

Collaborative Contracting

Delivering Aid In A Changing Environment

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1 Abstract

AusAID is facing a changing environment, including the need for:

1. More extensive integration of the Partner Government, other donors, NGO's etc. into the project delivery process.
2. The total management of all programs/projects in country;
3. Significant reductions in micromanagement.
4. Greater emphasis on a sector-wide approach rather than management of individual programs/projects.
5. A clear demonstration that programs/projects outcomes are being achieved.

These objectives are in part being addressed in the move towards a relationship style contracting approach. Several options are being examined and implemented: from changes to traditional contracts, through Partnering style contracts to Strategic Alliances. However, AusAID is not in the business of creating new relationship models and consequently will rely on adapting existing approaches to meet its strategic objectives.

The presentation will be very much a “work in progress”, which describes how the principles of relationship contracting are being tailored to meet the strategic needs of AusAID and the specific objectives of individual programs.

The challenge for AusAID is how best to integrate all parties into the arrangement, particularly to define what each party can contribute and what each has at stake if the program fails. The principal issue is the capability of some Partner Governments and their willingness to commit to the responsibilities of a relationship style contract.

The presentation will concentrate on the specific issues involved and the way in which the principles of relationship contracting may be able to address these issues.

2 Introduction

The changes that AusAID has made to its contracting approach has opened up many opportunities for a wider range of consultants/contractors to participate in the delivery of development aid. This is particularly relevant for companies with specialist Project Management skills. This paper and presentation will highlight some of those opportunities while concentrating on the growing emphasis on a range of relationship style contracts as AusAID moves towards Alliance Style Contracting.

AusAID has adopted the term “Collaborative Contracting” to embrace a number of approaches on the continuum of relationship contracting. The emphasis is to integrate the partner government agency into every aspect of the project as a means of strengthening the systems and operating procedures to maximise sustainability of the services and facilities delivered by the program or project. There is also a major objective to more closely involve the Development Contractor in establishing the parameters of the project and maintaining the relevance of those parameters over the life of the project .

3 Background

AusAID's corporate objective is:

"To advance Australia's national interest by assisting developing countries to reduce poverty and achieve sustainable development"

AusAID operates in a contracting environment in which it:

- Is the third largest procurement agency in the Commonwealth
- Delivers \$1.8 billion of development assistance, including \$1.4 billion in bi-lateral aid to more than 40 countries
- Awards approx 1,200 contracts each year, principally to Australian and New Zealand companies

For some time now AusAID has been responding to a changing environment in which it is delivering its development aid. Some of the factors that are driving that change are the need to:

- Integrate with partner government systems and procedures
- Involve more stakeholders
- Respond to changing priorities
- Share risk
- Maximise flexibility to change contribution/responsibility over time
- Relate remuneration to contribution and level of risk
- Relate rewards and penalties to performance
- Reduce micromanagement
- Reduce external monitoring

Many of these changes are reflected in the range and diversity of the contracting approaches which are now used to meet specific needs. (Refer to Figure 1). AusAID considers that a closer relationship and collaboration between all parties involved in the project delivery process will most effectively achieve these objectives.

