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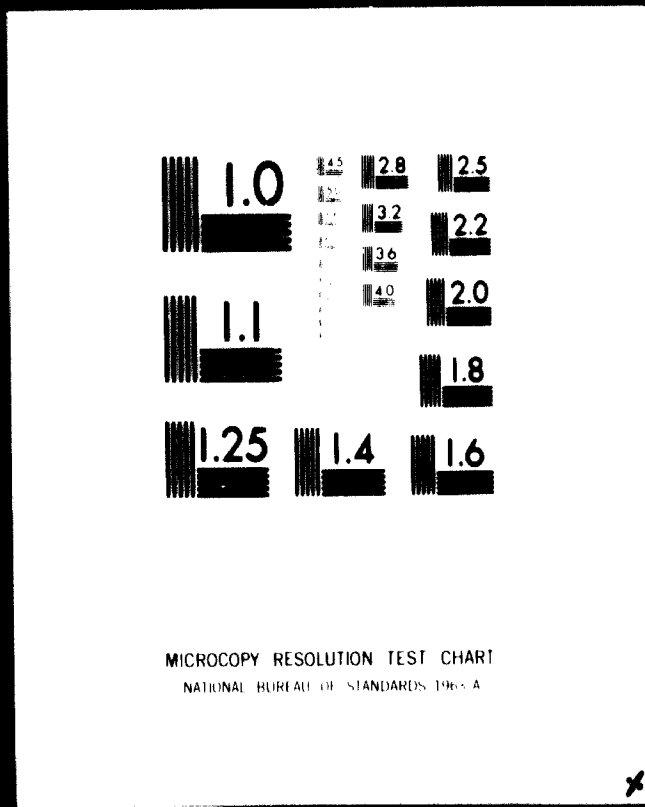
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AGREEMENTS FOR FERTILISER PROJECT
COOPERATIVE PROJECT VIEW

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AGREEMENTS FOR FERTILISER PROJECT COOPERATIVE PROJECT VIEW

1.0 Fertiliser Plant construction is a creative economic process. Large number of activities require formal agreements. Broadly, such agreements cover the following major activities:

- a. Process knowhow and Engineering
- b. Procurement of equipment and machinery
- c. Construction at site

2.0 The contracts/agreements for supply of process knowhow and engineering for the construction of fertiliser plant are basic agreements in the developing countries. In many cases such agreements are between the foreign company and the owner company. The scope of the foreign consultant/contractor includes process knowhow, engineering, procurement (assistance) of equipment, assistance/supervision of construction and commissioning. Such wide scope of work is to obtain 'guarantees' from the contractor for the performance of the plant as well as for the delivery schedule of the project. Selection of the consultant/contractor for this work is vital to the success of the project. It is necessary to properly evaluate the proposals keeping in view the local needs, costs and suitable levels of technology. It would be prudent to ensure that proper organization is built up at early stage of the project for this purpose or outside expertise is obtained. In India, these aspects of work are generally performed by the Owner company without the help of outside expertise. The technical team prepares detailed tender documents, evaluates the proposals, and finally enter into negotiations and formal agreements. In many developing countries, need for an outside consultant for performing these jobs on behalf of the Owner may be necessary. Typical problems encountered during this period are indicated subsequently.

The Contracts/Agreements for the procurement of plant and machinery are more specific and are well defined by the engineering specification. The consultant companies have developed standards/specifications for procurement of plant and equipment and represents their accumulated knowhow. Adherence to the specifications and to established procedures is necessary. Owner companies, by virtue of their previous experience, may specify additional requirements particularly for better material of construction, higher capacity of the machines etc. Technical team of the Owner should, therefore, acquaint themselves of the standards and specifications proposed for use by the consultant and indicate their own additional requirements before the start of the procurement activities. Such additional requirements may also be necessary because of the statutory requirements of the country for boiler regulations, electricity rules, environment standards etc. Much of the misunderstanding could be avoided by detailed discussions on the subject at the beginning of the job. The Consultant, should also, therefore, acquaint himself of such needs and take help from local engineering concerns.

