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Report

Procurement strategy

Better Barnsley Phase 2 Barnsley Metropolitan Borough Council

making the **difference**

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1 Introduction

This report has been compiled to outline the options available to Barnsley Metropolitan Borough Council ("BMBC") for the procurement of the construction works required for Phase 2 of the Better Barnsley scheme.

The works are expected to cost in the order of £50m and are therefore in excess of the statutory thresholds that trigger the processes contained in the Public Contracts Regulations 2015 for the procurement.

The procurement must be complete by the end of 2017, with a fixed Contract Sum, in order that the terms of an unconditional funding offer can be agreed for the construction of the scheme and therefore the requirements of the anchor leisure tenant met.

2 Procurement Objectives

The procurement of the works needs to support the project to achieve key objectives, such that it does not invite undue risk onto the scheme and provides you with the protection you need in terms of risk transfer, such that each of the key parties to the contract are accountable and have a defined responsibility for performance. In this instance, the key objectives of the procurement are to:

- Have a works contractor in place with a signed construction contract prior to the end of the year (2017).
- Provide programme certainty, in order that long-stop dates contained in lease agreements are secured.
- Provide cost certainty, in order that the scheme funder's financial position is not compromised, as the scheme's ability to make a profit is directly linked, through the development appraisal, to the capital cost of the scheme.
- Transfer sufficient risk to the contractor to make them responsible and accountable for performance throughout the works.

3 Market Conditions

It is important to understand the market environment in which the procurement will be undertaken, as this will steer the recommendation for the preferred option.

Six months on from the EU referendum, many of the dire economic predictions prompted by the UK's surprise vote for Brexit have failed to materialise. Britain's economy continues to make solid progress, with GDP rising by 0.6% in the third quarter of 2016 – an increase of 2.2% on the same period in 2015.

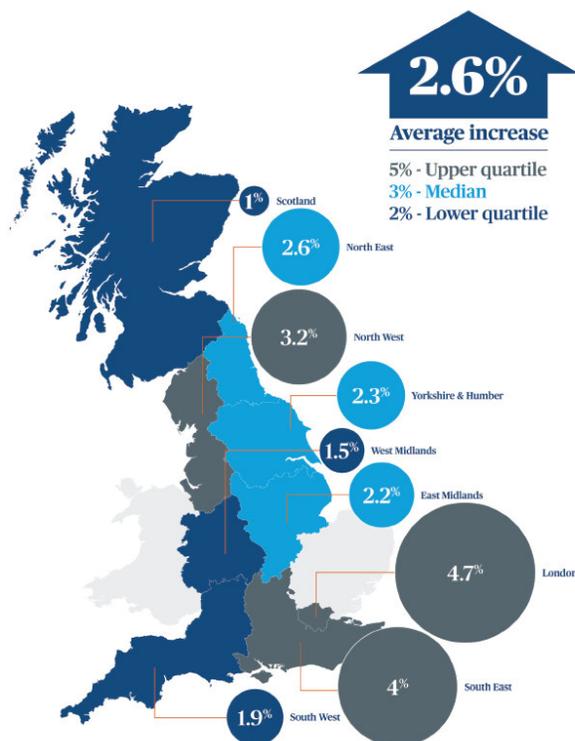
However, construction sector indicators have been more mixed. Construction industry output shrank by 0.8% in the third quarter and the total number of new orders fell by 1.7% compared to Q2, whilst increasing by 5.5% above the level recorded in the third quarter of 2015.

Sentiment in the industry has see-sawed, as knee-jerk concerns seen in the aftermath of the June referendum gave way to a more pragmatic, "business as usual" approach. In July, the UK Construction Purchasing Managers' Index, a closely-watched barometer of industry sentiment, plunged at its fastest level in seven years. Yet by September, it had vaulted firmly back into growth territory, before rising further in October and November.

Traditionally, periods of softening demand lead to increased competition and falls in tender prices; however, the third quarter's sudden rise in material costs, combined with long-term labour shortages, will drive up both tender prices and levels of competition – a trend that is set to continue as the industry confronts the Brexit process proper.

Our predicted tender price index annual percentage changes are outlined in the following table, with the regional estimated rise over the next 12 months depicted in the adjacent graphic:

Year	Building	Infrastructure
2016	3.6%	4.2%
2017	2.3%	4.3%
2018	2.1%	3.9%
2019	3.0%	3.6%
2020	3.5%	4.0%



3.1 Key Price Indicators

3.1.1 Materials

Recent hikes in input costs and Sterling weaknesses have placed further pressures on materials costs. Structural materials will see a significant rise in price over the next 12 months, with an average increase of 5.5% predicted.