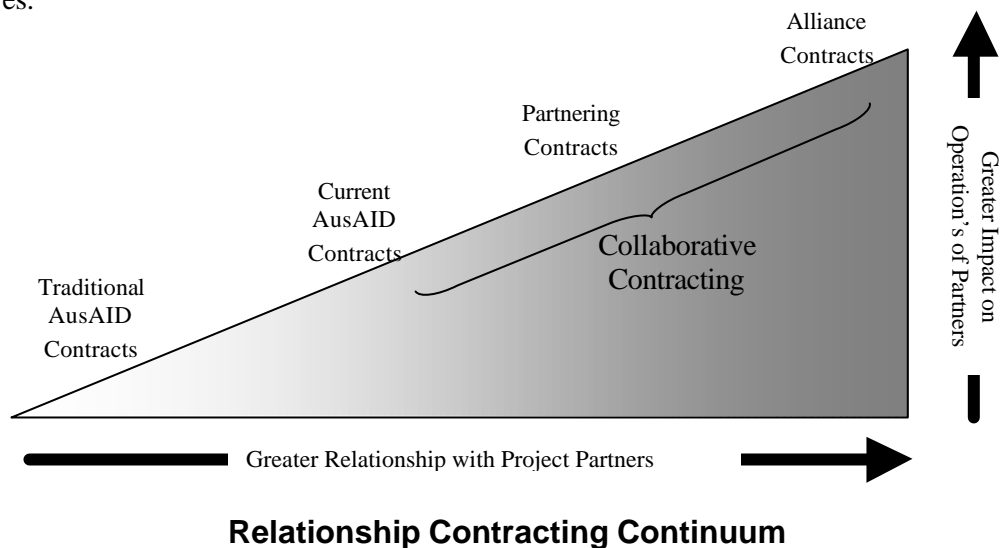


Figure 1

While this paper concentrates on the Collaborative Contracting and the scope to extend this approach towards the Alliancing end of the Relationship Contracting Continuum, it is appropriate to highlight some examples where changes to more traditional contracts have extended the opportunity for specialist Project Management Companies to participate in the delivery of development aid.

- **Hybrid Contracts:** These share financial risk by striking a balance between input and output payments. These contracts provide the opportunity for smaller companies to participate, which would otherwise find the financing costs of large value contracts overburdening. Generally payments are made on a 70:30 basis with regular monthly payments of 70% made for inputs and performance payments of the remaining 30% made on the achievement of milestones.

- **Managing Contractor:** These contracts allow specialist Project Management companies to manage the contribution of a wide range of technical specialist companies and individuals.
- **Program and Sector Wide Approach:** These contracts manage a whole sector (eg Health, Education, Law & Justice, etc) while integrating with the organisational arrangement and systems of the partner agency. Like the Managing Contractor approach they provide the opportunity for Project Management companies to lead a range of other specialists.
- **Outsourcing of Contract Management:** As part of a move to managing contracts solely within the country of development aid delivery, AusAID is outsourcing some contract management. A Project Management company will be engaged to manage a range of separate contracts that would otherwise be managed directly by AusAID. They will also be required to maintain a close working relationship with the partner government agency.

4 Collaborative Contracting

The remainder of this paper deals with AusAID's involvement in Program Partnering. It is acknowledged that Partnering is not new and that in many industries and sectors Alliancing has superseded Partnering. It is also acknowledged that Partnering has been used informally on development aid projects in the past. However, AusAID believes that a more formal relationship with the Partner Government and the Development contractor will more effectively embed the principles of good project management in contract management and will improve the working relationship between the parties. The approach also contemplates the involvement of other stakeholders, including Non-Government Organisations (NGOs).

AusAID proposes to achieve this through a formal and extensive Charter collaboratively developed and signed by all parties. Ultimately, the plan is to move to the full alliance style arrangement where all parties sign the contract. However, there are significant issues to be resolved before partner governments are willing and able to sign formal contracts involving AusAID and a Development Contractor.

5 Principles of Collaborative Contracting

The Principles of Collaborative Contracting that are most relevant to AusAID's operating environment are:

Best For Program

- All decisions made by all parties on the basis of what is the best program outcome

Respect for Partners' Distinct Attributes

- Partners respect and identify with each other's comparative advantage
- Partners value individual and collective contributions

Open and Honest Communication

- Communications will be open and consistent and based on a relationship of trust and honesty

Encouragement of Innovation

- Innovation will provide a key driver to the success of the program
- Learning and development is acknowledged as key to improving quality and program success

Regular Performance Review

- Review performance against KPIs
- Performance indicators and measurement protocols are agreed by Charter Board
- Performance expectations are recorded in Program Charter

Efficient Use of Scarce Resources

- Partners support maximization of use of program resources to achieve greatest impact

Equitable Balance of Risk and Reward

- Partners will equitably define risk
- Risk and rewards will be shared

Early Warning and Joint Problem Solving

- Partners give each other early warning of problems
- Partners jointly address problems

No Blame Culture

- Mutuality of purpose established
- Responsibilities of each partner clearly defined
- Clear understanding of individual and collective responsibility

6 Program Objectives

The above principles are adopted to achieve the Program Objectives, which are as follows:

