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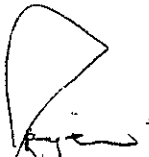
DEFENCE INDUSTRIAL PARTICIPATION (DIP) PRACTICE

SUMMARY: THIS DOCUMENT CONTAINS GUIDELINES FOR EXECUTION OF THE DEFENCE INDUSTRIAL PARTICIPATION POLICY APPLICABLE TO DEFENCE PURCHASES WITH A FOREIGN CONTENT OF USD 2 MILLION AND MORE.

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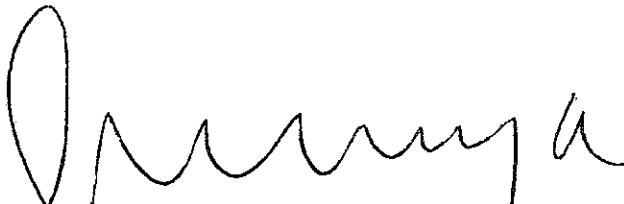
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APPROVAL PAGE



PREPARED BY
J E J POTGIETER (MS)
SNR MANAGER : DIP DIVISION

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DATE

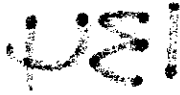


APPROVED BY
M E PHIYEGA
GENERAL MANAGER:
CORPORATE SERVICES

11/11/2002
DATE

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1. SCOPE

- 1.1 This practice on Defence Industrial Participation contains the guidelines with respect to the execution of the Defence Industrial Participation Policy as contained in A-POL-6000.

2. DOCUMENTS

2.1. Applicable documents

- 2.1.1. A-POL-6000 - Defence Industrial Participation Policy
- 2.1.2. A-PROC-6031 - Defence Industrial Participation Procedure
- 2.1.3. A-CORP-001 - Directives relating to decision making powers
- 2.1.4. A-PRAC-9010 - Acquisition Security
- 2.1.5. A-PRAC-1034 - Practice for the selection of contractual sources
- 2.1.6. A-POL-1000 - Acquisition Policy
- 2.1.7. A-PRAC-1011 - Supplier registration

2.2. Reference documents

- 2.2.1. MOD-7/5/97 - Secretary for Defence (MoD) Policy on Defence Industrial Participation Issue 6 dd 22/02/97, replaced by Revision 1 of 07/05/1997.
- 2.2.2. NIP-30/4/97- National Policy on Industrial Participation of the Department of Trade and Industry, dated 18/02/97 as approved by Cabinet on 30 April 1997.
- 2.2.3. The White Paper on the South African Defence Related Industries, dated December 1999.

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2.2.4. The Defence Review dated April 1998.

3. DEFINITIONS AND ABBREVIATIONS

3.1. "AAAC" means the Armscor Acquisition Authorisation Committee.

3.2. "Company" means any individual or collective defence-related company/companies, supplier, service provider, partnership, association, organisation, joint venture or other business entity organised or existing under South African laws or doing business in South Africa under SA laws. It further includes Armscor in its capacity as an accredited quality assurance organisation, acquisition authority, a service, research or equipment product provider where and when applicable.

3.3. "DIP" means Defence Industrial Participation which is a Government initiated process whereby defence purchases are used as a leverage to oblige a foreign seller of defence commodities/services to do defence-related business in SA on a reciprocal basis in order to advance military strategic and defence-related industrial imperatives.

3.4. "DIP Agreement" means the agreement containing the scope, definitions, commitments, terms and conditions regarding the DIP obligation, and contains details of project proposals (business plans) in accordance with the DIP policy. This is an agreement separate from the Main Agreement between the Seller and the Armscor DIP Division, even though it results from the Main Agreement, signed prior to or concurrently with the Main Agreement, by all parties concerned.

3.5. "DIP credit" means the value granted by the DIP Committee for the Seller's agreed performance, which results in the subsequent reduction in the Seller's obligation.

3.6. "DTI" means the Industrial Participation (IP) Secretariat of the Department of Trade and Industry.

