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BASIC HOST COUNTRY CONSTRUCTION CONTRACTING FOR DEVELOPMENT PROFESSIONALS: A PRIMER

January 2012

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ACRONYMS

A&E	Architecture and Engineering
ADS	Automated Directives System
COTR	Contracting Officer's Technical Representative
CPM	Critical Path Method
D&CMC	Design and Construction Management Contractor--(used alternately with Architecture and Engineering (A&E))
D&CM	Design and Construction Management
EGAT	(USAID Bureau for) Economic Growth, Agriculture, and Trade
FARA	Fixed Amount Reimbursement Agreement
HC	Host Country
HCC	Host Country Contracting
HCIU	Host Country Implementation Unit
HG	Host Government
IFB	Invitation for Bids
IL	Implementation letter
LES	Locally Employed Staff
O&M	Operation and Maintenance
SOW	Scope of Work
USAID	United States Agency for International Development

EXECUTIVE SUMMARY

Over the last three decades, USAID has invested billions of dollars to support engineering and construction projects as part of its efforts to achieve its development objectives in many countries. USAID-funded construction projects covered many sectors and varied in size and complexity. The capacity of the Host Country (HC) Implementation Units (HCIU), contractors, and even USAID missions to undertake construction activities varied from one project to another. As a result, USAID selection of the contracting mechanism has always been a subject of discussion. Among the most commonly used contracting mechanisms were: USAID Direct contracts, USAID Host Country contracts, and Fixed Amount Reimbursement Agreements (FARA).

This Primer provides engineering and non-engineering development professional with a one-stop reference for using USAID-financed Host Country Contracting (HCC) approaches in construction activities. It provides definitions, contracting and implementation guidelines, a discussion of USAID experience in construction projects, a discussion of the challenges and constraints faced and those to be expected, and finally, a discussion of the important lessons learned and recommendations for follow-on activities.

Under HCC for construction, USAID finances goods and services being provided under a contract between the HCIU and the construction contractor. While USAID is not a party to this contractual relationship, USAID must ensure that both parties to the contract are qualified, possess the required technical, management, and financial capabilities and systems that are essential for the successful completion of the construction project, and that the procurement process complies with applicable US Government regulations.

Under Fixed Amount Reimbursement Agreements, USAID reimburses the HC for construction costs upon the physical completion of an activity, a sub-activity, or a quantifiable element within an activity. Reimbursement is based on outputs rather than inputs or costs and the amount of reimbursement is generally fixed in advance.

USAID policy and regulations require that when USAID considers using an HC contract for any procurement anticipated to exceed \$250,000, USAID must first assess the Contracting Agency's procurement system and then obtain the Mission Director's certification of its capability. The assessment may be carried out by the Mission's staff or by an independent contractor.

Construction services are complex, include technical specifications that vary from one project to another, and involve a number of parties and stakeholders, including: the employer, the contractor, subcontractors, the Architecture and Engineering (A&E) firm responsible for providing

design and construction management services, the local authorities, and the community. The HCIU, the technical unit responsible for the procurement of the construction services, and the prime construction contractor are the two legal parties to the construction contract.

The HCIU, generally referred to as “the Employer” or the “the Owner” in the contract document, may be a government entity or a public company. The contractor may be a US, local, or third-country contractor, a prime contractor with a number of US, local, or third-country subcontractors, or a joint venture.

The Employer is the ultimate recipient of the facilities being constructed under the construction project and is responsible for identifying the need and securing required funding.

The construction contractor is responsible for carrying out the construction in accordance with standards, specifications, and contract conditions, on time, and within the contract budget.

The A&E (The Engineer) provides engineering and construction management services. The A&E’s responsibility starts at the design phase and covers the pre-construction and procurement phases, the construction phase, and the commissioning and start-up. It may also extend beyond that to the operation and maintenance period.

USAID provides assistance to the HCIU and the contractor by explaining USAID regulations to ensure compliance with regulations and to safeguard USAID interests and rights. USAID reserves the right to approve most critical steps of the contracting process for any HC procurement in excess of \$250,000. USAID monitors implementation of the project to ensure compliance with the terms of the agreement and contract, proper use of US Government funds, and to ensure that USAID development objectives are achieved.

When using HC contracts in construction, USAID faces a number of challenges and constraints, including: HCIU and contractors’ capabilities, cultural issues, local contracting environment and transparency issues, unclear contract document and specifications, inefficient legal systems, and unclear understanding of roles and responsibilities.

It is important to realize that the Employer is the ultimate recipient of the facilities being constructed under any construction project and as such, the Employer should be involved in every step of the process. USAID also needs to work closely with the HCIU and the A&E to clearly define roles and responsibilities and identify issues as early as possible.

Based on USAID experience in implementing HC construction projects, it is reasonable to emphasize that competition, and transparency of the procurement process, ensure that the contract is awarded to the most qualified contractor at the lowest price. The prequalification process is extremely important and the prequalification criteria determine the qualifications of the prospective bidders.

USAID and its implementing parties have identified a number of important lessons learned over three decades of implementing USAID-funded construction projects. USAID and its partners now realize that clarity of the evaluation and selection criteria minimizes procurement delays and protests; clear contract clauses lay the foundation for successful implementation; the A&E plays a major and crucial role in the success of any project; periodic review of the Project Schedule and early identification of critical activities is essential to avoid costly delays; and of utmost importance is that construction is a team work job – success and failure affect the whole team.

I. INTRODUCTION AND BACKGROUND

I.1. USAID CONTRACTING

Over the last three decades, the United States Agency for International Development (USAID) has provided billions of dollars to finance engineering and construction projects in many countries. This has been part of USAID efforts to achieve US Government development objectives. USAID funds have been successfully utilized to support a variety of construction projects in a number of sectors, including health, water and wastewater, energy, education, roads, telecommunications, and others. These projects varied from country to country according to the nature of each project, its size, and its technical complexity. The capabilities of the Host Country (HC) counterparts tasked with implementing the projects were different from country to country and in many cases within the same country. The qualifications and capabilities of the contractors and engineering firms designing and carrying out the actual construction were also different.