- Integration with Partner Government Systems and Procedures will build and/or strengthen the management and decision-making capacity and processes. It will allow Partner Government systems to progressively take over responsibility for delivery of program.
- Involvement of other donors as a means of coordinating delivery of development aid, joint monitoring & evaluation and simplifying reporting.
- Respond to changing priorities
- Establish what each party contributes and their incentives to perform
- Appropriate allocation of risk
- Relate remuneration to contribution and level of risk
- Maximise flexibility to change contribution/responsibility of each party over time to reflect:
 - Growing level of competence of partner government organisations
 - Reduced management input by AusAID
 - Increase in policy/technical input by AusAID;
 - Changes in the level of financial contribution of other donors to the sector;
 - Reduced involvement of Development Contractor as competence of partner government organisations increase

7 Organisational Arrangements

AusAID plans to merge the Principles of Collaborative Contracting and the Program Objectives in a three-tiered structure (Refer to Figure 2),

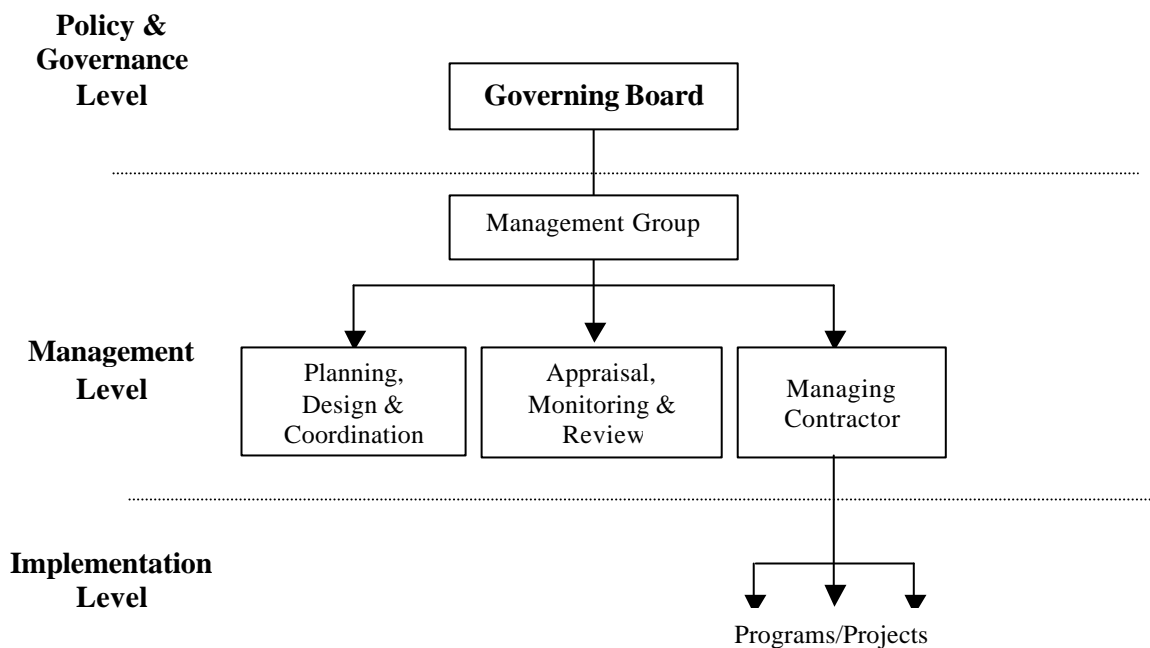


Figure 2

The objective of this arrangement is to allow a range of stakeholders to participate at the appropriate level. For example, the principal partner government agency can be involved at the Governance and Policy Level, while other interested agencies, NGOs, etc. can be involved at the Management Level. The same principle applies for contractors, with the Development Contractor involved at the Policy and Governance Level, and major sub-consultants and sub-contractors contributing at the Management Level.

Separating the Implementation Level provides the opportunity for a range of smaller organisations to remain involved the programs and provide greater contestability for many elements of the program/project.

