

A FUTURE MODEL FOR PROCUREMENT



REVERSE ENGINEERED TWO-STAGE



THE FIRST IN A SERIES
OF FUTURE54 REPORTS
WITH A DETAILED VIEW
OF TRENDS IN THE
INDUSTRY.



REVERSE ENGINEERED TWO-STAGE PROCUREMENT

The contracting market has become very heated over the last few years in London and there has often been difficulty in procuring main contractors (even large reputable ones) who have the leverage to get specialist sub-contractors to tender on projects. Specialists are increasingly key to projects and often hold more cards than main contractors.

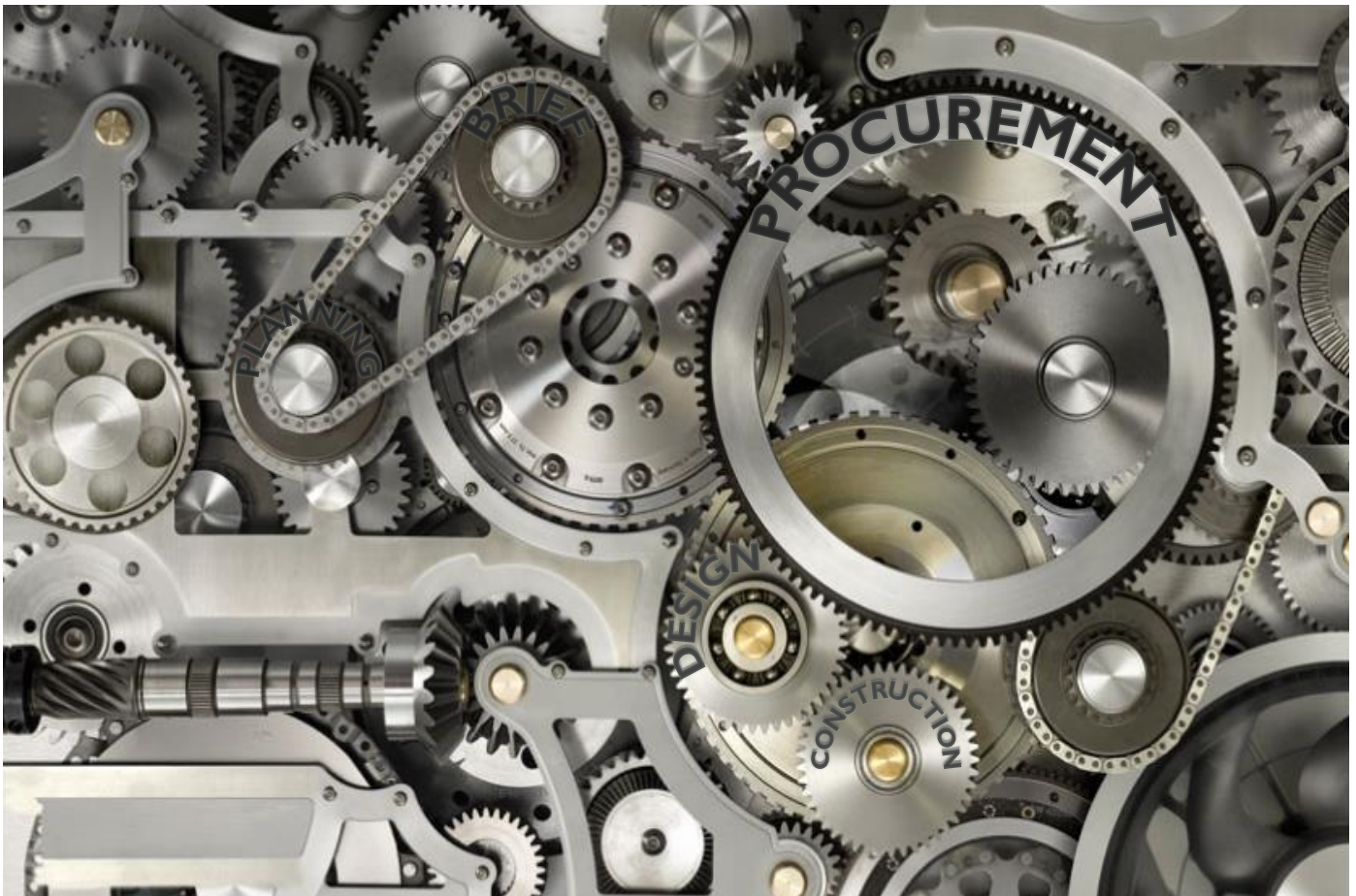
As a result, there has been a move towards Clients getting more actively involved in the supply chain rather than leaving it to contractors who, despite their historic role in tendering are becoming less effective in getting tenders from good quality specialist sub-contractors on larger projects. Specialist sub-contractors like this approach as they get closer to the Client and with the use of a project bank account their payments are better protected.