Projects funded by USAID varied in terms of size and complexity from major state-of-the-art power plants, paved trunk roads, water treatment plants, and wastewater treatment plants costing hundreds of millions of dollars, to simple one-classroom schools, rural earth and gravel roads or water stand posts in a village, each serving few households.

In implementing these projects, USAID has worked closely with the Host Country Implementation Unit (HCIU), the Host Government unit authorized by the recipient Host Government (Borrower or Grantee) for implementing projects in accordance with the Bilateral Agreements between USAID and the Host Government. While these HCIUs were, in a few cases, major well established and capable government authorities with thousands of employees and relatively sophisticated systems, in most cases, they were simple local government units operating in small urban or rural areas with very limited resources and few qualified personnel. It is important to point out that not many of these government units had appropriate management, procurement, and financial management systems and expertise that made them capable of undertaking infrastructure programs. In most of the cases, these units needed significant assistance and hand-holding throughout the design, procurement, and construction phases of USAID-funded infrastructure programs.

Similarly, design, construction, and construction supervision of these projects were either carried out by major US engineering and

construction contractors or by local engineering and construction contractors. Local contractors' capabilities also varied greatly from one country to the other and within the same country.

USAID had a crucial and important role to play in ensuring that Host Government counterparts and contractors successfully completed projects. However, it is important to realize that USAID missions were also different in terms of their ability to handle construction activities for a number of reasons, including not having the required engineering staff and contracting experience required for designing and implementing construction programs. Missions were faced with the need to make many important decisions, including the selection of the contracting mechanism to be used in carrying out construction activities. USAID Direct Contracting, Host Country Contracting (HCC), and Fixed Amount Reimbursement Agreements (FARAs), or a combination of these three types, have been the most commonly used contracting mechanisms.



USAID is undergoing major transformation in the way it is implementing its activities. To better realize development objectives, USAID is placing more emphasis on using Host Country systems in carrying out engineering and construction projects. This places more emphasis on using Host Country contracts and Fixed Amount Reimbursement Agreements.

I.2. OBJECTIVES

This Primer provides a brief description and discussion of the different types of acquisition contracting approaches that USAID has generally used throughout the years in designing and implementing its construction programs. The Primer then provides more details on providing contracting and implementation guidelines for using HCC mechanisms in carrying out a variety of construction activities. The document includes definitions, contracting and implementation guidelines, a discussion of USAID experience in construction projects, discussions of the challenges and constraints faced and those to be expected, and finally, a discussion of the important lessons learned. The USAID Automated Directive Systems (ADS) and its Supplementary References in effect at the time of drafting this document represent the primary source of guidance discussed in this document regarding the use of HCC in construction. ADS clauses are quoted throughout the document.

The primary objective of this Primer is to provide engineering and non-engineering development professionals with a one-stop reference for the use of USAID-financed HCC approaches and to describe USAID's role and responsibilities in the implementation of USAID-financed Host Country construction contracts.

Throughout this document, emphasis is placed on USAID/Egypt's 30 years of experience in implementing one of USAID's major, most

challenging, and diverse infrastructure programs using Direct contracts, Host Country contracts, and FARAs.

It is important to note that while USAID direct contracting and FARAs are not the subject of this Primer, it provides a brief overview of the use of direct contracting and sheds light on the difference between direct contracting, HCC, and FARAs.

It is equally important to note that USAID ADS guidance regarding the “Use of Reliable Partner Country Systems for Direct Management and Implementation of Assistance” (ADS 220) are not discussed in this Primer, as they apply to assistance to the Host Country in general and are not specific to the use of HCC in construction projects.

2. USAID INFRASTRUCTURE CONTRACTING OVERVIEW

Over more than 30 years of providing funding to support infrastructure projects, USAID selection of the contracting mechanisms to be used in implementing its infrastructure programs has always been a subject of discussion and has varied from mission to mission. USAID missions' decisions were based on several crucial factors, including: the size and complexity of the project to be implemented; the contracting, engineering, and management capabilities of the HCIU; and the technical and engineering capabilities of mission staff charged with the design and implementation of the infrastructure program.

Most USAID-funded large complex infrastructure programs have been generally carried out by US construction contractors, either in the form of one prime US contractor with US and local subcontractors, or a joint venture of US contractors with US and local subcontractors. USAID-funded simple, small-scale construction projects have been generally carried out by local qualified construction contractors and subcontractors. Based on the selected contracting mechanism and the type of contract used, USAID funding has been either in US dollars or local currency (local procurement).



It is important to point out that, regardless of the contracting mechanism used, USAID has relied in almost all of its successful projects on qualified engineering firms for the design, procurement, and construction management services. While these services were provided mostly by US engineering firms or consortia with local engineering subcontractors in large infrastructure programs, the same services were generally provided by local qualified engineering consultants in simple small-scale infrastructure projects. USAID played a major and leading role in introducing the concept of utilizing the services of an Architecture and Engineering (A&E) firm when carrying out construction programs. USAID's role included providing guidelines for developing the scope of work (SOW) for these engineering services, establishing the selection criteria, developing cost estimates, and monitoring performance of the A&E firms.

During the first generation of USAID-funded infrastructure programs, several A&E contracts were awarded under HCC arrangements. Under these contracts, A&E firms faced many challenges, including maintaining impartiality and receiving payments for services rendered. In the late 1980s, USAID decided to award A&E contracts through direct contracting, the model used throughout this Primer.

3. USAID INFRASTRUCTURE CONTRACTING MECHANISMS

Following is a brief overview of three contracting mechanisms USAID has generally used in implementing its construction programs:

3.1. USAID DIRECT CONTRACTING

In direct contracting, USAID enters into a mutually binding legal relationship obligating the seller (“contractor”) to furnish supplies or services and the buyer (“USAID”) to pay for them (ADS 301).