7.1 Policy and Governance Level

The Governing Board is the most important part of the Policy and Governance Level and would comprise the parties to the Collaborative Contracting Agreement (normally AusAID, Partner Government Agency and Development Contractor). The Governing Board would establish and continually review the:

- Decision-making structure;
- Priority allocation of funds;
- Key Result Areas (KRAs);
- Key Performance Indicators (KPIs);
- Protocols for monitoring and evaluating KPIs;
- Management Level incentive frameworks;
- Extent of the Development Contractor's role and responsibilities;
- Processes for determining the types of contracts used at the Management and Implementation Levels; and
- Terms of withdrawal from the relationship.

All decisions require unanimous agreement of Board members, failing which the dispute resolution procedure will require each party to detail its position. These will be presented to a neutral third party who can only select the most appropriate option in the circumstances.

7.2 Management Level

The Management Group would be responsible to the Board for operational and coordination aspects of the program, including:

- Program Management;
- Integration with Partner Government systems and procedures;
- Performance payments against KPIs;
- Risk management; and
- Approval of contracting methodologies and delivery mechanisms at the Implementation Level.

Other elements at the Management Level would have a range of functions, including:

- Development of strategy, planning, design and coordination;
- Technical appraisal, sector monitoring and reviews
- Project management of the Implementation Level activities under a Managing Contractor model; and
- Compliance checking.

The contracting strategy at the Management Level will be approved by the Governing Board and operate under the aegis of the overarching Collaborative Contracting Agreement negotiated at the Policy and Governance Level.

The Development Contractor may be required to enter into a Collaborative Contracting Agreement with appropriate organisations to deliver the outcomes defined for the Management level. Alternatively, the Development Contractor may be engaged directly to provide some of the services at this level, including acting as a Managing Contractor for the delivery of services. There will, however, be some activities where it may not be appropriate for the Development Contractor to be involved, for example compliance checking.

7.3 Implementation Level

Competitively tendered, fixed price and other traditional contracting arrangements will generally be used at this level. However, there may be occasions where a Collaborative Contracting Agreement would be appropriate. For example, where a facility has been constructed and it is desirable for the contractor to have an ongoing role in operation and/or maintenance of the facility.

8 Program/Project Charter and Contract

The parties to the Governing Board will sign a Charter Agreement. A contract will also be signed between AusAID and the Development Contractor. The Charter will include a description of values, beliefs, philosophy and culture together with measurable objectives against which the success of the project can be evaluated – Attachment 1 “*Outline of Charter*”. The process of establishing the Charter is as important as the final document since it helps to build a cooperative approach to project management and more clearly identifies the expectations of all parties. The Charter will be built around:

1. The most appropriate way of sharing risk and returns;
2. Capitalising on the resources and expertise offered by each party;
3. Achieving clear and concise communications;
4. Rigorous pursuit of industry best practice;
5. Continuous improvement and quality assurance;
6. Mutual respect, trust and integrity;
7. Breaking down traditional organisational boundaries;
8. Minimising paperwork;
9. No litigation.

Once agreed, the Charter becomes the basis for project administration. However, it should not be regarded as a static document but rather a basis for continual dialogue between the parties to ensure that it continues to meet contemporary conditions over the life of the project. To allow this to function effectively, the Charter is designed as a comprehensive document containing many of the provisions that would otherwise be contained in the contract. Consequently, changes to the program/project can be made quickly by the unanimous agreement of the Governing Board without waiting for contract amendments to be drafted and approved.

The Charter will not alter the rights and/or obligations of the parties under the Contract, but will establish the management strategy and partnering philosophy. The contract is written to move in parallel with changes made by the Governing Board and periodically these changes will be formalised by a contract amendment.

9 Performance Payments

AusAID is keen to develop a clear linkage between performance and payment and considers that the elements and linkages in Figure 3 are critical to achieving this in a fair and equitable way.