3.7. "Foreign content" means the monetary value of all items, products and/or services sourced from foreign contractors and/or subcontractors in execution and fulfilment of the Main Agreement.

The purpose of this definition is the determination of the obligation of the Seller.

3.8. "Imported content" means the duty-free, free-on-board (FOB) / free carrier (FCA) value of goods and services of overseas origin incorporated into the products and services of the company to be supplied to the seller, and/or the seller's subcontractors and suppliers, and must be taken into consideration in determining the actual value of a DIP order or contract for the purposes of granting DIP credits.

The purpose of this definition is the determination of the DIP Credit value of a claim.

3.9. "Main Agreement" means the main agreement or purchase contract concluded between Armscor and the Seller for the supply of goods/services and which places the Seller under a DIP and NIP (where applicable) obligation.

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- 3.10. "MoD": References to "MoD" in this document refer to all the accountable line functions of the Secretary for Defence as Head of the Department of Defence (DoD), located in the Ministry of Defence (MoD).
- 3.11. "NIP" mean National Industrial Participation, which refers to the process as prescribed in the National Industrial Participation Policy, which is administered separately by the DTI, in accordance with their own rules and procedures, and which concentrates on civilian (non-defence) projects.
- 3.12. "RFI/RFP" means Request for Information/Request for Proposal.
- 3.13. "Seller" means the party defined as seller in the Main Agreement and subsequent DIP Agreement who becomes liable to supply the products/services via Armscor and to perform the DIP and NIP (where applicable) obligation.
- 3.14. "USD" means any amount in US dollars, automatically means and refers to any other monetary equivalent thereof.

4. PRACTICE

4.1. Responsibilities for Defence Industrial Participation

4.1.1 The Department of Trade and Industry

It is hereby acknowledged that the non-defence portion of the industrial participation programme will, where and when applicable, be the full responsibility of DTI, in accordance with the provisions of the NIP policy. Neither the DoD/MoD nor Armscor will be involved in the aforementioned process of DTI.

4.1.2 Armscor's DIP Division

All defence-related industrial participation projects emanating from Armscor's acquisition and procurement programmes shall be the full responsibility of Armscor's DIP Division. The DIP Division shall be fully responsible and accountable for the total process of managing and controlling all aspects relating to DIP, from contracting to completion. It includes the process of interaction, co-operation, communication and liaison with all the various role players.

4.1.3 Armscor's Divisional Head: DIP Division

The Divisional Head of the DIP Division is responsible and accountable for managing the DIP Division and its resources, for maximising DIP opportunities and attending to the full process of DIP negotiations and the subsequent DIP contract management processes. The Divisional Head of the DIP Division will also be expected to provide the Armscor Programme Manager, at his request, with suitable DIP provisions/documents for inclusion in the RFI/RFP, as and when applicable.

4.1.4 Armscor's Programme Manager

The Armscor Programme Manager must ensure that all RFI/RFP documentation for contracts with a potential foreign content exceeding USD 2 million include specific instructions to prospective Sellers regarding the DIP and NIP (where applicable) prescriptions which will officially be obtained from the DIP Division. The aforementioned must also assist the DIP Division with guidelines on direct and indirect DIP activity preferences, insofar as the latter might relate to defence industrial strategic considerations. Up and until a tender/contract is awarded, the Programme Manager and the DIP Division will co-operate as a team. However, once the respective agreements (Main, DIP and NIP) have been signed, each of these managers will take full and independent responsibility and

subsequently be responsible for the management of their respective agreements.