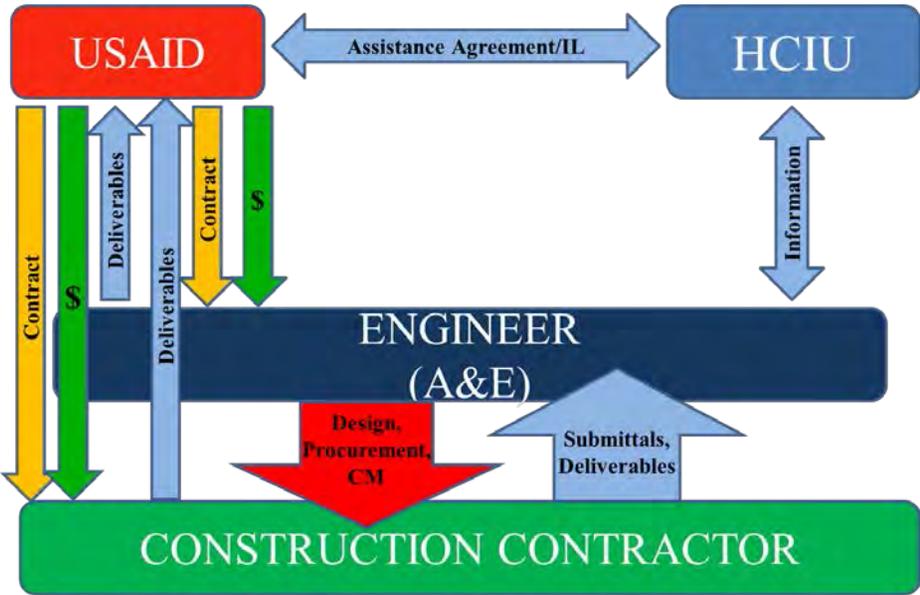


FIGURE 1: USAID DIRECT CONSTRUCTION CONTRACTS

In direct contracting, USAID has a clear direct contractual relationship with the contractor (Figure 1). USAID receives the goods or services and pays for them. USAID is directly involved in the procurement process and implementation.

Under this type of contracting, USAID would generally: contract with the A&E firm to prepare the designs and required studies (environmental, feasibility, demographic, geotechnical, etc.), manage the

procurement process, and provide construction management services. USAID would also contract directly with the construction contractor.

3.2. HOST COUNTRY CONTRACTING (ADS GLOSSARY)

Host Country Contracting is a means of program implementation in which USAID finances, but is not a party to, contractual arrangements between the Host Country and the supplier of goods and/or services. (ADS 301, 305).

3.3. HOST COUNTRY BILATERAL AND IMPLEMENTATION RELATIONSHIPS

Before discussing HCC for construction services it is important to clarify the bilateral and implementation relationships governing USAID-funded HCC construction projects. These relationships can be best explained by dividing them into four separate levels, as illustrated in Figure 2.

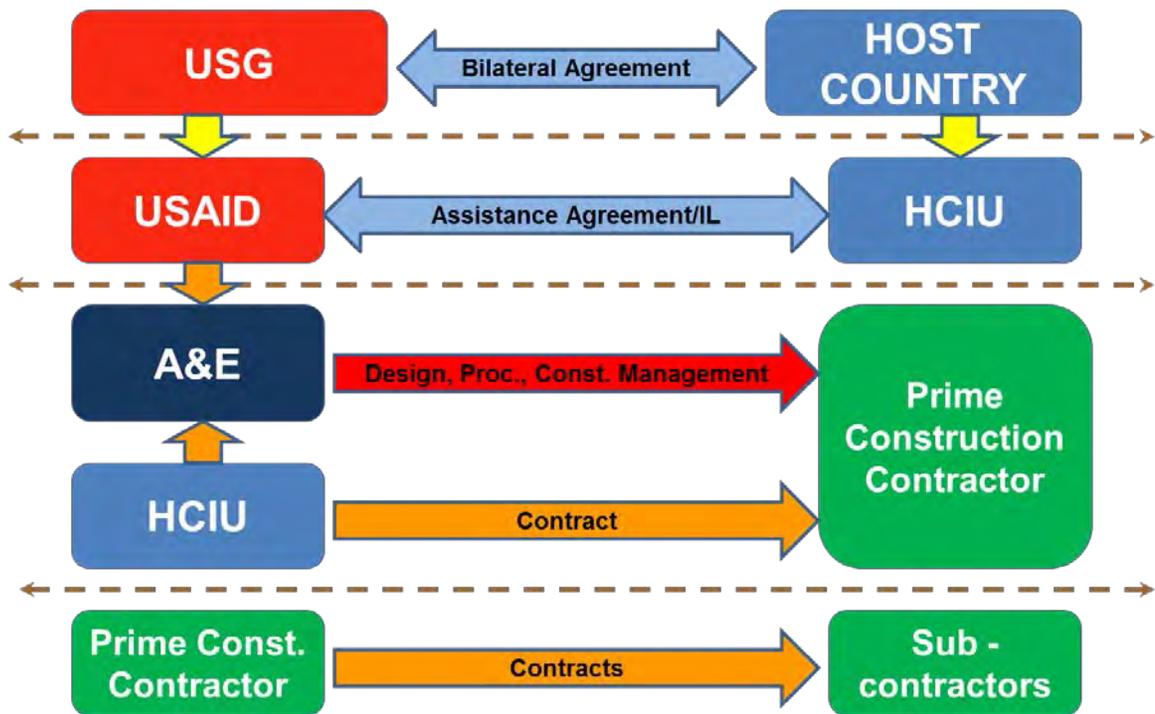


FIGURE 2: HCC CONSTRUCTION RELATIONSHIPS LEVELS

The first level or tier is the bilateral relationship between the US Government and the Host Country Government, which is usually established through a Bilateral Agreement that describes the general terms of the relationship between the two countries in relation to USAID’s development program.

The second level is the implementation relationship or working relationship between USAID, representing the development arm of the US Government, and the HCIU receiving USAID support, on behalf of the Host Country Government, and tasked with the implementation of the project. This is usually established through an Assistance Agreement or an Implementation Letter (IL)

The third level is the relationship between the implementation partners: the HCIU, the prime construction contractor carrying the construction activities, and the Engineering firm (A&E) responsible for the design, procurement, and construction management of the project. These relationships are generally established through contract agreements that are in most cases subject to the review and approval of USAID.

