

COMMISSION ON WARTIME CONTRACTING

TESTIMONY OF PAUL HINKS, CEO, SYMBION POWER LLC

JULY 26, 2010

My name is Paul Hinks. I am the Chief Executive Officer of Symbion Power LLC, a U.S. power engineering and construction firm that was formed in 2005 specifically to undertake electrical reconstruction work in Iraq and Afghanistan. I am grateful for your invitation to appear before this distinguished Commission, and to assist you and your staff with its important work on Wartime Contracting issues. Your hearing today on the subject of Subcontractors is aptly titled, "Subcontracting: Who's Minding the Store?" I am here to share with you my experience and views as both a Prime Contractor and as a Subcontractor, having managed two different companies in Iraq and Afghanistan since 2003. Because of this, I am presenting this testimony in the first person. Before giving you my views, I will provide you with a brief background of my experience.

I have spent my entire working life as a contractor. Initially I studied and trained in the United Kingdom for a state power company. In the early eighties I lived and worked in Africa where I was responsible for the construction of a large array of projects that included power plants, transmission and distribution lines and substations. For the past 29 years I have carried out work in developing countries, some of which have been conflict zones, although many are now stable and secure. These include Zimbabwe, Mozambique, Angola and Uganda. There was a time 20 years or so ago when building a project in Mozambique was akin to working in Iraq in the period after 2003. I was in Uganda during the civil conflict there, hiding under a bed as gun battles raged outside the house. I lived in East Africa for 10 years, during which I traveled to work in other African countries in the region. In those days the African National Congress (ANC) of South Africa built and maintained large camps in Tanzania and Zambia for thousands of their exiled supporters. I installed power systems to one of those camps. Today the ANC is the government of South Africa.

In 2003 I went to work in Iraq for the world's largest transmission line company, KEC International. I worked there full time for almost one year. During that time I was responsible for the construction of five major 400kV and 132kV transmission line projects. In all cases we were a Subcontractor to some of the major U.S. Prime Contractors. In almost all cases we did everything, from the design and engineering to procurement and installation. We were turnkey Subcontractors with very minimal management and oversight by the Prime Contractors.

I managed the following five projects, which were successfully completed in less than one year, each of which was a Firm-Fixed-Price Lump Sum subcontract:

1. Hartha to Al Amara 400kV transmission line, 130kms
2. Khor Zubyara to Nassiriyah 400kV transmission line, 120kms
3. Burzagan to Al Amarah 132kV transmission line, 60 kms
4. Erbil to Qaraqoosh 132kV transmission line, 80kms
5. Baiji to Baghdad 400kV – completion of a section of stringing work

The model that each Prime Contractor employed was to have us, the Subcontractor, accept the contract execution risk and to deliver each project to them. The Prime Contractor would bill the government for our costs and whatever margins and fees they

had negotiated with the government themselves. This is a relatively low risk endeavor for the Prime Contractors because the subcontractor is bound to his lump sum, save for any agreed changes, and all the Prime Contractor's costs are paid no matter how much those costs are.

This Cost-Plus model of contracting was alien to me before my experience in Iraq. All my life as a contractor I have worked under pressure to meet tight budgets that are based upon competitive estimates. When we saved money through efficiencies and good performance, we made good profits. When we made mistakes, we paid for them dearly and our profits were eroded. The Cost-Plus model that the U.S. government uses means that if the contractor makes mistakes, it does not lose anything as a consequence, rewarding poor performance at the government's expense. It also means that as the overall level of expenditure escalates, the contractor earns more money, because the margins and fees are based on percentages. Thus, the dollar amounts that the percentage represents become larger as the costs increase. There is no longer a natural incentive to save money because there is no penalty for not doing so. In fact there is a financial benefit to over-spending. As a consequence, overall project costs can soar out of control. It is like giving your children whatever money they ask for. Like your children, a Cost-Plus contractor will lose any appreciation for the value of money.

In 2005, a number of the large Prime Contractors began reducing the scope of their operations in Iraq because they felt that it was becoming impossible to execute contracts due to the deteriorating security conditions there. Yet there were many important electricity projects that had not been started. At this time, the U.S. government decided to try a new model of contracting, and revert to a more traditional Firm-Fixed-Price Lump Sum model by opening the work up to international competition. Since all the work I had done in Iraq had been Firm-Fixed-Price, and because I felt that I could create a contracting model to get the work done in very dangerous areas, I decided to form Symbion Power LLC. The fundamental challenges that these Firm-Fixed-Price projects presented were a) how to control costs, especially for security, and b) how to manage and supervise work in areas where it was impossible to utilize foreign expatriate workers due to the extreme risks that existed. In some places such as Al Anbar, we could not even get workers from Baghdad to go into the area.

