

Project Administration Instructions

PAI 3.06
Revised February 2007
Page 1 of 4

DOMESTIC PREFERENCE SCHEME

A. Introduction

1. ADB's domestic preference scheme may be only applied in evaluating bids under international competitive bidding (ICB). Procurement through other methods such as Shopping, national competitive bidding, and limited international bidding are ineligible for the domestic preference scheme. The scheme grants a margin of preference for domestically manufactured goods to be procured and domestic contractors to be engaged under ADB-financed projects.

B. Domestic Preference for Goods

2. All borrowers may request preference for the procurement of domestically produced goods. Related incidental services are not eligible for the preference.

3. The scheme provides that

- domestically manufactured goods are eligible for preference compared with imported goods only if the proportion of domestic value added is equal to 30 percent or more of the ex-factory bid price;
- the 30 percent domestic value added must be applied to the total ex-factory bid price of goods and not just to one item in a list;
- domestic preference cannot be applied to goods offered in a schedule if one item has more than 30 percent domestic value added but the total domestic value added does not result in the required minimum 30 percent of the total price of the schedule; and
- ADB will not object if the borrower stipulates a minimum that is more than 30 percent domestic value added.

4. Where there is any doubt about eligibility for preference for any domestic goods for which bids have been invited, the borrower (or its consultant) assesses the proportion of domestic value added locally to see if it meets the required minimum.

5. Domestic value added is generally considered as the value of labor added in producing goods. If calculating domestic value added is difficult and time consuming, a rule based on the direct import content of the goods can be used as a proxy for these calculations. If the direct import content under cost, insurance, and freight (CIF) is less than 50 percent of the quoted ex-factory price, the goods are eligible for the preference.

6. Before agreeing to include domestic preference in the financing agreement or bidding documents, ADB must be satisfied that the borrowing country has the manufacturing capacity and experience for adding the minimum value required to goods intended to benefit from the preference. If at the time of signing the financing agreement, inadequate information is known about the goods to be procured (for example, in a sector project), provision of preference may be included in the financing agreement (the financing agreement would be written as if manufacturing capacity exists for some of the goods to be procured). In such cases, the capacity to produce the required goods domestically would be assessed

when bidding documents are prepared for the goods to be procured.

7. Bidders are required to certify, as part of their bid, the existence of the necessary manufacturing capacity where local value is to be added.

8. Eligibility for preference for goods is determined by referring to the source of domestic goods and not to the nationality of the bidder. Therefore preference is given not to the bidder but to the goods where the domestic value added is 30 percent or more. The nationality of the bidder or supplier is irrelevant. A foreign bidder submitting a bid for goods with domestic value added of 30 percent or more in the borrowing country would be entitled to the scheme provided

- the bidder quotes the bid price in local currency or in a mix of currencies as specified in the bidding documents, which will include customs and import duties in the borrowing country for imported components and raw materials; and
- the bidder indicates separately the percentage or amount of the quoted bid price that is to be paid in local and foreign currency to reflect costs of imported components and raw materials included in the bid.

9. Such a foreign bidder, having effected the above, is not allowed to take advantage of the evaluation of its bid under CIF (exclusive of taxes and duties in the borrowing country for the imported components and raw materials included in the bid). The foreign bidder would be treated as a domestic bidder who may claim the preference.

10. The margin of preference is limited to 15 percent of the CIF price before tariffs on imported goods.

C. Domestic Preference for Turnkey Contracts, and Contracts for Goods and Related Services Involving Multiple Items

11. A margin of preference may be applied to domestically manufactured goods in single-responsibility turnkey (including design-build) contracts, and large and complex contracts for goods and related services:

- when procured through ICB,
- with discrete items of goods and supplies grouped in one contract package, and
- where the CIF or ex-factory cost of goods and supplies for permanent works is estimated prior to bidding to equal or exceed 60 percent of such works.

12. The following provisions apply to turnkey and eligible large and complex contracts for goods and related services:

- Preference margins will not apply to the whole package, but only to locally manufactured goods within the package. Goods offered from abroad will be quoted under CIF, and goods offered locally will be quoted ex-factory (free of sales and similar taxes).
- Components, such as design, works, installation, and supervision, will be quoted separately, and will not be subject to preference.

- Bids are not to be classified into categories I, II, or III.¹ When comparing bids, only the CIF price in each bid of the goods offered from outside the borrower's country will be increased by 15 percent.
- The scheme is not applicable for part of a schedule, which includes several items, if the bidding documents state that the evaluation will be on a schedule basis and not on an item basis.
- Preference will not be applied to any related services or works included in the package.
- Bidding documents must specify how the preference is to be applied, and bidders must not be permitted to modify the mix of local and foreign equipment after bid opening.

D. Domestic Preference for Works Contractors

13. Preference will only be extended to domestic contractors for civil works in countries with an annual per capita GNI that is less than a specified limit. The limit is set each year in consultation with the World Bank. The current limit and list of countries where preference may be extended to domestic contractors is given in Appendix 1.