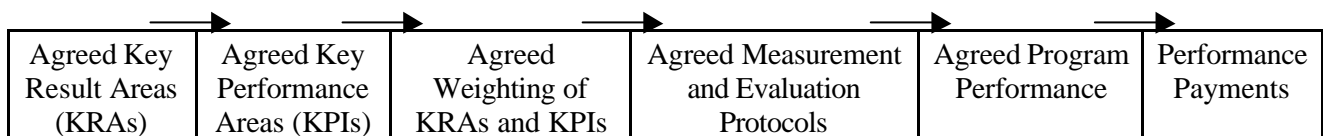


Figure 3

The objective is to meet the direct cost of the program/project while retaining a meaningful amount as an incentive to perform. The amount the Development Contractor has at risk may be as defined in Figure 4:

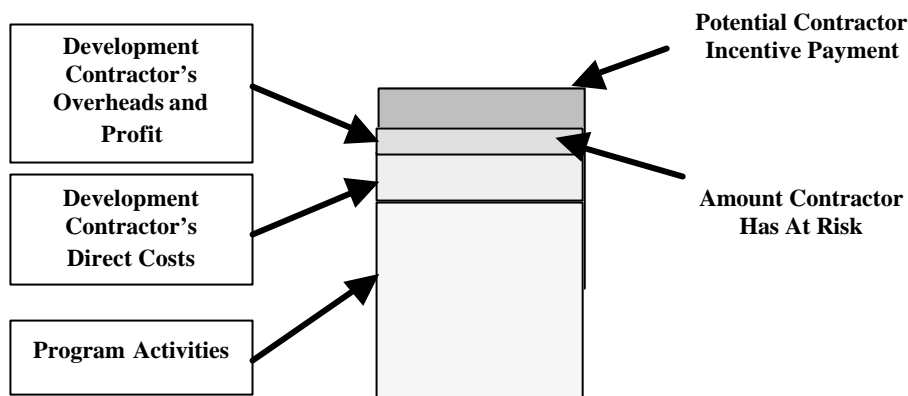
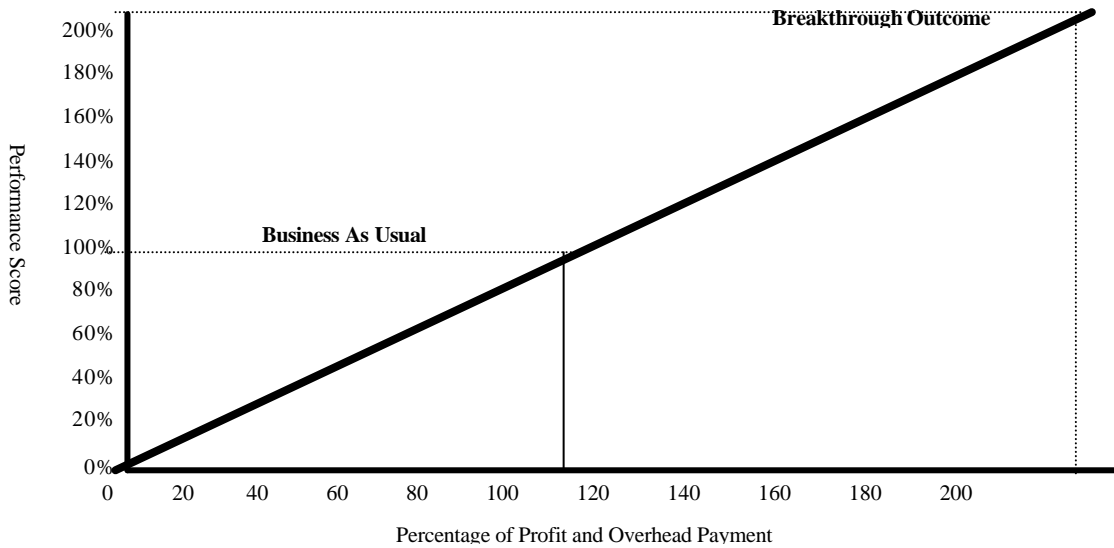