The fourth level includes the relationship between the prime contractor and its subcontractors and suppliers of goods and services. These relationships are usually established through subcontract agreements between the prime contractor and the subcontractors. USAID and the HCIU have very little involvement, if any, in these relationships.

3.3.1. HOST COUNTRY CONSTRUCTION CONTRACTING

In HCC for construction services, USAID finances the goods and services being provided under a contractual relationship between the HCIU and the construction contractor (Figure 3). Although USAID is

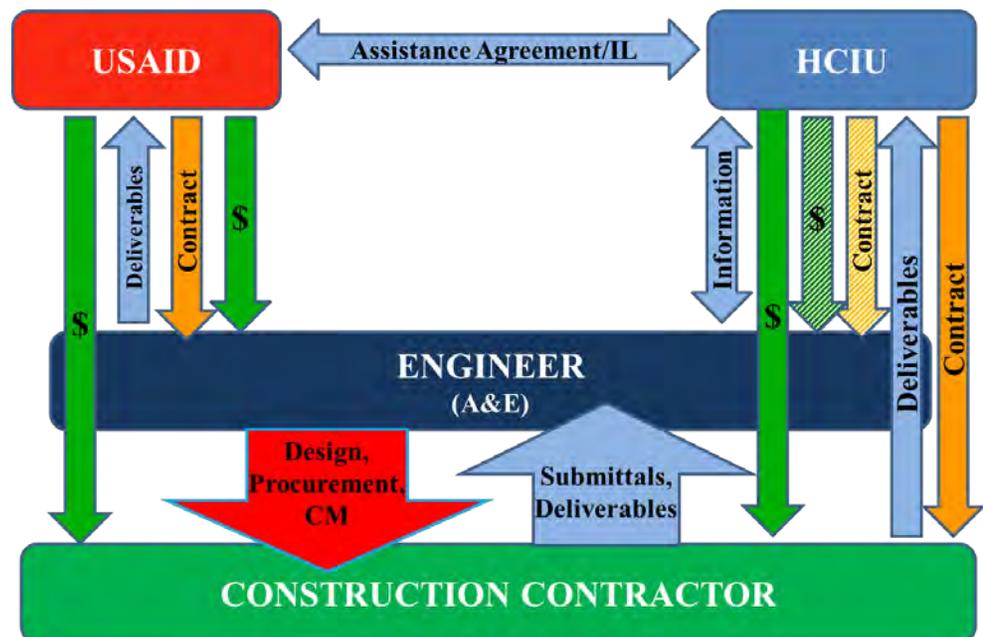


FIGURE 3: USAID HC CONSTRUCTION CONTRACTS

not a party to this contractual relationship, USAID is interested in seeing this activity completed successfully in order to protect its investment

and achieve its development objectives. USAID must ensure that both parties to the contract are qualified; possess the required technical, management, and financial systems that are essential for the successful completion of the construction project; and that the procurement process and implementation steps are in accordance with applicable US Government regulations.

In order to illustrate the relationships between the parties under a Host Country contract, the model used successfully by several USAID missions in implementing large and small size infrastructure programs will be presented.

Under this model, USAID enters into a direct contract with the A&E firm. The HCIU contracts with the construction contractor. In other words, it is a combination of direct and HCC. This model has been used throughout the second generation of USAID-funded infrastructure projects in Egypt to address some of the issues and concerns that developed when both the A&E and construction contracts were host country contracts with the HCIU. Under this model:

- USAID enters into a direct contract agreement with the A&E firm to carry out its tasks on behalf of the HCIU.
- The A&E firm provides support to the HCIU throughout the process to develop construction tender documents, prequalify construction contractors, evaluate tenders, and award contracts.
- The HCIU awards the construction contract to the lowest responsive and responsible bidder.
- The A&E provides all contract administration and construction management services and submits contract submittals and deliverables related to the direct contract to USAID.
- The construction contractor undertakes construction services and submits deliverables and submittals to the Engineer for review and approval. The A&E reviews the submittals and deliverables and either approves or rejects the submittals. The A&E keeps USAID and the HCIU informed of the status of submittals and requests approval when required by the contract.
- The construction contractor submits progress payment requests to the A&E firm for review and approval.
- Once a progress payment request has been approved by the A&E, the HCIU approves the progress payment request and pays the local portion to the construction contractor. USAID pays the US dollars portion to the construction contractor.
- The A&E inspects the works on a continuous basis and issues the certificate of final completion and acceptance of the work.

- The A&E works closely with the contractor and the HCIU to ensure successful taking over and operation and maintenance of the facilities completed.
- The A&E ensures settlement of all outstanding obligations and assists the HCIU in the evaluation of outstanding claims.

3.4. FIXED AMOUNT REIMBURSEMENT AGREEMENTS (FARA)

The use of Fixed Amount Reimbursement Agreements is a form of assistance under which the amount of reimbursement is generally fixed in advance based upon cost estimates reviewed and approved by USAID. Reimbursement is made upon the physical completion of an activity, a sub-activity, or a quantifiable element within an activity. The emphasis is upon reimbursement based on outputs rather than inputs or costs (ADS 317, 630). Figure 4 illustrates the relationship between parties under a FARA.

