

“Low Cost Tendering and the Sustainability of Building Contracts”

Rudi Klein recently wrote in *Building* (Issue 37, 17/09/10) about the dangers of Traditional Procurement. In particular he stated that traditional procurement was wasteful, a fragmented process with countless interfaces and hierarchical. Klein goes so far as to say that ‘...it could be considered negligent to advise a client that it procure its construction work using a traditional procurement approach and select the designers, contractors and the sub-contractors on the basis of lowest price’. It seems Klein is not alone in his thoughts. For a long time now we have been very concerned with the shift towards price only tenders and also low cost tendering.

As Consultants we were recently invited to tender on the basis of lowest cost only. When asked whether they would like to know about our proposed team, approach and methodology to the commission, the response was ‘Well, we know what you’re like, that’s why you’re on the list’!! Not surprisingly, we failed to win the tender and indeed found that our fee was nearly twice that of the winning consultant. The Client undertook a degree of due diligence on the lowest tender but with pressure from Board members and a limited budget (despite our tender being within budget) the client in essence was presented with an offer he couldn’t refuse. This behaviour is not uncommon.

Lowest price tendering is also reappearing in construction tenders. For some clients this has always been the way but over the past 10 years, particularly, post Egan, the mindset and attitude had changed with the public sector leading the way, particularly under Best Value following the Local Government Act 1999. However, with cash strapped Councils and other public sector bodies feeling the austerity measures of the new coalition, there is a movement back towards lowest price tenders. ‘Oh no, a return to the Thatcher years of Compulsive Competitive Tendering (CCT) I hear you cry’! These were bad days for everyone, not least of which the people involved in delivering projects during this time. Lowest price tendering seems to bring out the worst in everyone. Claims and disputes, cost and time overruns, short term relationships, fragmented supply chains and in most cases – FAILURE.

So who is to blame? I recently spoke with a mid size regional contractor with a turnover circa £80m per annum, specialising in new build homes in the social housing sector. He felt that low cost tendering was a result of a number of factors including:-

1. Market conditions;
2. A poor client;
3. Poor quality tender documentation caused by Consultants trimming input to match the fee;
4. Poor procurement practices including mix of quality and cost criteria
5. ‘If you can’t beat ‘em, join ‘em’ attitude!’

So I then said, *'Well what's the answer?'*

To which he responded, *'In an ideal world, all the tenderers would get together and agree to submit commercially realistic prices, but of course, we can't do that!'* Bearing in mind the OFT have recently found a number of contractors guilty of bid rigging!

So it seems then that tenderers are 'caught between a rock and a hard place'. So too it would seem, clients. Clients want a low price but equally they want good quality and an easy life. Contractors can of course provide a low price, but that comes with a high cost and this is why Traditional Procurement must be avoided in the current climate.

The recent demise of Connaught has highlighted that low pricing is simply not sustainable. This was exemplified none more so in the fateful award of contract by Norwich City Council to Connaught to undertake day to day repairs. Despite a challenge from Morrison on the grounds of the tender being abnormally low, the Council still decided to award the contract. The drive to increase shareholder value over the short term has led to a lot of very unhappy people. Think about the residents who are not receiving a repairs service; the client who is left to pick up the pieces of a failed contract; the unpaid sub-contractors and suppliers and most of all, the employees who no longer have a job (300 in Norwich alone). The long term impacts will be felt for years to come.

What alternatives are there then to Traditional Procurement? Well, PPC2000 and TPC2005 offer potential solutions. These of course are only contracts which are part of an overall procurement strategy. A sustainable procurement strategy must:-

1. Identify the procurement needs of the organisation, i.e. clearly defined project or programme;
2. Set out a clear strategy for the overall procurement process;
3. Ensure that collaboration and integration are at the heart of how the project will be delivered including the early appointment of the core team;
4. Ensure that contractor selection strategies reflect the procurement need. For example, if the product/service is of low value such as stationery, then lowest price may be perfectly acceptable. For high value, complex products such as the design and build of new homes, then selection criteria must be weighted more heavily in favour of quality;
5. Set out a realistic budget for the project or programme.

PPC2000 and TPC2005 contribute to a sustainable procurement agenda through the following mechanisms contained in the contract:-

Early contractor appointment – PPC2000 allows for the early appointment of the contractor to enable them to contribute to design development as part of an integrated team;

Supply Chain Development – Both PPC2000 and TPC2005 include provision for ‘Supply Chain Business Cases’ which is a mechanism for getting specialists and sub-contractors integrated into the team at the earliest opportunity;

Open Book Accounting – The Client may exercise their option to undertake open book accounting. This can apply in the development of prices through open book tendering, as is more prevalent in PPC2000 or as a management tool on Term Partnering Contracts. In the case of the former, open book can be used to determine whether the contractor is achieving a fair and reasonable return and that the client is receiving value for money;

Project and Term Reviews – This is an (contractual) exercise for all partnering team members to review progress and performance and to implement continuous improvement measures.

In addition to the above, TPC2005 in particular, is used on longer term contracts. Therefore, getting the right pricing from the start is critical to long term success. Given that the pricing established at the start of a programme is usually via a tender exercise, it is imperative that these are sustainable from the start. If contractor selection remains on lowest price then the current market that is driving low cost tendering may mean that low prices remain for the life of the contract, resulting in all of the problems set out earlier. The client and/or consultant advising the client must be prepared, where necessary to challenge pricing and in some cases, reject tenders that would appear to be abnormally low and in any event unsustainable. As Rudi Klein put it, in not doing so, could be negligent. Now, where is the risk? Rejecting a tender and facing a challenge or accepting a tender, facing a negligence claim and the fallout from the failing contractor. To my mind, the answer is simple. The question is ‘Which way will you go?’