Traditional Contracting Reform

Developing a National Approach:
Traditional contracting of infrastructure projects

CONSULTATION PAPER
FEBRUARY 2012
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CONSULTATION PROCESS

REQUEST FOR FEEDBACK AND COMMENTS

The Department is seeking the views of Industry Participants and other interested parties on whether further work would be of benefit to promote improvements in the productivity of infrastructure delivery through traditional contracting.

This proposal is part of a package of micro-economic reforms aimed at improving the planning and delivery of public infrastructure across the Nation.

Submissions may be lodged electronically or via post using the address details provided below. For accessibility reasons, please email responses in a Word or RTF format. An additional PDF version may also be submitted.

All information (including name and address details) contained in submissions will be made available to the public on the Department of Infrastructure and Transport website, unless you indicate that you would like all or part of your submission to remain in-confidence. Automatically generated confidentiality statements in emails do not suffice for this purpose. Respondents who would like part of their submission to remain in confidence should provide this information marked as such in a separate attachment. A request made under the Freedom of Information Act 1982 (Commonwealth) for a submission marked ‘confidential’ to be made available will be determined in accordance with that Act.

Closing date for submissions: 30 March 2012

Email: DC_submissions@infrastructure.gov.au

Mail: Mr Andrew Danks (Director)
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INTRODUCTION AND BACKGROUND

INTRODUCTION

Australia’s productivity as a nation and infrastructure productivity in particular, has been widely debated, with the Commonwealth Government publicly stating that it will be seeking to improve infrastructure productivity.

As a Council of Commonwealth Governments’ (COAG) Infrastructure Working Group (IWG) initiative, the Victorian Department of Treasury and Finance and the Commonwealth Department of Infrastructure and Transport was tasked to investigate opportunities for improving the efficiency and effectiveness of market engagement and tendering strategies for Traditional Contracting, particularly Design & Construct (D&C).

The investigation was conducted through a qualitative research method using semi-structured interviews to gather experience and insight from many practitioners in the public and private sectors (covering both client and supplier groups). The results of the investigation have been outlined in the report ‘Towards agreed expectations: Tender strategies to improve Design & Construct infrastructure delivery outcomes’.

The report highlights a number of opportunities where further work would be of benefit and which will promote improvements in the productivity of infrastructure delivery through traditional contracting. The main theme is the development of a national approach or set of principles for traditional contracting in infrastructure.

The report notes that the jurisdictions have to varying degrees, different sets of comprehensive and long standing legislation, common law, regulations, policies and guidelines applying to traditional contracting. Whilst these approaches have achieved good outcomes, there were strong views from practitioners that improvements could be made.

Although it makes sense to maintain separate policies that address the unique features of each jurisdiction, this paper outlines seven recommendations where further work would be of benefit to promote improvements in the productivity of infrastructure delivery.

BACKGROUND

Public sector procurement of capital assets follows three (3) main delivery models, distinguishable by the allocation of management accountability for the project delivery risks. The models are commonly referred to as:

- Public Private Partnerships
- Alliance Contracting
- Traditional Contracting¹

Each of these main delivery models have numerous variants with various levels of use and maturity.

The Infrastructure Working Group (COAG) sponsors agreed on national frameworks (of policy and guidelines) for Public Private Partnerships and Alliance Contracting (see Figure 1).

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¹ For the purposes of this paper, the term ‘Traditional Contracting’ covers Design & Construct (D&C) and similar forms of contract (often referred to as ‘hard dollar’ contracts).
Therefore, it is viewed that a national approach for traditional contracting of infrastructure will also promote improved productivity at all phases of the project lifecycle; planning, procurement, construction and operate and maintain. It will do so by improving the efficiency and efficacy of traditional contracting by identifying, developing and promoting best practice delivery of traditional contracting from across jurisdictions.

In developing the recommendations for the development of such a national approach for traditional contracting in infrastructure, the procurement phases in Figure 2 were used to provide a structure for considering the likely topics.

Figure 2: The typical phases in the planning and delivery of traditional contracting projects and related Recommendations
### Summary of Recommendations

These recommendations address further work that can be undertaken in traditional contracting. This work was identified as result of investigations conducted for the report: *Towards agreed expectations: Tender Strategies to improve Design & Construct infrastructure delivery outcomes.*

#### Recommendation 1:
Prepare a National Infrastructure Guide on Good Practice and Commercial Principles as a basis for best practice and policy (recognising that the development of a national policy may be an initiative for the longer term).

**Objective:** to establish a common set of Principles (from planning to the post build evaluations) that each jurisdiction uses as a basis for its best practice policy and practices when using traditional contracting.