3.1.2 Preliminaries

Limited movement in the level of preliminaries was evidenced in Q3 2016 and they stay in line with 2016 results as a whole.

3.1.3 Overheads and Profits

Across the UK, OH&P's have largely stayed the same over the past three months, yet downwards movements have been mooted to secure work streams.

3.1.4 Labour

Skills shortages and scarce availability of specialist trades are driving labour cost inflation higher.

3.2 Procurement Outlook

Since recovering from the last recession, the construction market has reassessed their approach to tendering. Many contractors lost money on projects tendered at unsustainably low prices and with little regard for the risk that was transferred to them, which halted abruptly, with many local and regional contractors suffering financial difficulties.

The market is now more robust in its approach. Negotiated and two-stage procurements are preferred and, within them, contractors are demanding a greater time period to understand the project detail and risks, in order that the contract sum is robust ahead of signing contracts.

Single-stage tendering is much less appealing to them, with many now limiting either the number of projects they will tender on this basis or capping the value and complexity of the projects that they are willing to consider under this approach.

We are seeing high value (over £20m), complex projects fail to attract significant interest in the marketplace through a single-stage tendering approach. The market is currently reasonably buoyant, therefore if there are other, more attractive, tendering opportunities through a two-stage or negotiated procurement route, estimating resource would be allocated to these procurement routes and single-stage opportunities would be returned without a bid.

4 Procurement Options

There are several procurement options available to BMBC in the procurement of the works for Phase 2. The options cover both the procurement procedures and the form of the procurement as follows.

4.1 Procurement Procedures

- Public contracts regulations ("PCR") 'Open' procedure.
- PCR 'Restricted' procedure.
- PCR compliant contractor framework.

4.1.1 PCR Open Procedure

The PCR open procedure allows the contracting authority to issue the tender to any contractors in the European Union who request it, as a result of information provided in a Contract Notice published in the Official Journal of the European Union (OJEU).

The open procedure can be used with both single and two-stage procurements. The main issues of this type of procedure are:

- BMBC could be inundated with tender responses, increasing the programme for review and recommendation of the selected contractor.
- Contractors may consider that as they are tendering against an undefined number of other contractors, the risk in bidding is high and therefore decline to tender.
- The tender list is made up of tenderers who do not have sufficient experience or capacity to undertake the works.

4.1.2 PCR Restricted Procedure

The PCR restricted procedure allows the contracting authority to pre-qualify contractors based on defined suitability criteria, before drawing up a shortlist of contractors to be issued with the tender. Pre-qualification credentials are requested from contractors through the issue of a Contract Notice published in the OJEU.

The restricted procedure can be used with both single and two-stage procurements and is the most commonly used form of procurement for projects above the PCR threshold cost. The main issue with this type of procurement are:

- Tender information (representing the information on which the pre-qualified tenderers are expected to base their price) must be issued with the pre-qualification questionnaires.

4.1.3 PCR Compliant Contractor Framework

Pre-qualification of contractors to tender the works can be fast-tracked, through the use of a construction framework. The framework used must have been established through a PCR compliant quality and pricing assessment.

The use of a framework will give BMBC access to a pre-selected shortlist of contractors, who can be invited to express their interest in tendering for the works before being issued with the tender documentation. This results in a shorter process than the PCR restricted procedure, as the need to pre-qualify has already been satisfied and contractors on the framework have already demonstrated they have sufficiently good standing to undertake construction works.

Two examples of frameworks that can be used by BMBC are YORBuild and the Ministry of Justice Strategic Alliance agreement. An access fee is sometimes payable to the framework managers to allow the use of the framework.

The main issues associated with this type of procurement are:

- An access fee is sometimes payable to the framework manager by the contracting authority.
- Contractors on the frameworks may already be saturated with work through the framework and therefore interest may be reduced.
- The framework contractors may not have specific experience related to the type of construction works required by the contracting authority.
- Framework places are often won by contractors tendering rates for overheads, preliminaries costs and profit. These can be abnormally low, as they are put forward in competition and contractors can then attempt to recover their 'loss' against these low rates in sub-contract package prices.

4.2 Procurement Strategy

The following is a resumé of the characteristics of potential procurement strategies and their likelihood of success in meeting the client's objectives. The key options are:

- Traditional procurement.
- Design & Build (single-stage and two-stage).
- Management Contracting.
- Construction Management.
- Design, Manage & Construct with GMP.
- Partnering.