- 3.1 Another important aspect which must be considered during this stage is the measurement system legally used in the country. For example, in USA, FPS system is used as against the metric system followed in many other countries. Particularly, where considerable amount of local materials are available, need for conversion to metric system should be provided for.
- 3.2 The vendor guarantees generally are obtained for the material and workmanship. Such guarantees should be available to the Owner at least during the first 12 months of operation of the plant. Such period cannot be precisely defined and outer limit from the delivery date is also specified. In case of imported machinery items guarantees are extended to periods of 36 months after the delivery or 12 months of operation,

whichever is earlier to cover expected period of transport, erection and delays, if any, during the construction of the project.

- 4.0 The third category of Agreements is for 'Supply & Erection' or 'Supply and Apply' type of sub-contracts. These are for the 'field work. Such sub-contracts require proper organisation at the plant site. These contracts require adherence to the 'statutory' requirements. Generally, such contracts are 'Item-Rate Contracts' and provide for 'variations' in the contracted work. Procedures for measurement certification and payment should be clearly spelt-out in such contracts to avoid difficulties of execution.

It has been found advisable to provide for contingency amounts while obtaining the approvals for the total cost of the work. If delays are encountered, difficulties regarding payments to the contractor could be taken care of by provision of such approval. It is better to select contractors with past proven experience and resources to complete the work in time.

- 5.0 As indicated earlier, the basic agreement for the fertilizer project is the one for the engineering services with the consultant, generally outside the country. These contracts involve payments in 'foreign' exchange and taken considerable negotiating period. Even after the negotiations, the proposed draft documents are reviewed before approval by the Financing Institutions and the concerned Government authorities of the country. These approvals take considerable time if the Agreements deviate from certain established features. There are Governing laws, place of Arbitration, Taxes, use of indigenous materials and services, period of approval from the Government for each case where foreign exchange is involved etc. In this context, this Conference will review the experience of the developing countries. If necessary,

Technical Committee may be formed to develop 'guidelines' for the Agreement which should be acceptable both to the Consultant and to the Owner and recommend these for adoption by the Governments and the Financing Institutions.

6.0 Experiences of contract negotiations are enumerated in brief and may help to arrive at satisfactory contract in short time.

6.1 INVITATION TO BID

In consultation with Financing Institution, prequalified list of vendors was agreed. Invitation to Bid (ITB) was issued alongwith a 'draft of Agreement'. The ITB itself defined the scope of work expected of the contractor in fair detail. The coordination procedure for project execution was also suggested. This specified number of copies of documentation, drawings, letters and telexes, addresses etc. The ITB also gave clear indication of the Owner's preference for the design philosophy of the fertilizer units covered by the Contractor.

6.2 Bid Analysis and Contract Negotiation

The bid analysis was carried out in Two-Step procedure. The technical bids were evaluated as well as the conditions in the unpriced commercial bids were reviewed and analyzed. The contractors' representatives were called only after such technical analysis and review of the unpriced bid. These discussions with four contractors could be completed within 15-20 days because of the preparatory work by the Owner. Evaluation procedure was also developed which reduced time and effort in company bids. After receipt of the clarifications and the adjustment of the price on a stipulated date, the commercial tenders were opened. It was possible to come to a final conclusion almost within next day of opening of

the commercial tenders. In other case, the choice has to be made between the most experienced and lowest offer. Further clarifications were obtained even though the valuation could be completed within a very short time and final decision arrived at. It is, therefore, stressed that it is possible to arrive fast to the final choice, provided adequate care is taken to draft the Invitation to Bid in clear terms, and scientific methods adopted for evaluation. It may be mentioned at this stage that the desire to obtain maximum technical data from the competing firms sometimes lengthens this process of final selection. If the technical staff themselves are well experienced and capable of recognizing the inherent technical advantages of the bid, early appraisal of the bids can be ensured.

The system of weightage factors was applied for making the preliminary technical selection. These factors covered items such as experience, process and engineering, local participation in the engineering, procurement in the country as well as in other countries, project management system, construction supervision, estimated capital cost of the Plant based on the proposed scheme. Such analysis, even though subjective, helped to arrive at a proper analysis of the bids and the relative suitability of the contractor.