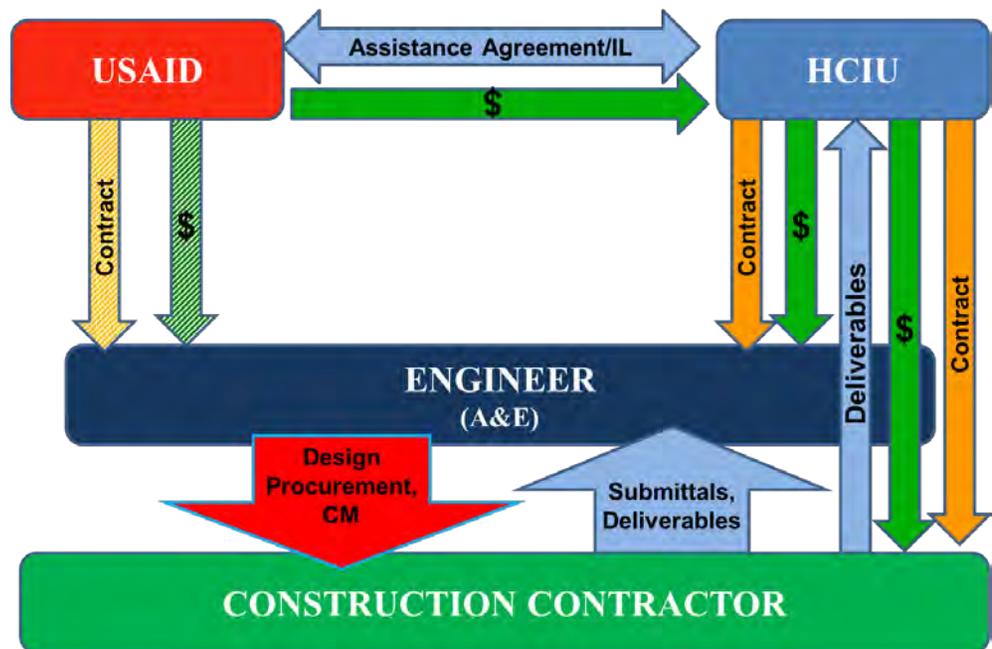


FIGURE 4: FIXED AMOUNT REIMBURSEMENT AGREEMENT

Under this model, the HCIU enters into contractual arrangements with the A&E firm and the construction contractor. USAID reimburses the HCIU upon the physical completion of the activity, a sub-activity, or a quantifiable element (stages of the work). The amount of reimbursement is generally fixed in advance. An alternative to this model has been used where USAID enters into a direct contract with the A&E on behalf of the HCIU.

3.5. DISTINCTION BETWEEN DIRECT AND HOST COUNTRY CONTRACTING

USAID direct contracts follow the Federal Acquisition Regulations (and USAID Acquisition Regulations) and maximize USAID control over the activity in question. When USAID decides to use HCC procedures, on the other hand, it acts as a financier and not a contracting party, reserving certain rights of approval and activity monitoring (ADS301.5.1a).

4. GENERAL HOST COUNTRY CONTRACTING GUIDELINES

4.1. SCOPE OF HOST COUNTRY CONTRACTING

Host Country Contracting is generally used for the procurement of:

- Goods
- Services
- Construction Services

4.2. SELECTING A CONTRACTING MECHANISM (CONTRACTING APPROACH)

- USAID regulations do not specify a general preference. However, there are a number of factors that have a major effect on such decision including: the Host Country preference; the activity design and objectives; the type of goods or services required; time constraints; the procurement capability of the proposed contracting agency for contractor selection, contract administration, and contract audit; the estimated relative costs; availability of Host Country systems and procedures; availability and experience of USAID procurement, legal and program staff; and the expected effects on the institutional or professional relationships with the Host Country (ADS 301).
- ADS 301.5.1.b).5 states that: in special circumstances, such as having a contract for construction services, the use of a Host Country contract is usually more appropriate for the procurement of construction services.

5. ASSESSMENT OF THE HOST COUNTRY CONTRACTING AND PROCUREMENT SYSTEMS (ADS 301.5.2)

5.1. USAID POLICY

USAID policy and regulations require that when USAID considers using a Host Country contract for any procurement anticipated to exceed \$250,000 (including local currency), USAID must first establish a team to assess the Contracting Agency's procurement system and then obtain the Mission Director's certification of its capability. The assessment team shall consist of Mission staff with qualifications necessary to assess all aspects of the Contracting Agency's capabilities: the Controller, Contracting Officer, and Legal Advisor (either as members of the team or reviewers). Other Mission or Regional personnel, such as the Mission Engineer and Commodity Management Officer, may participate or provide advice to the extent that their areas of expertise are pertinent to the assessment. Institutional contractors may also be used to conduct the assessment.

5.2. RESULTS OF THE ASSESSMENT

If the assessment results in a recommendation that Host Country Contracting is practical, then the Mission Director shall make a positive determination that the Host Country Contracting Agency has or will obtain the capability to undertake the procurement. If the assessment indicates that use of Host Country Contracting would be impractical or inappropriate and the Mission Director cannot make such a determination, then contracting by USAID itself or procurement by another US Government Agency must be used.

5.3. RESPONSIBILITY FOR THE HOST COUNTRY CONTRACTING ASSESSMENT (ADS 301.3)

- The Strategic/Development Objective team is responsible for ensuring that activities are designed to assign the responsibility for procurement where it will best serve the objective. When HCC is going to be used, the Strategic Objective team has the primary responsibility to see that the required assessment of the Contracting Agency's procurement system has been conducted.
- The contracting officer, controller, and legal advisor are responsible for assessing the Contracting Agency's procurement system as part of the Host Country assessment team, or for reviewing the assessment and offering recommendations before the Mission Director can certify that the Contracting Agency's procurement system is acceptable.
- When their areas of expertise are involved, the Mission Engineer and Commodity Management Officer are responsible for participating in the Host Country assessment.
- The Mission controller is responsible for ensuring that the Contracting Agency's accounting system and internal controls are adequate.
- The Mission Director is responsible for reviewing the recommendations of the Host Country assessment team and for certifying the acceptability of the Contracting Agency's procurement system if the facts support doing so.

5.4. USING A CONTRACTOR TO CONDUCT AN ASSESSMENT

- USAID may decide to engage an independent contractor for conducting or participating in the assessment. In this case, USAID has to review and approve the contractor's determination and recommendations.

5.5. CERTIFICATION REQUIREMENT (ADS E 301.5.2b)

- The Mission Director must certify, in writing, that the Contracting Agency has the capability to undertake the specific procurement action.
- If the assessment discloses significant weaknesses in the Contracting Agency's capability, but not so significant that the Mission cannot work with the Contracting Agency to overcome them and the Mission

intends to proceed with approving HCC for the specific activity in question, then the Mission Director's certification must be modified to identify the particular weaknesses in capability identified, the Mission's plans to resolve the problems, and in view of the foregoing, the Mission Director's determination that HCC is the appropriate contracting method.