14. Preference may be applied to works including construction, land clearing and leveling, land development, field drainage, well drilling, site clearing for urban projects, installation of water supply mains, erection of electricity lines, aerial photography, mapping, or crop spraying. For contracts for goods and related services, if the CIF or ex-factory cost of equipment to be used in the permanent works is less than 60 percent of the total value of works, then such contracts will be classified as civil works. The scheme does not apply to consulting services contracts.

15. ADB determines which contractors are genuine domestic contractors and therefore eligible for preference. ADB ensures that specific criteria for eligibility are agreed upon and included in the procurement plan and/or bidding documents. ADB will not object if the borrower wishes to grant preference to state-owned construction corporations or firms, provided that they are eligible to bid. The Central Operations Services Office advises on any problems arising when applying the scheme. The Office of the General Counsel advises on any specific legal issues arising when applying the scheme. If necessary the procurement committee makes the final decision.

16. Bidders are required to submit evidence of the eligibility of individual firms and joint ventures for preference as part of the bid. Preference applies to prime contractors and to nominated subcontractors only (nominated subcontractors are subcontractors of the prime contractor who are selected by the employer through a separate bidding process). Bidding documents and contracts will specify limitations on subcontracting by domestic contractors to foreign contractors that will safeguard the essential intent of the preference scheme. For example, a domestic contractor qualifying for preference under majority local ownership will not subcontract more than 50 percent of the works to a foreign contractor.

¹ PAI 3.06, Appendixes 2, 3, and 4.

E. Implementing the Preference Scheme

17. Domestic preference for goods, turnkey contracts, and works will be applied only if
- requested by the borrower, and
 - provision is made in the financing agreement (or through a separate exchange of letters), and
 - bidding documents specify how the preference will be applied when comparing bids.
18. Provision for implementing the scheme is included in the procurement plan. If provision is not included in the procurement plan and the borrowing country subsequently wishes to adopt the scheme, arrangements can be specified in an exchange of letters or subsequent updates to the procurement plan. Even after provision for preference is included either in the procurement plan or by an exchange of letters, its application to individual contracts is still at the option of the executing agency or borrower. The procurement plan states the basis for comparison of bids for goods, turnkey contracts, or works, and the sequence for comparing them, when the scheme is applied.
19. Implementing the scheme requires that provisions are included in the prequalification and bidding documents on the method of comparing bids and related matters.
- Appendix 2 contains model provisions for prequalification documents.
 - Appendix 3 contains model provisions for bidding documents for the procurement of goods only.
 - Appendix 4 contains model provisions for bidding documents for turnkey contracts, and large and complex contracts for goods and related services where the CIF or ex-factory cost of equipment or goods to be used in the permanent works is equal to or exceeds 60 percent of the total contract value.
 - Appendix 5 contains model provisions for bidding documents for civil works, turnkey contracts, and contracts for goods and related services where the CIF or ex-factory cost of equipment to be used in the permanent works is less than 60 percent of the total contract value.

Comparison of prequalification applicants and bids must follow the provisions outlined in Appendixes 2–5.

20. For works, ADB ensures that the borrower's decision does not adversely affect competition and that all firms qualifying as domestic contractors meet ADB's and the borrower's criteria.

References

1. R11-06: *Revising the Procurement Guidelines*, 6 February.
2. R108-91: *Review of Domestic Preference Scheme*, 8 August
3. R27-86: *Review of Domestic Procurement Policies*, 17 June.

Countries Eligible for Domestic Preference

Afghanistan
Bangladesh
Bhutan
Cambodia
India
Kyrgyz Republic
Lao People's Democratic Republic
Mongolia
Myanmar
Nepal
Pakistan
Papua New Guinea
Solomon Islands
Tajikistan
Timor-Leste
Uzbekistan
Viet Nam

Based on per capita annual GNI limit of \$875 as of January 2007.

Model Provisions to be Included in Prequalification Documents
(Preference for Domestic Contractors)

1. A 7.5 percent margin of preference is given to eligible domestic contractors when comparing bids of prequalified domestic and foreign contractors. Domestic contractors and joint venture firms must meet the following minimum criteria for eligibility under the domestic preference scheme:

- (i) Domestic contractors
 - are incorporated or established under the laws of the borrower's country, and
 - have majority ownership by nationals of the borrower's country, and
 - will not subcontract more than 50 percent of the total value of the work to foreign contractors.

- (ii) A joint venture between a domestic contractor and its foreign partner is eligible for preference only if
 - the domestic partner(s) are individually eligible for the preference according to the criteria stated in (i);
 - the domestic partner(s) would not qualify for the work on technical or financial grounds without the foreign participation; and
 - the domestic partners, under the arrangements proposed, carry out at least 50 percent of the value of work.

- (iii) If the contract is awarded to a contractor who receives the preference, the contractor should not subcontract more than 50 percent of the value of the work to any foreign contractor.

