



# Procurement

*This guideline expands on what is expected by the criteria statements in the Hydropower Sustainability Tools (HST) for the Procurement topic, relating to assessment, management, conformance/compliance and outcomes. The good practice criteria are expressed for the preparation and implementation stages.*

*In the Hydropower Sustainability Assessment Protocol (HSAP), this topic is addressed in P-12 for the preparation stage and I-8 for the implementation stage. In the Hydropower Sustainability ESG Gap Analysis Tool (HESG), this topic is addressed in Section 9.*

This guideline addresses all project-related procurement including works, goods and services. The intent is that procurement processes are equitable, transparent and accountable; support the achievement of project timeline, quality and budgetary milestones; support developer and contractor environmental, social and ethical performance; and promote opportunities for local industries.

**Procurement** in this context means the purchase of goods or commodities by the project developer or operator, as well as contracting for services or goods. Hydropower projects rely upon a range of works, goods and services being provided to the project. These are usually in the form of contractors doing works, consultancies providing expert advice, materials, manufactured goods and equipment, and services.

Procurement is guided by selection criteria, for example to select the highest quality or lowest cost or a combination of these. Procurement may involve direct purchase from a known supplier for items under a certain value, and most commonly involves a bidding process for higher value items in which the bidders or sellers quote their prices. The bidding process begins when the procurer identifies the need for goods or services and starts to search the market for bidders. This may take place through publicising a tender. After identifying suppliers, a request for bids, proposals, quotes, and information can be made. Direct contact with bidders can also be made instead of advertising the above requests. After selecting the suitable bidders, a quality check may be undertaken to confirm the suitability of the goods or services in question. The next step is agreement on the terms, conditions, quality, and delivery schedules, followed by delivery and payment. All of these items are usually included in the bidding documents, which form the basis of the bidding process.

Procurement is a standalone topic in the preparation and implementation assessment tools because of the significant level of procurement that is required at these project stages. During the operation stage, procurement activity is lower and is therefore addressed as a component of the Governance topic (O-2). Procurement is strongly linked to the Integrated Project Management topic, where considerations relating to the overall project works programme, budget and scheduling are addressed.

## Assessment

*Assessment criterion - Preparation Stage: An assessment of major supply needs, supply sources, relevant legislation and guidelines, supply chain risks and corruption risks has been undertaken with no significant gaps.*

The most significant decision at the early stage of the project is the approach to be taken to major contracts, which is closely interrelated with management of financial risks (see the Financial Viability guideline). Approaches to the major contracts can vary widely, with different pros and cons and different outcomes regarding risk. Two widely differing examples are shown below, but there are many variations on these approaches to meet particular circumstances:

- **Unit price** – the owner manages all major construction contracts and pays a fixed sum for each completed unit of work based on estimated quantities of items and their unit price. Contracted costs will be lower than total project costs because costs to the owner are not reflected. Advantages are that the owner can easily verify that prices are not inflated and variations are relatively easily managed. Disadvantages are that this model requires a high degree of experience and capacity on the part of the owner, the owner carries a high level of administration and supervision, and the owner carries the major risks. One approach to reduce risks to the owner is to contract an **owner's engineer** to fill in resource and expertise gaps, provide administration and supervision services, and ultimately protect the owner's short- and long-term interests by ensuring all contractors are adhering to project specifications and advising the owner on any issues which arise.

- **EPC – an Engineering, Procurement and Construction (EPC)** contract involves a principal contractor implementing the project through the use of sub-contractors. The scope of services may cover from design right through to commissioning and handover to the owner depending on how it is set up. An EPC contract typically has project costs closer to the total project cost because a large part of the risk is transferred to the EPC contractor. Advantages for the owner include engagement with a single point of responsibility, working to a fixed price and completion date, and relying on performance guarantees to ensure delivery of required functionality. Potential disadvantages to the owner can include less involvement in the design process and quality control during project implementation, which may ultimately result in higher life cycle costs and reduced performance outcomes. Another potential disadvantage is that the EPC contractor may not have direct responsibilities for, nor take a long-term view, on environmental and social issues relating to the project.

Under any scenario, it is essential to itemise all procurement requirements for the project as this is necessary to estimate project costs and to inform procurement strategies. The feasibility studies and detailed design report should include identification of potential sources for major supply needs as this will influence accessibility, transport costs, financial planning in relation to taxes and duties, and logistical planning.

Major supply examples include:

- consultancies for design, economic, financial, technical, environmental and social studies;
- contractors for project construction works;
- materials for construction such as concrete, aggregate, and steel, as well as hydro-mechanical and electro-mechanical equipment for the project;
- equipment for processes relating to construction such as storage tanks, generators, and pumps; and
- services such as accommodation, food, driving, catering, cleaning, auditing, independent review, waste management, and medical for the site offices and labour camps.

Sources may be local or within the country, or from international locations. The assessment process should include investigations of sourcing options and related risks, and determinations on specifications to include in bidding documents.