- The assessment of the Contracting Agency's procurement capability and the certification by the Mission Director must be kept as part of the official activity files.

5.6. NO WAIVER PROVISION

USAID regulations do not allow for waiving the requirement of conducting an assessment of the Host Country's procurement systems and contracting capabilities and obtaining the required certification prior to the use of HCC.

6. HOST COUNTRY CONTRACTING FOR CONSTRUCTION SERVICES

6.1. IS HOST COUNTRY CONTRACTING THE RIGHT CHOICE?

Procurement of construction services is different from procurement of other simpler types of services, technical assistance, goods, or equipment. In construction projects, the nature of the work is generally more complex, with technical specifications that vary according to the function of the facility being constructed. It also involves more parties and stakeholders, including: the employer, the contractor and its specialized subcontractors, the A&E firm responsible for providing construction management services, the local authorities, the community where the facility will be constructed, existing on-site and off-site utilities, etc. Other important and influencing factors include the need to protect and care for the environment, land tenure, right of way permitting, and safety of workers and the community.



It is quite normal in any construction project that all parties are faced with unforeseen site conditions, or the need to modify the technical specifications to respond to any unpredicted circumstances or new developments. This requires parties to make quick and technically defensible decisions that may result in minor or major changes to the contract cost or time for completion.

Disputes may arise over some of these variations to the contract and in some cases may result in interruptions to the construction schedule or the anticipated completion date. A clear definition of the roles of parties involved and the ability and willingness of the HCIU unit to assume its responsibilities as the employer and the ultimate recipient of the facilities being constructed is essential for avoiding claims and for settlement of disputes.

In Host Country contracting, the HCIU is the contracting authority for the contract with the construction contractor, and as such, is responsible and has the liability for all the consequences of any inaction or non-compliance with any of the contract provisions by the Host Government.

6.2. PARTIES TO A HOST COUNTRY CONSTRUCTION CONTRACT

The two legal parties to any Host Country construction contract are the HCIU, the technical unit responsible for the procurement of the construction services – and in most cases, the operation of the facility once completed – and the prime construction contractor (Contractor).

The HCIU, generally referred to as “the Employer” or the “the Owner” in the contract document, may be a government entity or a public company. The contractor, depending on the USAID-authorized geographic code for the project and nationality requirements, may be a US, local, or third country contractor. The contractor may be a prime contractor with a number of US, local, or third country subcontractors. The Contractor may also be a joint venture of two or more contractors with a number of US, local, and third country subcontractors.

6.3. SCOPE OF WORK UNDER A HOST COUNTRY CONSTRUCTION CONTRACT

Similar to any construction contract, the scope of construction services under a Host Country construction contract includes technical and specialized work that results in complicated relationships with other contractors, suppliers, local authorities, etc. The scope of work may cover a wide variety of disciplines, including: engineering design, environmental, geophysical, structural, electrical, mechanical, cost estimating, geotechnical surveillance, scheduling, legal, etc.



A construction contract would typically specify the required work, quantities, general specifications and requirements, general conditions of contract, conditions of particular application, financial requirements, liability of parties, safety measures to be undertaken by the contractor, environmental mitigation measures, etc. USAID has used the FIDIC (International Federation of Consulting Engineers)-based conditions of contract in its construction programs. These conditions specify the role of the parties to the construction contract and the A&E, and lays down all the conditions related to the performance of the work under the construction contract. Conditions of particular applications are usually added to specify special requirements and to include USAID requirements and mandatory contract clauses.

The contract may be amended during construction through change orders or variation orders to respond to varied work conditions or site specific conditions or requirements. Rather than amending the contract every time there is a need to address justified changes, it is recommended to include a “Provisional Sum” line item in the contract budget to address these situations. The Provisional Sum is usually a fixed amount that is included in the bid and can be used for payment of any costs resulting from approved variation orders.

The contract usually specifies the approach for settling disputes and litigation.

Some construction contracts include additional provisions such as Value Engineering and Alternate Dispute Resolution. These provisions help the parties reach agreement on disputes without having to go through lengthy and costly litigation.

6.4. ROLE OF THE EMPLOYER

The Employer (Owner) is the ultimate recipient of the facilities being constructed under the construction project and is responsible for securing required funding. It is reasonable to assume that the Employer has to make every effort to clearly identify the problem and the need. Once this is done, the employer has to engage the right resources for drafting a problem statement, developing preliminary designs, identifying alternatives, estimating required resources and time frame, developing designs and specifications, and procuring engineering and construction services. Although, in some cases, part or all of the foregoing might be done using the Employer's own staff and technical offices, it is reasonable to expect that in most cases, the employer typically would not have the required engineering expertise. An example would be construction of medical facilities. In this example, the employer's staff are mostly medical and administrative professionals, with limited engineering expertise for maintenance purposes. Another example would be the construction of a school, where the technical expertise of the Employer's staff is in education.

On the other hand, when constructing a road for the transportation sector, the Employer's engineering expertise might not be an issue. However, one can argue that even in this case, the role of the employer should be limited to developing the scope of work and monitoring the performance of an A&E firm that can bring multiple skills to the task.

6.5. ROLE OF THE CONSTRUCTION CONTRACTOR

The construction contractor is responsible for carrying out the construction in accordance with the standards, specifications, and contract conditions, on time, and within the contract budget. To achieve this goal, the contractor is expected to provide all required resources, including: qualified subcontractors and suppliers, construction equipment, and a highly qualified team to cover all required expertise. The contractor is expected to furnish all required bonds and warranties, ensure safety of his team and other stakeholders on the job, and indemnify USAID, the employer, and the A&E from any liability resulting from performing the scope of the construction contract.

6.6. ROLE OF THE DESIGN AND CONSTRUCTION MANAGEMENT CONTRACTOR

During the design phase of the project, the A&E firm is responsible for undertaking a number of tasks, including: developing the project's preliminary and final designs, conducting the required environmental studies, developing feasibility studies, developing preliminary cost estimates and alternatives, and preparing a preliminary schedule for the project.