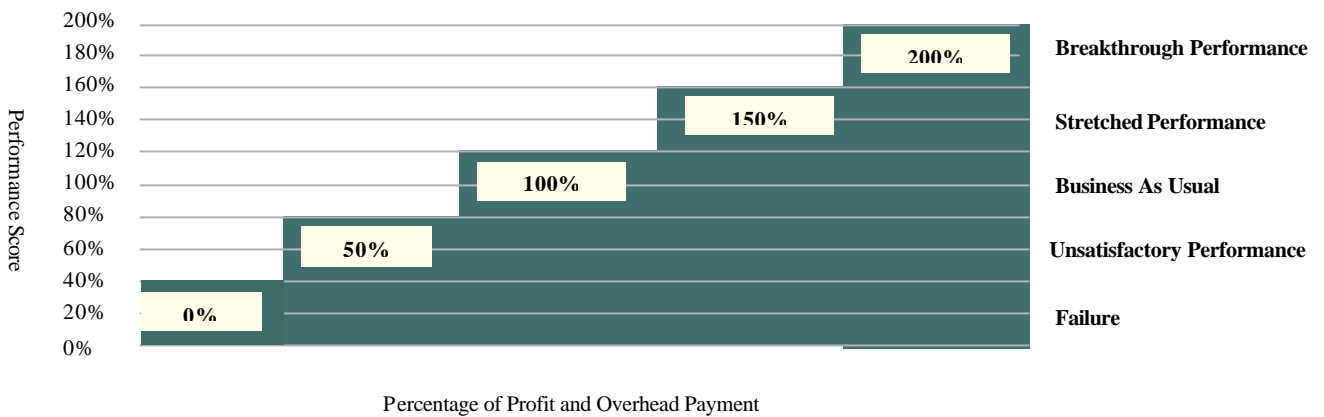
Figure 4

AusAID is considering two ways to apply the amount the Development Contractor has at risk, in the form of “Pain/Gain” share:

1. A “Sliding Scale” (Refer to Figure 5), where the performance score relates directly to the amount paid; and
2. A series of “Stepped Increments” (Refer to Figure 6), where the performance score relates to a band of payment



Sliding Scale - Figure 5



Stepped Increments - Figure 6

Public Sector organisations like AusAID are often reluctant to provide above Business As Usual (BAU) payments because these are regarded as a “bonus”. This is compounded by the concern of some Partner Governments, which regard the contractor’s payment as a reduction in the money available to their programs. Consequently, greater than BAU payments are regarded with great suspicion. However, the view taken is that incentive payments are justified where additional services and/or greater value of service as measured against BAU can be demonstrated. In these circumstances, the payment to the contractor can be regarded as their “share” of the additional benefits available to all parties of “stretched” or “breakthrough” performance.

In the partnering approach, incentive payments are an essential balance to the disincentives that are traditionally applied for a reduced service or a value less than BAU. The approach strives to reinforce the

fact that all parties are in a Win:Win or Lose: Lose arrangement. This requires a culture change for all parties, more used to the adversarial approach engendered by more traditional contracting.

10 Risk Matrix

The following are some of the key areas of risk as identified by AusAID

Issue	Comment
Lack of commitment from senior levels of the partner organisations	Lack of commitment may lead to insufficient or inappropriate resources being allocated to the program
Negative impact on other parts of the partner organisations	Elements of partnering may be incompatible with corporate culture and lead to undermining of partnering approach when things go wrong.
Approach may be too difficult or resource intensive for partner organisations to justify.	People at management and implementation level may not obtain necessary resources and support.
Charter Board cannot agree on critical issues	The approach relies on unanimous agreement by Charter Board on all issues, problems and the resolution of disputes.
Performance payments appear to produce supernormal profits	Payments to the contractor for profit and contribution to non-program Head Office costs must always demonstrate value for money
Continuity of involvement of representative of all organisations at all levels	Trust and respect for other program partners is developed over time. Important to obtain the benefits of the trust and respect developed
Trust and respect are not developed	Difficult to see how the partnering arrangement can continue to operate.
Lack of understanding and acceptance of partnering approach	Insufficient training and explanation may prevent adequate understanding and commitment leading to failure to adopt partnering principles.
Lack of continuity/compatibility between charter and contract	Need for charter and contract to be compatible and to remain compatible as the charter is developed by unanimous agreement of the Charter Board.
Misalignment develops between the partner's objectives, motivators, desired outcomes, etc.	The partnership approach relies on maintaining a synergy between the objectives, motivators, desired outcomes, etc of all partners.
Lack of fulfilment of partnering expectations	Partnering promises many advantages such as flexibility, improved outcomes, cost effectiveness, more appropriate allocation of resources, etc. - these must be realised to maintain commitment to the approach
Approach is not responsive to external factors	Partnering cannot control external factors, (changes caused by political decisions, funding availability, etc) but must be more responsive than the more traditional program delivery mechanisms