Legislation and guidelines relevant to procurement for the project, for example with regards to labour laws or occupational health and safety, need to be thoroughly understood and built into the project's procurement procedures. Lenders may have requirements relating to aspects of the project they are funding, such as the use of international competitive bidding.

Supply chain risks should be thoroughly outlined and investigated for their likelihood and probability, magnitude and consequences, and mitigation measures. Supply chain risks may relate to, for example, inability to meet the contract provisions (e.g. with respect to cost, time, amounts, quality, specifications), corruption (e.g. bribes, facilitation payments, favouritism, shortcuts on specifications), transport impediments (e.g. floods, fire, civil unrest), and human rights (e.g. child labour, forced labour used by suppliers of suppliers). The viability of a particular supplier, and their quality assurance/quality control commitments and processes, are important elements to include in the assessment of potential supply sources. The assessment should include identification and evaluation of risk mitigation measures (such as inspections, insurances, independent evaluations) and monitoring programmes to identify emerging risks and assess the effectiveness of mitigation measures.

The assessment processes should include corruption risks as one of the supply chain risks. Corruption risks at the contracting and bid evaluation stage may include, for example: non-transparent pre-qualification; confusing tender documents; non-transparent or non-objective selection procedures; bid clarifications not shared with other bidders; award decisions not made public, or not justified; deception and collusion; unjustified agents' fees; and conflicts of interest for officials and consultants.

Provision of and support for creating opportunities for local employment and local capacity building may be a requirement for project development or may be a commitment

made by the developer. Local suppliers are those within geographic proximity of the project who can or have the potential to deliver the required good and services. The definition of 'local' will be context specific (e.g. those in the project affected area or local government district). Local capacity development refers to assistance that is provided to entities in the proximity of the project who have an identified need to develop a certain skill or competency or general upgrading of performance ability in order to meet or deliver a desired service. Enhancing local capacity may be a project benefit committed to by the developer. Assessment processes should include local capacity assessments and investigation of mechanisms by which such commitments could be fulfilled. This could include a local employment policy or statements of preference for local suppliers in contract documents, and support provided to local suppliers to enable them to participate in the tendering process. Assistance and training may also be provided to increase the capacity of local workers to comply with higher standards than they might be used to for issues such as safety. In some cases local employment may not be possible because of skills shortages; in such situations, the developer might establish training programmes to upskill local people to enhance local employment opportunities associated with the project. Packaging of some procurement needs into smaller units more accessible in scale to local businesses may be used to promote opportunities for local suppliers; however, this approach should not be used to avoid more stringent tendering requirements associated with larger procurement lots and it needs to be consistent with national, regional, and/or institutional policies and guidelines.

## Assessment

*Assessment criterion - Implementation Stage: Major supply needs, supply sources, relevant legislation and guidelines, supply chain risks and corruption risks have been identified through an assessment process; ongoing monitoring is being undertaken to monitor effectiveness of procurement plans and processes.*

Monitoring is an essential accompaniment to procurement during project implementation. Monitoring should be directed at:

- ensuring procurement processes are properly implemented and fully ethical (e.g. through independent auditing);

- processes to receive, review and respond to procurement-related grievances, and to identify any underlying issues so that corrective actions can be implemented;
- ensuring that contracts, materials, equipment, supplies and services procured meet required specifications and are on time and within budget; and
- identifying any emerging political or logistical issues that may affect the supply of goods and services, such as political unrest, road closures, strikes, materials shortages, or price changes.

Factory assessment tests can be an important assessment tool to ensure quality assurance/ quality control during the off-site manufacturing of major equipment. Monitoring through inspections before, during and after transport of major equipment are in the developer's interests.

## Management

*Management criterion - Preparation Stage: Procurement plans and processes have been developed for project implementation and operation with no significant gaps.*

*Management criterion - Implementation Stage: Measures are in place to guide procurement of project goods, works and services and address identified issues or risks, and to meet procurement related commitments.*

Procurement plans and processes should already have been developed during the preparation stage as this stage already involves contracting of services and provision of equipment (e.g. for investigations). Contracts need to be awarded during the project preparation stage for investigations, design, environmental and social impact assessments, and early site establishment works.

The development of procurements plans and processes for implementation and operation may not have taken place during the project preparation stage in cases where the project is sent to a bidding process at the end of the preparation stage. In such cases the plan for procurement could consist of a commitment to utilise the corporate entity's procurement plans and processes, which would then be required to meet the stated criteria.

Procurement plans should include procurement objectives and commitments or refer to these if they are in a policy document. The plan should include lists of works, goods and services required and the timing of these needs, and then specify how items will be bundled and the method and timing by which they will be procured (e.g. call for bids, quotes from preferred suppliers, direct purchase). Processes should be specified regarding approaches to various types of procurement to be used and under what circumstances each approach is appropriate (e.g. linked to a value threshold or the funding source, where a lender may have its own requirements). For major competitive bids, processes should specify the approach to pre-qualification screening, bidding, awarding of contracts, anti-corruption measures, and mechanisms to respond to bidder complaints. Procurement plans should include risk mitigation measures, such as inspections, insurances, and independent evaluations. Procurement plans and processes should also clearly allocate responsibilities, accountabilities, and monitoring and evaluation.