During the pre-construction phase of the project, the A&E firm is responsible for a number of tasks, including: managing the solicitation process, developing the prequalification questionnaire and the list of prequalified construction contractors, developing bid and contract documents and specifications, developing the final cost estimate, arranging for the pre-bid conference, responding to requests for clarification, issuing the Invitation for Bids (IFB) addenda, receipt and evaluation of bids, and recommending contract award.



During the construction phase of the project, the A&E is responsible for a wide variety of tasks, including: construction monitoring and inspection, keeping daily logs, measurement, acceptance of the work, non-compliance reports, review and approval of as-built drawings, project schedule, project budget and cash flow, variation orders (according to the authority delegated by the Employer), immediate action variation orders and field orders, progress and final payments (unit price, lump sum, fixed), final inspection, commissioning, O&M manual and plans, spare parts, defects liability, on-the-job training, claims management, settlement of disputes, and other required services.

6.7. USAID/HOST GOVERNMENT BILATERAL RELATIONSHIP

USAID programs are usually covered by a bilateral grant agreement that provides a description of the project to be funded by USAID, specifies the level of funding, and sets the terms for carrying out the project. At this point in time, the information available may not allow for having detailed designs or accurate cost estimates. In this case, activities may be specified by expected outputs in terms of final product or capacities, or even number of beneficiaries.



6.8. ROLE OF USAID IN HOST COUNTRY CONSTRUCTION CONTRACTING

When defining the USAID role in any Host Country construction contract, it is extremely important to remember that: USAID is not a party to the Host Country construction contract, USAID acts as the

financier, and that USAID has development goals and represents the US Government.

USAID is responsible for providing assistance to the Contracting Agency in understanding USAID regulations. USAID may also explain USAID procedures to the contractors. This will help in ensuring compliance with USAID regulations and in safeguarding USAID interests and rights.

USAID responsibilities include: assisting the HCIU in preparing and publicizing prequalification questionnaires and requests for proposals; guiding the HCIU in developing independent cost estimates; overseeing and monitoring all aspects of the project from conceptualization through design, approval, funding, negotiation; signing project agreements; implementation; monitoring contractors' performance; participating in periodic review meetings with the HCIU and the contractors to review progress; making periodic visits to the site of the project (normally with representatives of the HCIU and the A&E); reviewing and approving progress payments; assisting the Host Country Contracting Agency and/or the contractor in resolving problems hampering the work of the contractor; and conducting the final evaluation. The USAID role includes developing the SOW for the A&E, clearly defining roles and responsibilities, monitoring A&E performance, checking deliverables, reviewing payment requests, reviewing project schedule, approving contracting steps; reviewing requests for variation orders approval, and assisting parties in contract close out and settlement of disputes.

In sum, USAID is responsible for undertaking all required actions for ensuring the proper and prudent use of the US government funds.

6.9. USAID APPROVALS OF CONTRACTING STEPS (ADS 305.5.1)

USAID reserves the right of prior approval of the most critical steps of the contracting process for any Host Country procurement in excess of \$250,000. It is important to note that USAID exercise of its approval rights is not to be construed in any case as making USAID a party to a contract. Following are some of the steps that require USAID approval:

- Notices to prospective offerors
- Lists of prequalified offerors prior to issuance of the solicitation document
- Complete solicitation document, prior to issuance
- The contractor selection method (may be part of approval of solicitation document)
- The selected contractor

- Any host Contracting Agency decision to terminate negotiations with the highest ranked offeror and to initiate negotiations with the next ranked offeror or to reject all offers
- The contract, prior to execution
- Signed contract documents, before financing
- Contract administrative actions such as subcontracts, amendments, and change orders, as determined by the Mission and stipulated in an Implementation Letter
- The Mission may require additional approvals for other actions taken by the Contracting Agency during the contracting process. Such additional approval requirements must be set forth in an Implementation Letter
- USAID Mandatory Contract Requirements and Clauses (ADS 305.5.7) must be included in every USAID-financed Host Country contract, including Legal Effects of USAID Approvals and Decisions, Audits and Records, Host Country Taxes, Nationality and Source, Air Travel and Transportation, Settlement of Disputes, Documentation for Payment, Disposition of Personal Property, Equal Employment Opportunity, Workers Compensation Insurance, Anti-Corruption Provisions, Marking, Vesting of Title and Diversion Rights, Nationality, Terrorist Financing, Branding, and Debarment, Suspension, Ineligibility, and Voluntary Exclusion.

6.10. PROCEDURES FOR AWARDING HC CONSTRUCTION CONTRACTS

Formal competitive bidding among qualified bidders is the normal procedure for awarding contracts for construction services. Formal competitive bid procedures include public advertising, issuance of invitations for bids, public opening of sealed bids, evaluation of bids, and award of a contract to the lowest responsive and responsible bidder.

Contracts for construction services may be awarded on the basis of competitive negotiation only if the Contracting Agency has failed, after diligent efforts, to secure a contract through formal competitive bid procedures and further use of formal competitive bid procedures clearly would not be productive. The Mission Director must approve the use of competitivenegotiation. (ADS 305.5.2b)



6.11. TRADITIONAL HC CONSTRUCTION CONTRACTS AND FARA

WHAT IS THE DIFFERENCE?

Under a traditional Host Country contract, USAID provides all or a portion of the funding to cover the signed contract between the HCIU and the contractor. The amount of USAID's commitment is outlined in an Implementation Letter. USAID pays invoices that reflect progress of the work. USAID may pay directly to the contractor, or in some cases reimburses the HCIU for invoices paid to the contractor. USAID has significant approval rights for the selection of the contractor and contract administration actions. Although the total contract amount may change as a result of any approved change orders in response to varied site conditions or any unforeseen circumstances, USAID commitment is limited to the amount stated in the IL. However, USAID may increase the amount if necessary. In a Host Country contract, USAID has monitoring responsibilities and relies on the A&E firm for construction management services and on-site daily supervision of the work.