6.3 Draft Agreement

As indicated earlier, the proposed draft agreement was attached with the Invitation to Bid. The bidders pointed out the clauses which were not acceptable to them as per the draft. Discussions were held on those points and modified drafts were made during the negotiations. It, therefore, became easy to agree to a final agreement with the selected party(ies) within a very short period. Such agreements would have to follow certain pattern prevalent in the indi-

vidual country. However, there are number of clauses of the Agreement which can be standardised on an international basis. The basic articles like (a) Scope of Work of the Contractor, (b) Obligations of the Owner, (c) Price, (d) Terms of Payment, (e) Changes in work, (f) Payment procedure, (g) Completion time and the Guarantees, (h) Performance Guarantees would vary for each Agreement. However, even here it would be useful to develop 'standard guidelines' particularly for (a) terms of payment, (b) Variations, (c) guarantees both for delivery period and the performance. These are 'operative' Articles in the Agreements. This Conference would well suggest the minimum that must be specified. It would be also possible for us to elaborate the provisions which are insisted by the developing countries but are of little consequence to the performance of the work by the Consultant. The Articles such as (a) Patent Liability, (b) Assignment, (c) Indemnity, (d) Force Majeure, (e) Termination of the Contract, (f) Arbitration, (g) Governing Laws, (h) Misc. Provisions etc. are common. These Articles are useful only in event of dis-agreement between the parties. They are provided to meet the emergency situations. It is, necessary that the interests of both the Owner as well as the Consultant are taken care of. It is suggested that the work already done on this subject should be reviewed and a format developed by UNIDO for guidance and adoption.

6.4 Miscellaneous Problems

Under Indian scene we have somewhat peculiar problems related to such Agreements and consumed considerable time. They are:

- a. Tax Problem
- b.. Number of Agreements to link the total liabilities.
- a. Tax Problem

Tax laws of the country are subject to change. For long periods, income accrued on the work and payments

made outside the country were not subject to local income taxes on Corporations. The agreements, therefore, required to be drafted carefully so that the provisions ensure clear distinction between the work done outside and payments made outside as against work inside the country. Income-tax liabilities arise for the work done and income earned in India. However these tax laws are being simplified and tax liabilities can now be calculated without much difficulty. It may also be noted that income-tax is also leviable on the 'personal' incomes. The various countries have bilateral agreements for exemption of double income-tax on individual income. These and other legal matters complicate the issue and make the finalisation of the Agreements a legal and long affair. Clear understanding of the tax laws of the country of the work would, therefore, make negotiations proceed at a fast pace.

b. Number of Contracts involved:

As indicated above, because of the tax structure, it becomes necessary to enter into two or more distinct agreements for carrying out the total job. At the same time to ensure that the guarantees by the foreign Consultant, are available by linking the Agreements. It would be better if we could develop a suitable simplified form of Agreement. The international engineering companies by their very experience have adequate knowledge in this field and should suggest suitable safe guards.