11 Conclusion

The fundamental question for AusAID is how does this process differ from its current operations. In essence this comes down to the greater level of involvement of the Partner Government, Development Contractor and other stakeholders in the policy development, governance and implementation of the program. The approach also embeds in the attitudes and principles of good project management into the procedures and operations of the program/project.

The question of whether this is worth the effort can only be effectively answered in the degree to which the Strategic Objective are addressed and satisfied. There is every indication at this stage that these will be effectively and appropriately addressed and that the approach is worth pursuing.

Outline of the Charter

The Program/Project Charter will establish the underlying philosophy that will guide the management and implementation of the project. The Charter will place particular emphasis on working together to establish goals and objectives in the following areas.

Key Result Areas (KRAs) and Key Performance Indicators (KPIs) - The Charter Partners will jointly develop KRAs and KPIs to focus on aspects of the program/project that are of paramount importance and offer the best opportunities for satisfying the priorities established for the program/project. They may be modified, new indicators introduced or indicators removed where all parties agree that this is a more relevant representation of the goals and contemporary objectives of the project.

Quality Assurance – All Charter Partners have a responsibility to assist the Contractor to achieve industry best practice. The partners also have a responsibility to facilitate continuous improvement in the standard of output. The Charter Partners will agree on the standard expected in the circumstances in which the project is being delivered. Wherever possible the standard will be quantifiable and specified with reference to established standards. However, where this is not possible or practical the standards should be specified as appropriate qualitative measures.

Measurement Protocols - The Charter Partners will agree on assessment mechanisms and protocols to measure performance against the agreed standards and expectations. Wherever possible these should be refined to minimise the reporting and evaluation process, consistent with:

- Accountability for the expenditure and efficient management of resources (including time);
- Accountability for results and outcomes.

The use of external evaluation processes and/or internal quality assurance certification processes should be reviewed to ensure that:

- Assessments are impartial; and
- Lead to simple certification of payments;
- Advice is integrated into the Contractors QA systems to rectify any shortfall in standards.

Cost Management – The purpose of the cost management process is to achieve the goals and objectives of the project for the contracted cost. All Charter Partners have a responsibility to demonstrate value for money in all aspects of the project delivery. However, the Partnering Approach requires all parties to help ensuring that the Contractor achieves the financial outcomes expected in the amount tendered. Certification by the Contractor (if necessary by Statutory Declaration) is an effective way to minimise financial reporting while still maintaining accountability for the proper use of funds. This may involve periodic external auditing to provide AusAID with the necessary financial and probity assurances. The important test for all Charter Partners remains value for money and cost management systems should clearly demonstrate whether this is being achieved.

Risk Management - The Charter Partners will focus on the contribution and responsibilities of all parties required to achieve the program objectives. The objective is to ensure that each party bears the risk it is best able to manage. Clear milestones and clear performance indicators linked to payments will lessen the risk of unsatisfactory work and lack of value for money. Management of risk means periodic review and mutual agreement to revise the risk matrix. The Charter Partners must ensure that the risk management strategies are used to ensure that the project's goals and objectives are achieved.

Communications Matrix – The Charter Partners should be clear on the issues that will be dealt with at various levels within their respective organisations and the personnel that are responsible for communicating with each other. Adequate authority should be provided to allow decisions to be made at the appropriate level and the communication arrangements must alert senior management to situations where decisions cannot be taken at the operating level or are not being taken within agreed timeframes.

Problem Solving - The Partnering Approach requires the parties to develop an issues resolution process. The aim is to have issues resolved at the lowest possible level and at the earliest possible opportunity. The system also alerts higher levels of management at an early stage to possible problems. Issues are automatically elevated to a higher level if not resolved within a specified (short) period of time. Such a structure is intended to break down the adversarial positions that can arise in traditional contracts.