Under a FARA, USAID agrees to finance an activity without getting into any form of contractual relationship with the contractor. The amount of reimbursement is generally fixed in advance based on cost estimates and specifications that have been reviewed and approved by USAID. Reimbursement is made to the HCIU when an activity, a sub-activity, or a quantifiable element within an activity is physically completed according to the approved specifications. The emphasis is on reimbursement based on outputs rather than inputs or costs. The reimbursement amount is generally fixed in advance and may be more or less than the actual contract amount. USAID is not obliged to pay for any contractual cost overruns or variation orders. USAID is not a party to the construction contract and does not approve the selected contractor, the contract, or any of its administrative actions. USAID has monitoring responsibility to ensure that specifications are met. USAID relies on the A&E firm for construction management services and on-site daily supervision of the work. USAID liability and the risk involved are much less than that in a Host Country contract.

Host Country Contracting can be used for simple projects as well as for large complex infrastructure project. Generally a FARA is a recommended approach for simple, low cost, short duration projects.

6.12. PRIOR TO ENTERING INTO HC CONTRACTS

Prior to using HCC in construction activities, USAID should address some important questions including:

- Has USAID conducted an assessment of the Host Country procurement and contracting capabilities?
- Do prospective construction contractors, subcontractors, and suppliers possess the technical and financial capability to undertake the construction activity?
- Are prospective A&E firms qualified to perform the required engineering tasks?
- What is the risk involved and how can we mitigate it?
- Is sustainability an issue?
- Does the USAID mission have qualified staff to manage the design, procurement, and implementation of the project?
- Does the legal system have the capacity for settlement of disputes that may arise as a result of the contract?

6.13. CONSTRAINTS OF USING HOST COUNTRY CONTRACTING APPROACH

When using Host Country contracts in construction, USAID faces a number of constraints including:

- HCIU capabilities (technical, financial, management, administrative, language)
- Contractors capabilities (technical, experience, resources, familiarity with type of contract)
- Cultural issues
- Local contracting environment and transparency issues
- Unclear contract document and clauses
- Unclear specifications
- Inefficient legal systems
- Delays in responding to correspondence and variation orders requests
- Unclear understanding of roles and responsibilities
- Site access and right of way issues
- Required permits by multiple government authorities
- Host Country taxes and levies
- Sustainability issues (O&M costs, preventive maintenance, cost recovery)

6.14. USAID SUPPORT TO HCIU UNDER HOST COUNTRY CONSTRUCTION CONTRACTING

USAID has important development goals. A Host Country construction contract is not only a mechanism to procure construction services; it is also a tool for development. In designing Host Country procurement, USAID should also consider how to develop the capabilities of the HCIU and provide it with required assistance to implement HCC in a way satisfactory to USAID. As an example, USAID may fund the A&E contract to provide design and construction management services throughout the construction program. This helps ensure a successful project and can also serve as an effective on-the-job training opportunity for HCIU officials. USAID may also fund an institutional development technical assistance contract to provide a more structured approach to enhancing the capabilities of the HCIU officials for the short and long term.

6.15. HCC REPORTING REQUIREMENTS

Under a Host Country construction contract, the contractor submits a number of reports to the A&E firm. These reports cover a wide variety of areas including: technical, financial, staffing, management, scheduling, etc. The A&E firm submits to USAID monthly and quarterly reports covering all aspects of the project and technical reports. Monthly and quarterly reports cover all aspects of the project, including: progress, anticipated activities for coming month, major problem areas and recommendations, contractor's staffing, contractor's compliance with contract requirements, schedule/critical activities using the Critical Path Method (CPM), financial summary, cash flow, cost to complete, outstanding claims, anticipated claims, etc.

6.16. USAID MANAGEMENT OF HOST COUNTRY CONSTRUCTION PROJECTS

Missions planning to finance construction projects should have technically qualified staff to manage the design, procurement, and monitoring of engineering and construction activities. Engineers, US and/or Locally Employed Staff (LES or foreign service nationals), provide the Mission with the technical capability required in addition to other staff with experience in contracting, finance, and legal issues.

It is equally important to realize that while some USAID missions have little or no experience in the design, procurement, and implementation of construction projects using HCC, there are some missions with long experience and qualified engineering staff, who have a successful track record of implementing large and small infrastructure programs. This represents an excellent opportunity for cooperation between missions to develop the capacity of missions when needed.

The USAID Bureau for Economic Growth, Agriculture, and Trade (EGAT) is well situated to provide support to missions through its engineering staff or through the use of the A&E Indefinite Quantity Contract (IQC).

7. LESSONS LEARNED AND BEST PRACTICES

Following are some of the lessons learned that were identified by USAID staff who were involved in designing and implementing construction projects under HCC arrangements during the last three decades:

- The Employer is the ultimate recipient of the facilities being constructed under any construction project and should be involved in every step of the process.
- Work closely with the HCIU and the A&E to identify issues as early as possible.
- Dealing with a different culture needs more effort. Do your best to understand and respect other cultures in developing countries.
- Clearly define the role of each party.
- Clear and well-defined scope and specifications reflect your expectations. You get what you specify in the contract.
- Planning for the whole project is essential. This saves a lot of time during procurement and implementation.
- Competition, and transparency of the procurement process, ensure that the contract is awarded to the most qualified contractor at the lowest price.
- Prequalification of contractors is necessary to ensure only qualified bidders submit price proposals or bids. It minimizes the chances of an unrealistically low bid from unqualified contractors that the HCIU would later have difficulty throwing out.
- Evaluation and selection criteria should be clear to avoid delay and protests.
- Discuss areas of controversy as early as possible. Chances of resolving disagreements are higher at the beginning of the contract execution.
- USAID requirements should be clearly stated and well-documented.
- Clear contract clauses represent the basis for successful implementation.
- Avoid repeating contract clauses to avoid contradiction.

- Use contract tools such as the Alternate Dispute Resolution clause to resolve disagreements.
- Construction is a team work job. Success and failure affect the whole team.
- The A&E firm plays a major and crucial role in the success of any project. A qualified A&E firm ensures a better product.
- The A&E firm is your representative on the job. Delegate authority to the A&E firm to perform the job properly.
- Continuously review the Project Schedule and identify critical activities.

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