A move towards re-verse tendering has therefore started to take shape with the Client's project team looking to procure key specialist packages in advance and then 'wrapping' these under a standard form of building

contract with a main contractor. For those who remember, this is akin to the old 'nominated' sub-contractor approach but with the main contractor taking them on board as a domestic sub-contractor and accepting insolvency and performance risk.

In many ways, this is a quasi-construction management approach pre-contract and could also act as an initial halfway house for those Clients who would like to dip their toe in the water ahead of a full construction management approach, supported with an appropriate Construction Management team.

THE ROUTE



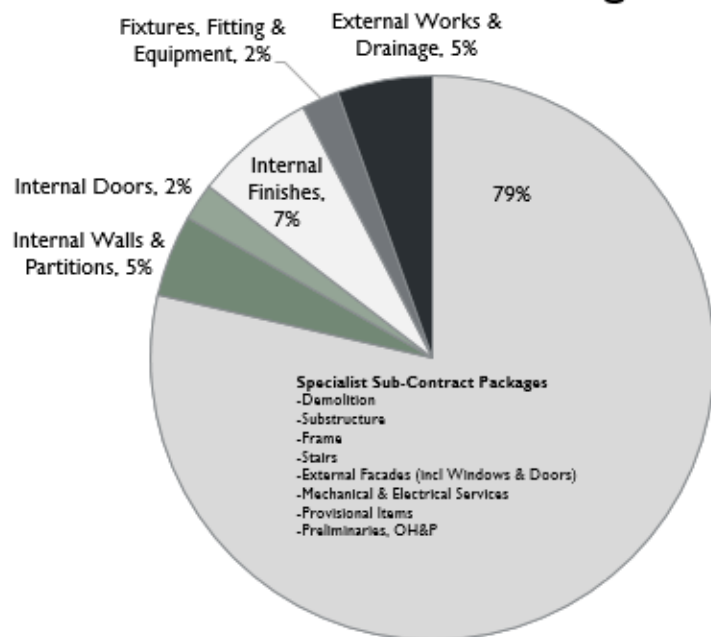
APPROACH

The key components are shown in the activity journey overleaf. Clearly each project will be different and a bespoke strategy and programme will need to be developed to reflect the particulars of the present.

In broad terms, the approach comprises the identification of key specialist trades and the procurement of these in parallel with a main contractor and any residual packages. The main contractor will accept these specialists as a domestic sub-contractor and provide a final lump sum commercial offer at the end of the 2nd stage procurement stage.

It is not intended that all packages are tendered direct to specialists but, only those that provide programme and/or commercial advantage. The residual packages will be tendered by the main contractor who will have been chosen under a separate and parallel 2-stage procurement approach. We would expect that the packages tendered directly to specialists could deliver up to 80% fixity of costs, depending on the project type and agreed packages.

