (London, Paris, Hong Kong etc.)
- all being in different countries or languages.

Other legal issues relate to bonds and guarantees, warranties and payment terms.

A true story relating to translation resulted, not in the subcontract, but the subcontractor being executed!!

4.9 Payment Terms

An understanding of the payment terms including letters of credit, various forms of security and advance payment together with an understanding of offset rules is paramount.

4.10 Local Business Requirements

Some countries only allow bidders with established companies and this can often be defined with minimum requirements for example a Branch Office or Representative Office.

Other requirements may include a proportion of local input or a requirement to JV with a local company.

4.11 Local Customs

Other restrictions can include a limit on the use of international suppliers, use of local labour and working hours and holidays.

4.12 Agents/Representatives

A potential minefield where strict laws, in for example the USA, make a detailed knowledge of the requirements, legality and payment of agents and representatives essential.

Recent news on the extradition treaties between the UK and the USA make this doubly important.

4.13 Design Responsibility

Design responsibility is an onerous responsibility when working in the UK; this is multiplied when working in some far off country with different laws and often less rigid controls on construction.

An understanding of the warranties required, law on negligence, corporate responsibility, fitness for purpose, defects liability and latent defects is essential.

4.14 Risk

Finally, the risk.

5. ESTABLISHING A LOCAL PRESENCE

5.1 Introduction

Well, you have been awarded the project, assignment or other contract.

I think at this stage a sample check list of some of the issues to be addressed may be useful:

- Country Rules
- Local Partner – JV/Association
- Office
- Subsidiary
- Branch or Representative office
- Taxation
- Withholding Tax

- Remittance
- Personal Taxation – local/alien
- Visas and Work Permits
- Registrations
- Securities and Exchange
- Internal Revenue
- Social Security
- Embassy/Trade Office

6. BECOMING A GLOBAL PLAYER

6.1 Conclusion

If you haven't been dissuaded by the hurdles described above, some advice on selling yourself to the Global Market.

Emphasise your strengths either in research and development, design and/or innovation and any free advice you can provide to clients and consultants will assist your aim for early entry into the project.

Identify the decision makers and understand the procurement process.

Finally, make contact with the embassy and trade office and develop your knowledge by meeting like minded competitors, preferably on the 19th hole!!

BIOGRAPHICAL NOTES

Professional Registrations: Fellow of the Institution of Civil Engineering Surveyors; Fellow of the Royal Institution of Chartered Surveyors; Fellow of the Chartered Institute of Arbitrators.

Current Position: Independent chartered quantity surveyor, claims and dispute resolution consultant and expert witness.

International experience: Lived and worked in the USA, Hong Kong, Somalia, Kenya and Trinidad and Tobago over a period of 15 years. Additional working experience in China, the Philippines, Thailand, Taiwan, Sudan, Tanzania, Egypt and the UAE.

Practical experience: Geoffrey Schmitt has dealt with all aspects of claim submissions, claim defence and dispute resolution on a range of civil engineering and building projects including hydro-electric dam storage projects, process facilities, pipelines, marine works, expressways, reclamations, water supply, submarine pipelines and a wide range of building projects presenting and defending cases in dispute resolution including arbitration support, preparation of expert witness reports and appearance as an expert witness in both arbitration and litigation.

Examples of major assignments include acting as commercial and contractual adviser to the World Bank presenting their case to a Dispute Resolution Board in respect of a major project in China; appearing as a quantum expert witness in a case in the High Court in London; providing contractual support to a contractor in arbitration in Taiwan and preparing a quantum expert report in respect of an oil pipeline/marine terminal project in East Africa.

Additional information: Furthering his interest in the global market, Geoffrey is the developer of two multi-lingual websites serving the construction industry, go4construction.com, a global supply chain directory, and go4constructionjobs.com

CONTACTS

Mr. Geoffrey Schmitt
The Institution of Civil Engineering Surveyors
1 Uplands Drive
Leatherhead
United Kingdom
Tel. + 44 1372 843222
Fax + 44 1372 844551
Email: g.schmitt@btinternet.com
Web site: <http://www.witnessdirectory.com/schmitt/>