I addressed the security challenges by asking a reputable security contractor, Hart Security Ltd., to be a founding investor and stockholder of Symbion, figuring that this would incentivize our security provider to greater efficiencies in providing security for our workers and equipment. At that time, security costs for construction projects in Iraq and Afghanistan had spiraled out of control, and I considered this model a means of controlling of them without jeopardizing safety. It worked, and for the first time I began to hear security personnel talking about how to save money as the project continued. In short, the security provider "bought in" to the financial performance of the project because it would earn profits if Symbion achieved its targets.

To deal with the remaining element of the security challenge – getting the work done in areas of extreme risk and conflict -- I decided that the only way was to collaborate with local, indigenous people who had little or no previous experience in electric transmission and distribution projects. To that end, I found local and Turkish companies, made them our joint venture partners and/or our subcontractors, and then trained them to do the work in areas that were safe for expatriates to undertake training. Some firms had previous experience, but in many cases we worked with tribal leaders who managed the work in their areas of influence. In some of the most volatile areas of the country, the

local Sheiks became Symbion's partners.

Using this business model, Symbion undertook nine Prime Contracts for the Department of Defense in Iraq. All but two of these projects are virtually complete today, with the final ones due for completion within a few months. We have completed our contractual obligations for the lump sum prices for which we bid the jobs, and have only been compensated for additional costs that are linked to additional scope of work. As a result, the government got the work done for prices close to what it expected them to be at the outset of the project. Those nine projects were:

1. Baiji to Haditha to Al Qaim 400kV transmission line, 300kms
2. Dohuk to Agra 132kV transmission line, 100kms in Kurdistan
3. Repair of 400kV transmission feeders into Baghdad
4. Hilla to Hashemiya to Shamiya 132kV transmission line
5. Five substations in Basra region
6. Fallujah substation
7. Ramadi substation
8. Two substations in Sadr City (Farabi and Jamila)
9. Two substations at Agra & Dohuk in Kurdistan

This work represented a value of \$260 million.

In 2007, I expanded Symbion's operations to Afghanistan, where most of the U.S. government's investment in electrification is being made through a \$1.4 billion dollar Cost-Plus Prime Contract to a joint venture of two U.S. firms, the Louis Berger Group / Black & Veatch Joint Venture (the LBG/B&V JV). My experience in Afghanistan was very different from what I experienced as either a Subcontractor or a Prime Contractor for DOD projects in Iraq. In Afghanistan, Symbion worked on three Subcontracts for the LBG/B&V JV:

1. 100MW Kabul Power Plant Balance of Plant (BOP) contract
2. 132kV switchyard for the Kabul Power Plant
3. Air survey of lines and roads in Afghanistan

This represented approximately \$80 million of subcontracting work for the LBG/B&V JV.

Working as a subcontractor to U.S. Prime Contractors varies considerably from company to company. My experience has been that the source selection process leaves a lot to be desired. More often than not, it does not have the integrity of a government bid evaluation. On the nine contracts Symbion bid for in Iraq, we found the process and the procedures to be professional, systematic and strictly consistent with government bidding requirements. Further, all those contracts were advertized on the government website Fedbizz Ops. In contrast, none of the RFPs for Subcontracts we worked on in Afghanistan were ever posted on that site, or in any other widely disseminated publication. As a consequence, many international companies did not even know about the opportunity to bid on work in Afghanistan. Posting on the Prime Contractor's own website, or on project websites, does not encourage or invite maximum competition in bidding. For example, it would be best to see postings in publications such as the United Nations Development Business website (www.devbusiness.com/), which is constantly tracked by most international contractors.

Payment practices also differ from Prime Contractor to Prime Contractor. Some are very

efficient and others are incredibly slow. However, they all rely on “pay when paid” clauses, so the Subcontractor is paid only after Prime Contractor receives its money. More often than not, this causes long delays in payment that are unbearable to small, often local subcontractors. It makes a mockery of the process of agreed-upon payment terms, because a “pay when paid” clause alone can prevent a Subcontractor from being paid on a reasonable and timely basis.

In the case of Symbion, we apply management and control systems and employee recruitment practices to assure that we meet the standards the U.S. government expects. We are diligent about training our employees about ethics and legal requirements. In the event that we find any issues, we will investigate and if necessary we will self-report our findings.

My experience in dealing with non-U.S. subcontractors is that many either do not understand or do not take seriously the FAR and/or other ethical and legal requirements. Even some large European companies I have dealt with do not take the FAR seriously, and do not comprehend its relevance. Some Prime Contractors use other forms of international contracts, such as FIDIC, but they still “flow down” FAR conditions, and this causes confusion. There are of course many exceptions but the vast majority of smaller subcontractors simply do not understand why they have to comply with FAR provisions.