Example Specialist Procurement vs Residual Trade Packages



PROJECT BANK ACCOUNTS

Project Bank Accounts (PBA's) are ring-fenced bank accounts whose sole purpose is to act as a channel for payment on construction projects to ensure that contractors, key subcontractors and key members of the supply chain are paid on the contractually agreed dates. The employer maintains adequate funds in the account to cover work in progress and other project commitments. Payments are made directly from the account to the contractor, key subcontractors and key suppliers in accordance with the payment arrangements agreed by those members of the project team who are party to the PBA. PBAs should speed up payment and reduce payment abuse, particularly for those lower down the supply chain for whom late payment can have a significant impact against what are often very tight margins. The reason for this is that payment does not have to flow down the contractual chain: instead, those members of the project team who are party to the PBA are paid directly from the PBA

- Graeme Barton at SH Legal, our partner.

ACTIVITY JOURNEY

KEY COMPONENTS

Strategy + Approach

- ◆ Identify Key sub-contract packages for Employer tender- those of high value, requiring long design or manufacture lead time, where commercial gain/ early commercial clarity is required.
- ◆ Produce programme- map design and planning activities against the procurement of key packages and main contractor
- ◆ Agree the specialist sub-contractor basis of tender and whether the packages can be tendered as a single tender basis or need a 2-stage approach under a PSCA agreement

Specialist Trade Package Procurement

- ◆ Warm up specialists, identify and Pre-Qualify against Long-list.
- ◆ Tender Packages.
- ◆ Evaluate and recommend.
- ◆ Finalise / agree Contract on which main contractors will appoint.
- ◆ Place any early orders – if necessary before main contract appointment.

Note: It may be necessary to procure under a 2-stage process certain key sub-contractors (part of the Strategy and Approach)

Final Negotiations and Contract Execution

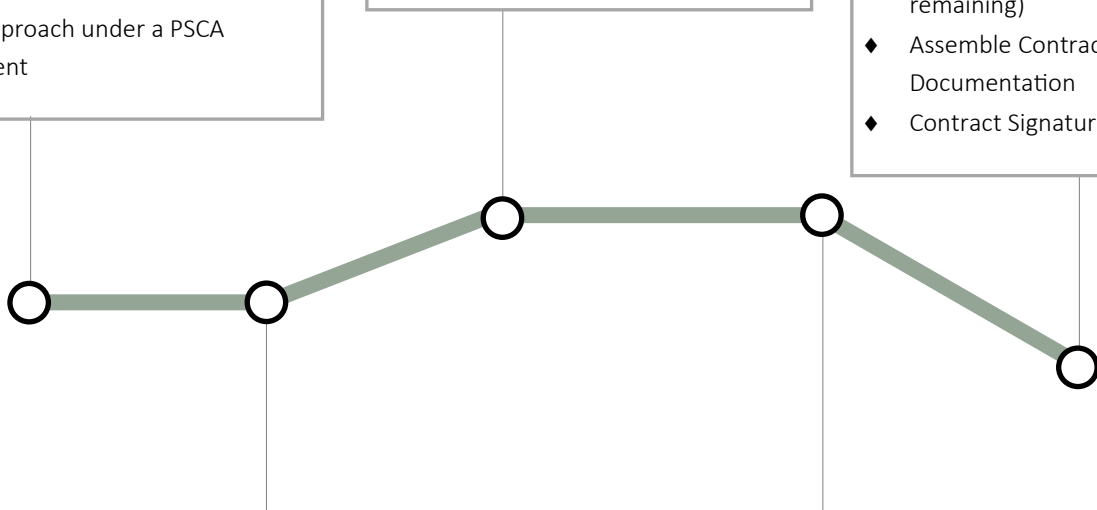
- ◆ Final Negotiations (if any remaining)
- ◆ Assemble Contract Documentation
- ◆ Contract Signatures

Package Split

- ◆ Produce and agree package split and identify key design interfaces.
- ◆ Identify key specialist sub-contractors and Main Contractors to tender (Long List).
- ◆ Align Cost Plan with trade packages.