Model Provisions to be Included in Bidding Documents
(Preference for Domestically Manufactured Goods)

1. In comparing bids offering domestic and imported goods, goods manufactured in the territory of the borrower are granted a margin of preference in accordance with the following provisions. This is provided that the bidder has established that the domestic value added is equal to 30 percent or more of the ex-factory bid price of such goods. The 30 percent domestic value-added applies to the total ex-factory bid price of all of the goods and not only to one item in a package.

- (i) When applying domestic preference, all responsive bids are first classified into one of the following three categories. The purchaser reviews each bid to confirm or modify how the bidder categorized itself when preparing the bid.
 - **Category I:** for bids offering goods manufactured in the borrower's territory that meet the minimum domestic value-added requirement,
 - **Category II:** for bids offering other goods manufactured in the borrower's territory, and
 - **Category III:** for bids offering imported goods.
- (ii) The lowest evaluated bid in each category is determined by comparing all evaluated bids in each category. This comparison excludes customs duties, import taxes, and other taxes levied in connection with the importation, sale, or delivery of the goods.
- (iii) The lowest evaluated bids in each category are compared with each other and if, as a result of this comparison, a bid from categories I or II is found to be the lowest, that bid is selected for the award of contract.
- (iv) If, however, as a result of the comparison under (iii), the lowest bid is found to be from category III, it is then further compared with the lowest evaluated bid from category I. For this comparison only, an upward adjustment is made to the lowest evaluated bid price of category III by adding 15 percent of the CIF bid price of such goods

If, after such further comparison, the category I bid is determined to be the lowest, it is selected for the award of contract; if not, the lowest evaluated bid from category III is selected for the award.

2. Bidders applying for the preference provide the necessary evidence with their bids to establish the eligibility of the bids for the preference, including the minimum domestic value added.

Model Provisions to be Included in Bidding Documents

(Domestic preference for turnkey contracts, and large and complex contracts for goods and related services where the CIF or ex-factory cost of equipment or goods to be used in the permanent works is equal to or exceeds 60 percent of the total contract value)

1. A margin of preference will be applied to the domestically manufactured goods in accordance with the following provisions. Bidders applying for the preference will provide evidence with their bids to establish the eligibility of the bids for the preference. The provisions include the following:

- The margin of preference is not applied to the whole package but only to the domestically manufactured goods within the package.
- Goods offered from outside the territory of the borrower are quoted CIF and goods offered domestically are quoted ex-factory or ex-works (free of sales and similar taxes).
- All other cost components such as design, installation, supervision, works, and commissioning are quoted separately.
- When comparing bids (which should not be classified into categories I, II, or III as is done with the domestic preference for goods), only the CIF price in each bid of the goods offered from outside the territory of the borrower is increased by the preference margin (15 percent).
- No margin of preference is applied to any other cost components or works included in the package.
- Bidders are not permitted or required to modify the mix of domestic and foreign goods after bid opening.

Model Provisions to be Included in Bidding Documents

(Preference for civil works contracts, turnkey contracts, and contracts for goods and related services where the CIF or ex-factory cost of equipment to be used in permanent work is less than 60 percent of the total contract value)

1. When comparing domestic bids with foreign bids, domestic contractors (as defined in para. 2) are granted a margin of preference in accordance with the following provisions:

- (i) For application of domestic preference, all bids are first classified into the following two categories:

Category I: for bids offered by domestic contractors and joint ventures eligible for the preference in accordance with the applicable criteria in para. 2; and

Category II: for bids offered by other contractors.

- (ii) The lowest evaluated bid in each category is determined by comparing all evaluated bids in each category.
- (iii) The lowest evaluated bids in each category are compared with each other and if, as a result of this comparison, a bid from category I is found to be the lowest, it is selected for the award of contract.
- (iv) If, however, as a result of the comparison under (iii), the lowest bid is found to be from category II, it is then compared with the lowest evaluated bid from category I. For this additional comparison only, an upward adjustment is made to the lowest evaluated bid price of category II by adding an amount equal to 7.5 percent of the bid price. If, after such comparison, the category I bid is determined to be the lowest, it is selected for the award of contract; if not, the lowest evaluated bid from category II is selected.

2. Domestic contractors and joint venture firms must meet the following minimum criteria for eligibility under the domestic preference scheme.

- (i) Domestic contractors
- are incorporated or established under the laws of the borrower's country,
 - have majority ownership by nationals of the borrower, and
 - will not subcontract more than 50 percent of the total value of the work to foreign contractors.
- (ii) A joint venture between a domestic contractor and its foreign partner is eligible for the preference only if

- the domestic partner(s) is individually eligible for the preference according to the criteria stated in 2(i);
- the domestic partner(s) would not qualify for the work on technical or financial grounds without the foreign participation; and
- the domestic partner(s), under the arrangements proposed, carry out at least 50 percent of the value of the work.

Contractors applying for the preference provide information with their bids, including details of ownership. This is to determine if, under the applicable criteria, a particular firm or group of firms qualifies for the preference.