Unfortunately, the Kabul Power Plant BOP Subcontract is the subject of a contractual dispute between Symbion and the LBG/B&V JV that is being arbitrated in a proceeding before the International Court of Arbitration of the International Chamber of Commerce (the “ICC Arbitration”).† As we have explained to the staff, the ICC Arbitration Panel has issued a confidentiality order that bars the parties and their lawyers from discussing matters that are the subject of the arbitration.† I opposed these restrictions, because I believe the details of this dispute present a valuable case study about subcontracting in a contingency environment.† However, the Arbitration Panel has ruled, and I must abide by it.†

The parties to the dispute are very fortunate to have an esteemed Arbitration Panel, which I hope will allow all the details to be made public once they have completed their work.† Indeed, this is a public works project.† I would be happy to return to testify to you about these issues if, as I hope, the findings of the ICC Arbitration Panel can ultimately be made public, and I would welcome an open debate about this with the LBG&BV Joint Venture at that time.† This payment dispute is complex in nature, so the appropriate time for this to occur is after the Arbitration Panel has studied it and adjudicated.

Based upon my experiences I have the following recommendations for the Commission:

1. In my view, Cost-Plus construction contracts in a contingency environment are not essential or in the public interest.† That has already been proved in Iraq from 2005 onwards.† Every effort should be made in Afghanistan to switch to Firm-Fixed-Price Lump Sum contracting, just as occurred in Iraq.
2. The government should employ an engineering firm to manage the administration of the contract and provide independent third party engineering oversight. That oversight should include the capacity to act as a “referee” or “honest broker” between the Prime Contractor and Subcontractors. The Prime Contractor cannot be left alone to manage itself. The World Bank traditionally uses a model like this. More recently, the Millennium Challenge Corporation, a

U.S. government agency, has created a contracting structure that I believe is the best model for U.S. government contracts, even in a contingency environment.

3. The FAR and other forms of engineering and construction contracts should be revised to assure that legitimate claims for additional costs for out of scope work and events that are outside the control of the contractor are recoverable much more quickly than is possible today. In Iraq, many legitimate claims are taking years to resolve, leaving contractors, particularly small ones, in a financial bind until they get paid. Many contractors cannot afford to wait two years for money that they have spent to support projects. Symbion first submitted claims for a project in Hilla, Iraq, in July 2008, and although the U.S. government recognizes our entitlement to payment, we are still waiting two years later for the payment process to be resolved. The delays in this process have been exacerbated by numerous government personnel changes. If it is useful, I am happy to go into greater detail about this with the Commission's staff.
4. The U.S. government should examine and reform the use of the "Pay When Paid" clauses that Prime Contractors use in their Subcontracts. Subcontractors get smaller in size as their tier level descends. When they sign a Subcontract that says they will be paid every 14 days, payment 14 days later is what Subcontractors are entitled to expect. Telling them 60 days later that the Prime is unable to pay because the government hasn't paid it, and that they will be "paid when the Prime is paid" can crush smaller firms that do not have the capital to continue. It has always been my understanding that the U.S. government hires large firms as Prime Contractors because they have financial muscle, so it makes little sense to see small contractors being unpaid because a Prime didn't get its money from the government. This is how projects fail.
5. Government agencies and their oversight firms should require contractors to employ staff at every level of management who have been properly screened and vetted to assure they have the experience and qualifications required for the job. Anyone who has worked in Iraq or Afghanistan will tell you that some companies hire personnel with inadequate skills or insufficient management experience, and place them in positions where they are in over their heads. You simply cannot take someone who is a foreman in the U.S. and convert him or her into a Project Manager on the flight to Afghanistan or Iraq. This is a common and avoidable root cause of management failure that translates into inefficiency, delays, waste and other problems.
6. When a Cost-Plus contract exists, there should be a high level of supervision of the subcontracting process.† Much depends on the management, systems and controls that the Prime Contractor employs. Some are very good, and they follow similar guidelines and systems as the government.† However there are many where inadequate controls are in place. They pay lip service to written procurement procedures, and they manipulate the evaluations to award subcontracts to friendly firms.
7. There should be a requirement that foreign Subcontractors or foreign firms with U.S. government Prime contracts undergo training with regard to the FAR.

I can go into considerable detail on all the issues I have discussed in this testimony, and I am available to assist the Commission and its staff in the future in its important work. I

have been a first-hand witness to the efforts the United States has made in Iraq and Afghanistan. Many good construction firms have done their utmost to deliver projects in unimaginably difficult circumstances. I have witnessed the bravery, the commitment and the determination of U.S. military forces who have worked hand-in-hand with the contractors and the subcontractors who have tried to rebuild these two nations. Wartime contracting is evolving and I hope that my experiences can be helpful to the government.