Pre-qualification screening is a means of shortlisting suitable suppliers based on specified criteria as an initial step in the procurement process. By way of example, screening could be for quality, reputation, and cost, and essentially involves evaluating a provider's prior performance in terms of meeting contractual obligations. Screening based on sustainability criteria might encompass additional criteria which could include, by way of example, social, environmental, ethics, human rights, health and safety performance, and preference and support to local suppliers where they meet other criteria. Screening to address anti-corruption might specify, for example, that companies tendering must have a code of conduct addressing anti-corruption and/or that they have never been prosecuted for unethical business dealings.

Procurement plans should clarify the processes to be followed to receive, review and respond to procurement-related grievances. These might involve, for example, a debriefing process with the company's procurement staff if requested by unsuccessful bidders. Independent audit processes might also be used to handle procurement-related grievances, and processes for escalation of grievances may be included in the relevant legislation.

Procurement plans should include anti-corruption measures. Examples of anti-corruption measures include: open bidding contracting processes to be above a low threshold; commitments by the contracting authority and its employees to an anti-corruption policy and/or project integrity pacts; mechanisms to report corruption and protect whistleblowers; and confidentiality limited to legally protected information.

## Conformance/Compliance

*Conformance/Compliance criterion – Preparation and Implementation Stages: Processes and objectives relating to procurement have been and are on track to be met with no major non-compliances or non-conformances, and any procurement related commitments have been or are on track to be met.*

Assessment processes and management measures relating to procurement need to be compliant with relevant government requirements. These may be expressed in licence or permit conditions or captured in legislation. Compliance requirements may relate to, for example, standards to be met, the frequency and type of monitoring to be performed, and reporting to be submitted by the owner to government. Meeting of design standards is of particular importance for procurement; quality control and independent review processes should be thorough and credible and include documentation to verify that all design standards are fully met (also note points relating to quality control in the Infrastructure Safety topic guideline).

Conformance refers to delivering what is in the plans and procedures. Following all processes and procedures consistently is a critical requirement to ensure equity and accountability.

Commitments may be expressed in regulatory requirements for addressing procurement, in relevant policy requirements of the developer, or in any relevant company statements made publicly or within management plans. Evidence of adherence to commitments could be provided through, for example, internal monitoring and reports, government inspections, or independent review.

The significance of not meeting a commitment is based on the magnitude and consequence of that omission and will be context specific. For example, breach of a lender requirement for international competitive bidding could be a major non-conformance; failure to demonstrate delivery of procurement commitment such as creation of opportunities for local suppliers could be a significant non-conformance; and a slight delay in delivery of a monitoring report could be a non-significant non-conformance.

## Outcomes

*Outcomes criterion - Preparation and Implementation Stages: Procurement of works, goods and services across major project components is equitable, efficient, transparent, accountable, ethical and timely, and contracts are progressing or have been concluded within budget or that changes on contracts are clearly justifiable.*

A range of documents relating to the procurement policies and practices of the developer should be readily accessible. Procurement information should be well-documented due to the commercial and legal implications of procurement activities. Policies and procedures that address the range of issues described in this guideline should be available. Other documentation that can demonstrate this criterion is met includes tender requirements/specifications; bidding documents; supplier screening criteria; evaluation of supplier performance; recommendation of the bid evaluation team; documentation in relation to conflicts of interest; bidder grievance log; record of compliance with relevant legislation and guidelines, including those of financing agencies; and monitoring and/or third-party review reports.

Procurement approaches should demonstrate a number of outcomes. Equity would be demonstrated through fair and open processes. Efficiency would be demonstrated by processes that are clear, consistent and able to be readily implemented, and meet timing and budget requirements. Transparency would be demonstrated by procurement processes that are easily accessible to and understood by suppliers and third parties (e.g. regulators, civil society), and outcomes where the rationale for choices made are readily provided. Accountability



would be demonstrated by ensuring those with responsibilities can be identified and can answer to how their actions align with business policies. Ethics would be demonstrated if processes to detect corrupt practices are sufficient, well-established and applied, shown to be effective, and show no unethical practices. Timeliness would be demonstrated if goods and services have been obtained within timeframes that supported meeting of project timelines and did not impinge on the project's critical path or cause management issues such as temporary storage shortages.

Project progress reports should show that projects are performing against time and budget targets. If contracts have not been concluded within budget, evidence should be provided to show that the changes on contracts are clearly justifiable and that variations have been handled with all the same principles as the original contract establishment. Evidence should be accessible to show that any changes to contracts and associated budgets have explicitly followed corporate or other relevant institutional procedures.