4.1.5 DIP Committee

The DIP Committee must be established by the DIP Division and will be responsible for the following:

- The ratification of RFI/RFP conditions with regard to DIP, as compiled by the DIP Manager for inclusion in such documentation, or determining whether or not a project must be subject to DIP, including the determining of the percentage DIP and its components.
- The approval of the evaluation results, as compiled by the DIP Manager, of DIP proposals received:
 - To evaluate, discuss, consider and approve DIP credit claims;
 - To recommend to the AAAC the approval for conclusion of a DIP agreement;
 - To discuss, consider and recommend to the AAAC the approval of any contractual amendments and/or revised business plans after the DIP Agreement has been signed;
 - To discuss, consider and recommend to the AAAC the approval of the cancellation of DIP Agreements;
 - To discuss, consider and recommend to the AAAC the application of a DIP contractual penalty in respect of a Seller's non-performance;
 - To discuss, consider and approve the utilisation of a Seller's banked credits for discharging partially or in full his indirect DIP obligation;
 - To approve that a Seller be notified that he has fully discharged his DIP obligations, and

- To approve that an audit be carried out at the Seller's or company's premises to verify any DIP claim received from the Seller.

The DIP Committee will consist of:

- Armscor's Divisional Head: DIP (the Chair),
- Chief of Acquisition: Defence Secretariat, or his appointed proxy (acting as co-chair),
- Armscor's DIP managers,
- a representative of Armscor's Finance Department,
- a representative of Armscor's Legal Division,
- Representatives from the maritime, aeronautic and army environment within Armscor's Acquisition Department (one representative for each area),
- Representatives from the maritime, aeronautic and army environment within the Defence Secretariat (one representative for each area),
- The Senior Manager: Technology, Management and Analysis Division (responsible for the management of the technology transfer activities contained in the DIP agreements).

4.2 Terms and conditions

4.2.1 Elements of DIP

DIP programmes may consist of the following two elements:

- a) Direct DIP shall mean specific DIP programmes, covering those activities which are directly (by specification) related to the products, services, materiel and/or equipment that are the subject of the Main Agreement.
- b) Indirect DIP shall mean those programme activities related to products manufactured by or purchased from, or services rendered by Armscor or

South African manufacturers in the defence industry in accordance with international industrial standards and/or military specifications at least equivalent or similar to those covered by the Main Agreement.

4.2.2. Discharge period/Fulfilment period

A maximum of 7 years (with agreed milestones within this period) is allowed for the Seller to discharge his DIP obligations. However, should the completion period of the Main Agreement extend beyond 7 years, the discharge period may be extended. The discharge period could furthermore differ from project to project.

4.2.3. Deviations

Deviations from the guidelines as contained in this par 4.2 can be approved by the Head of the DIP Division, in consultation with the Legal Division and/or the DIP Committee.

4.2.4. Evaluations

4.2.4.1. A comprehensive evaluation model/value system as devised by Armscor and used for the total evaluation of the RFP also forms the basis for DIP evaluation, and the DIP and NIP (where applicable) form(s) but one of the factors/elements to be taken into consideration. The Senior Manager DIP, in collaboration with the Programme Manager and with the approval of the DIP Committee, will decide on the weight the DIP and/or NIP will carry in the final evaluation model.

4.2.4.2 DIP proposals on defence projects must be evaluated on the basis of the contents of a prescribed business plan, clearly stating the Seller's proposed activities and milestones for discharging his DIP obligation.

4.2.4.3 The assessment of DIP proposals will be based on the extent to which such proposals support DIP objectives.

4.2.5. Investments

Investment can manifest in the following manner:

- a) It can be the amount of equity capital and/or value of capital equipment that the foreign Seller invests, for purposes of performing his DIP obligation, by physical transfer from the Seller's country to South Africa, for the benefit of the relevant industries. Investments should be for a period of at least five years in order to qualify for credit. Should the investment be for less than 5 (five) years, the DIP Division may decide to cancel and reverse any credit granted, unless the Seller can prove to Armscor that the return on such investment for any shorter period has resulted in a tangible advantage/gain for the relevant industry in South Africa. In such case only that portion of the advantage/gain for the industry in South Africa will be considered for DIP credit, and not the amount of the investment.

- b) Investments can also mean the accrued interest differential advantage gained by the local company for foreign loan capital granted by the Seller as part of his DIP obligation. Such loan repayments must be for a period of at least five years to be considered for granting of credits on the interest advantage portion gained or benefited from.