4.2.1 Traditional Procurement Methods

Traditional routes offer a number of benefits:

- Cost and time certainty prior to the commitment to build.
- Competitive tendering techniques.
- Effective design control.
- Effective and prescribed means of managing change.

However, the benefits are outweighed by a number of disadvantages. Extensive design and documentation is required prior to the tendering process, in order to achieve cost certainty and thus prolong the programme period. The overall timescale is lengthy, due to the sequencing of design, procurement and construction activities.

Furthermore, and more fundamentally, a high degree of design, programme (in particular during the design phase) and cost risk remains with the client and, for this reason in particular, such traditional methods are deemed inappropriate for this project.

4.2.2 Design & Build (Single-Stage)

Design & Build brings the advantages of a firm fixed price and programme prior to the commitment to build, reduced periods for design and procurement and a single point of responsibility. However, these advantages are offset by the tendency for contractors to seek to reduce their costs through reduction in design quality and specification, rather than through direct benefit problem-solving. Therefore, there is the perception of a dilution of quality and increased maintenance requirements.

These disadvantages can be offset by instilling control in the design through carefully prepared tender documents that control those elements of the project valued by BMBC, whilst leaving the non-critical elements to the contractor to apply value engineering principles to. This benefits the client in the form of a competitive tender and also allows the contractor areas to generate margin within the confines of the project and the contract, whilst also adding value to the package as a whole.

4.2.3 Design & Build (Two-Stage)

The two-stage route involves Stage 1 tenders based on a scheme design, engagement with one or two contractors for the second stage design development and final selection of a preferred bidder. This procurement method resolves some of the issues associated with a single-stage design and build project, particularly as design control can be maintained through the second stage. More importantly, it enables the earlier involvement of the contractor than many other routes. This is not always necessary but, on projects where detailed planning of construction method is required, this involvement is beneficial.

The concern with a two-stage approach is the difficulty in controlling costs during the second stage. Recent experience has suggested significant increases compared to the first stage tenders, predominantly as a result of risk transfer and an inability to engage with "busy" contractors. This can be mitigated by simplifying the process of selecting a single contractor for the second stage and by the introduction of a mechanism to incentivise the reduction of project costs by the contractor. With this mitigation in place, this route could be suitable to BMBC's needs on this project.

4.2.4 Management Contracting

The principal advantage of Management Contracting (in fact the only real rationale behind the choice of such a route) is the ability to overlap design, procurement and construction, enabling a very early start to be made on site. Therefore, it is of benefit where a short overall project timescale is of paramount concern.

Management contracting has the very significant disadvantage of no cost certainty before the commitment to build and, for this reason above all, is considered unsuitable for this project.

4.2.5 Construction Management

This route has similar benefits to Management Contracting, although it removes the potential for duplicated administration costs; however, Construction Management shares the principal disadvantage of Management Contracting and, as such, is not appropriate for the project.

4.2.6 Design, Manage & Construct with a Guaranteed Maximum Price (GMP)

This has the advantages of certainty of cost and time, providing that the GMP agreement can be achieved quickly, flexibility to make changes, accelerate design and construction, and utilises competition with value for money being maintained through 'open book' arrangements and incentivisation through shared savings.

A disadvantage is that the final design may have to be compromised to achieve the GMP, although this may be minimised through the novation of consultants. There is also the perception that tenders may be inflated, due to the contractor’s risk being committed to a GMP.

4.3 Summary Review Against Project Objectives

The scoring of these assumes that the Employer’s Requirements are well defined prior to tender, with minimal client changes during the post-contract stage.

BMCs Objectives	Traditional	D&B (single stage)	D&B (two stage)	Management Contract	Construction Management	DMC with GMP
Programme certainty	Poor	Good	Good	Average	Average	Good
Risk transfer	Average	Good	Good	Poor	Poor	Good
Early contractor involvement	Good	Average	Good	Poor	Poor	Average
Cost certainty (post-contract)	Poor	Good	Good	Poor	Poor	Good
Design control (post-contract)	Good	Average	Good	Good	Good	Average
Durable/ maintainable product	Good	Good	Good	Good	Good	Average
Market acceptance of procurement route	Good	Poor	Good	Good	Good	Average

Key:

Poor	Poor
Average	Average
Good	Good

From the above table, it can be seen that the most favourable option is two-stage design & build.

We would recommend that the procurement is undertaken using the PCR restricted procedure or through a framework, in order that the tendering contractors’ suitability to undertake the works can be determined ahead of the issue of the tender documentation.