Main Contract Procurement

- ◆ Warm up market, Identify and Pre-Qualify against Long-list
- ◆ 1st Stage Tender Period
 - ◇ Evaluate against approach and commercials (Preliminaries, OH&P plus Risk mark-up)
 - ◇ Evaluate and recommend
- ◆ 2nd Stage
 - ◇ Tender residual packages
 - ◇ Final programme and negotiations with specialists
 - ◇ Final Contractor Offer
 - ◇ Evaluation and recommendation 2nd Stage
 - ◇ Client approval



KEY ATTRIBUTES TO SUCCESS



- ◆ Develop strategy and programme and secure to buy in from the Client and design team.
- ◆ Develop a robust suite of sub-contract tender documentation and evaluation approach.
- ◆ Develop sub-contract documentation that aligns with the main contract documentation.
- ◆ Warm up the market so that they have absolute clarity and confidence in the approach- it is fairly new so they will want to be confident in how it works.
- ◆ Define the key packages and interfaces early and develop a trade package strategy.
- ◆ Develop the design at the appropriate stage to reflect the agreed approach (for example, post RIBA Stage 2).



- ◆ **Transparency** of sub-contractor tender process with direct feedback from specialist sub- contractors and not watered down via a main contractor- leads to better pricing.
- ◆ More attractive to sub-contractors with **better payment terms** able to be negotiated through use of a Project Bank Account and direct payment - greatly reduces risks to sub-contractors (Client needs to demonstrate their funding credentials too).
- ◆ More direct conversations on any 'better buying' or **value engineering** with benefits on price and / or programme.
- ◆ **Better visibility** on make-up of risk which will allow negotiation of appropriate risk transfer premium (where appropriate).
- ◆ **Transfer of risk** for performance and insolvency is still passed to the main contractor.
- ◆ Benefit of **shortening / de-risking programme** by earlier tendering and getting key specialist elements progressed.
- ◆ Scalable approach that can be **tailored to suit a Client's appetite** for risk and capacity and capability - option to flip into a Construction Management route.

“HAVING A CLEAR STRATEGY IS FUNDAMENTAL TO MAKING THIS APPROACH”

THE RISKS

- ◆ Need to ‘join’ specialist sub-contractors and Main Contractors together in contract - the need to have a clear strategy and to warm up the market is fundamental in making this approach work.
- ◆ Main Contractors and/or sub-contractors not willing to work with one another or under contract terms- need to be careful that any potential specialist sub-contractors and main contractor’s names are shared as far as possible to avoid this situation.
- ◆ Need to define specialist programme and methodology without main contractor on board- need programme expertise so there are no unintended consequences.
- ◆ Specialist sub-contractors are tendered and potentially orders placed (depending on programme) before the final cost is known- this is also an opportunity to gain programme advantage and/or de-risk programme by commencing specialist design earlier.



ROLES

In order to deliver this approach there will need to be a much more proactive involvement at the front of the project as the team look to provide a 'quasi' construction management role during the pre-construction stage. Under a traditional two stage procurement approach the Client would normally pay the contractor a fee for this work under a Pre-construction Services Agreement.

The additional roles that a Project Manager and Quantity Surveyor would deliver would include:

- ◆ Strategy and approach
- ◆ Trade package definition and programme
- ◆ Construction Programming
- ◆ Sub-contract procurement
- ◆ Sub-contractor names and pre-qualification (financials and capability etc.)
- ◆ Sub-contract terms of appointment (the main terms including sub-contract) upon which the main contract would appoint
- ◆ Any early sub-contract orders ahead of contract
- ◆ Project Bank account payment authorisation

Designers would need to input into the Package Strategy and provide 'Package Information' to support earlier tendering of specialists.

FUTURE54 ARE CURRENTLY DELIVERING THIS APPROACH ON LIVE PROJECTS. MORE OF OUR CLIENTS ARE SHOWING AN INTEREST IN BECOMING MORE ACTIVELY INVOLVED IN THE PROCUREMENT PROCESS IN ORDER TO SHAPE THE DELIVERY OF THEIR PROJECTS AND NOT BE A HOSTAGE OF FORTUNE.

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