4.2.6. Joint ventures

Joint ventures refer to an agreement between the Seller or industries in the Seller's country and Armscor, or defence-related industries in South Africa, in terms of which each party contributes for the purpose of achieving a common and mainly defence industrial interest. For the purposes of the aforementioned the DIP Division, in collaboration with the DIP Committee, may consider credits for investments, technology transfers, marketing assistance and the nett gain for Armscor or defence-related industries in South Africa.

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4.2.7. Technology transfers

Technology and know-how transfers, which increase the efficiency of defence-related companies in South Africa or help to develop goods not previously manufactured in South Africa, must have an inherent value to South Africa. The DIP Committee must determine the value of such transfer in collaboration with Armscor's Technology Management and Analysis (TMA) Division for the purpose of considering credits.

4.2.8. Liaison

The DIP Division, in co-operation with the DoD will be responsible for arranging the necessary liaison meetings with DTI as and when required.

4.2.9. Banking

Excess credits or credits earned through proactive DIP agreements may be banked and trading will be allowed. DIP and NIP credits will, however, not be interchangeable by the Seller. The DIP Division and the DTI may, upon mutual consent, interchange credits or activities when circumstances warrant such, on condition that the objectives of DIP are still adhered to.

4.2.10. Proactive DIP agreements

The DIP Division is authorised and encouraged to promote and engage in *proactive DIP* agreements with third parties.

4.2.11. Cancellation

In the event that a DIP contract is cancelled, in whole or in part, due to the sole fault of the local company (in SA), no amount shall be deducted from the credit originally granted to the Seller. In the event, however, of such contract being cancelled in whole or in part for any other reason, the credit must be adjusted by the DIP Division, pro rata to the price paid for the goods delivered and/or services performed.

4.2.12. Penalties

- a) A penalty of 5% is levied by the DIP Division, with the approval of the AAAC upon the recommendation by the DIP Committee, on any unfulfilled portion of the DIP obligation for projects with a foreign content of USD 10 million or more.
- b) A penalty of between 5% and 15% (sliding scale principle) is levied by the DIP Division, with the approval of the AAAC on the recommendation of the DIP Committee, on any unfulfilled portion of the DIP obligation for defence contracts with a foreign content between USD 2 million and USD 10 million.
- c) The format and type of guarantee must be specified in the RFP, and may be either a bank, corporate or government type of guarantee. Such guarantee must be obtained by the DIP Division when or before the DIP agreement is signed.
- d) Armscor reserves the right to blacklist a Seller or its sub-suppliers participating in discharging DIP Obligations in South Africa, in addition to the levying of a penalty, for a period to be determined by the circumstances, with the approval of the AAAC on recommendation by the DIP Committee, based on their non-performance. Blacklisting shall mean at least prohibiting the party from submitting tenders to Armscor and publishing the information with respect to the blacklisting during the period determined above.

4.2.13. Multipliers

No multipliers will be allowed for determining any DIP Commitment or subsequent DIP Credit.

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4.2.14. **Facilitation**

The DIP Division may engage in the exchanging and swapping of offset obligations with third parties. Fees at competitive rates may be levied in compensation to Armscor, for the facilitation of the successful discharge of the Seller's or Company's DIP/Countertrade/Offset Obligations either in South Africa or internationally.

5. RESPONSIBILITIES

5.1 **Process owner**

The Armscor DIP Division is the process owner of this process.

5.2 **Communication**

The Senior Manager of the DIP Division is responsible for communicating this document.

5.3 **Implementation**

The DIP Division is responsible for developing the necessary templates and guidelines to support document development.

5.4 **Review**

The Senior Manager of the DIP Division will organise an interdepartmental working group to review the document to be completed before the internal audit cycle. This working group will also be responsible for implementing corrective/preventive actions and improvements to the process.

5.5 **Data management**

N/A.