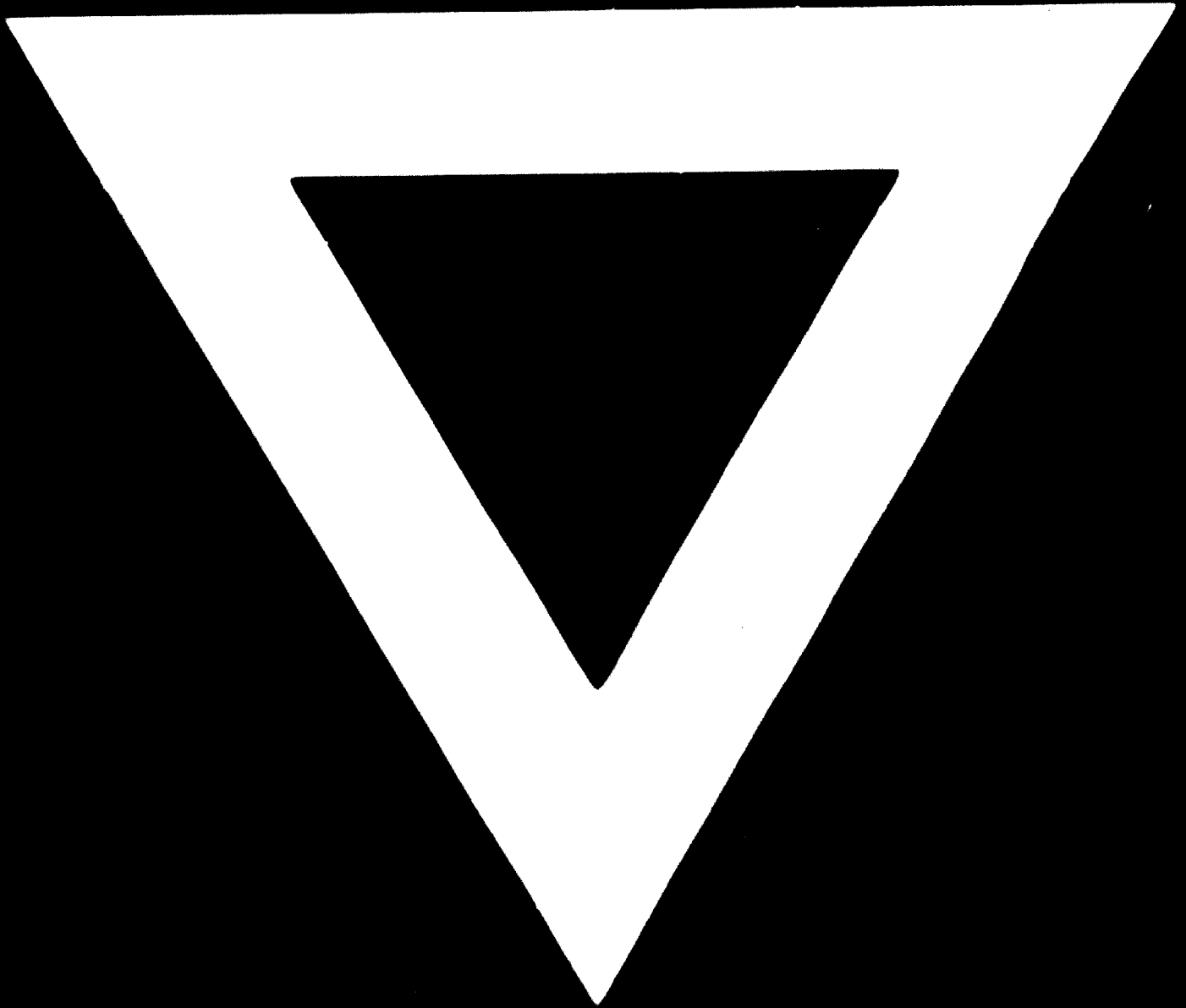
6.5 Preliminary Agreement

After general agreement is reached and draft agreement are ready for signatures, 'preliminary agreement' can be signed by the parties to initiate actions on particularly on long delivery items. A small portion of money is to be committed

for this purpose pending approval from financing bodies and the Government. Initial process engineering and procurement of long delivery items can be initiated. The project execution period can be reduced. We would recommend serious consideration of this approach if it is anticipated that long periods would elapse between agreement by the parties and making effective the agreement then reached.

7.0 In conclusion, it may be said that successful project depends upon the clear understanding of the scope of work involved and the payments due therefor. The contractor should not be subjected to the changing laws of the local Government. At the same time, the contractor should bear legal liability for the profits earned from work in the country. It is possible that financial liability of the contractor could be borne by the Owner, but the Contractor has to submit to the 'legal liability' of the local country. Further, knowledgeable Owner with careful pre-planning and knowledge of the work involved can reduce the period required for reaching agreement and also the areas of conflict during execution. The result of a harmonious agreement would be a job, the results of which both the Owner and the Consultant would be proud of.

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