**Comment:** Jurisdictions have comprehensive and long standing legislation, common law, regulations, policies and guidelines in traditional contracting. The optimal approach is to develop national good practice principles that jurisdictions can translate into their internal documentation and practices.

#### Recommendation 2:
Encourage member jurisdictions to consider opportunities for promoting internal consistency in contractual terms and conditions; and for consistency in the application of those contractual terms and conditions.

**Objective:** several fold: firstly to increase transaction efficiency (and hence lower costs to all), promote best practice, and assist alignment of expectations within a jurisdiction.

**Comment:** The *Towards agreed expectations* investigation confirmed little appetite for national standardised contractual arrangements. Agencies and contracting parties expressed the view that value is obtained from individual intra-jurisdictional consistency in contractual terms and conditions; and equally important is the consistency of application of those contractual terms and conditions.

#### Recommendation 3:
Develop a framework of nationally available training courses and capability strengthening activities for public officials.

**Objective:** to improve the capability of public officials engaging in traditional contracting by taking a national approach.

**Comment:** Whilst universal agreement was evidenced for the critical role that capability plays in optimising public sector outcomes, there are no coordinated training programs as seen in the PPP and Alliancing space. This initiative would also incorporate a structured “knowledge sharing” framework.
**Recommendation 4:**
 Develop a topic specific guideline on best practice project definition parameters (including project risks) for both the planning and procurement phases.

**Objective:** to increase the quality of documentation that forms the basis of tendering and thereby gives greater certainty to all parties on the sustainability of tender outcomes.

**Comment:** This would address an important concern from tenderers, and confirmed as an issue by some clients, the need to promote a consistent standard in design briefs; and a common project definition 'language' that can be used by both clients and tenderers.

**Recommendation 5:**
 Develop a topic specific guideline on best practice development of projects budgets, which would also allow for the benchmarking of outturn costs across projects and jurisdictions.

**Objective:** to establish robust (but achievable budgets) that reflect leading practice.

**Comment:** This would allow for the establishment of best practice guidelines for the development of project budgets; and importantly a consistency of cost data will enable the collection of ‘benchmark’ data that agencies can then use in negotiation and performance management with contractors.

**Recommendation 6:**
 Develop a topic specific guideline on best practice governance and contract management including dispute resolution during the construction phase.

**Objective:** to improve the quality of decision making during the construction phase by increasing empowerment, accountability and clarity of authority.

**Comment:** Governance structures can empower the client's project team to exercise effective and efficient decision making to manage project outcomes, and this can be integrated with contract management and dispute resolution across the project life cycle.

**Recommendation 7:**
 Develop a framework for the application of a tenderer's past performance as a key tender selection criteria when awarding future contracts for capital works.

**Objective:** to improve project delivery and reward tenderers who have performed well in the past.

**Comment:** Practitioners consulted in this investigation (both agencies and tenderers) see merit in the application of assessment of past contract performance when selecting the winning tenderer on new contracts being offered.
THE PROPOSAL AND CONSULTATION QUESTIONS

THE PROPOSAL

The proposal for consultation is to seek the views of Industry Participants and other interested parties on where further work would be of benefit to promote improvements in the productivity of infrastructure delivery through traditional contracting.

The report ‘Towards agreed expectations: Tender strategies to improve Design & Construct infrastructure delivery outcomes’ highlights that a good characterisation of the root cause of dissatisfaction was the expectation gap, identified in terms of the supplier’s understanding of the client’s need versus the client’s understanding of the supplier’s offer.

We wish to gather views on the merit of the seven recommendations listed above.

CONSULTATION QUESTIONS

There is now an opportunity for interested parties to contribute further to the work already done. The Commonwealth Department of Infrastructure and Transport and the Victorian Department of Treasury and Finance are seeking your comments and views on:

1. Do you agree that a national approach towards traditional contracting (incorporating the seven recommendations) would benefit the infrastructure industry?
   • If no, please specify the reason(s) for disagreement and provide any amendments or alternatives

2. Are there additional topics or issues that should be considered in developing a national approach that might promote improvements in traditionally contracted infrastructure projects?

3. What other work should be done (outside the national approach) to improve outcomes for traditional contracting of infrastructure projects?
RECOMMENDATIONS

RECOMMENDATION 1 –

PREPARE A NATIONAL INFRASTRUCTURE GUIDE ON GOOD PRACTICE AND COMMERCIAL PRINCIPLES AS A BASIS FOR BEST PRACTICE AND POLICY

Objective: to establish a common set of Principles that each jurisdiction uses as a basis for its best practice policy and practices.

Whilst the common use of PPP and Alliance Contracting models are relatively new to the Australian public sector, traditional contracting has been well established in jurisdictional policies, guidelines, regulations, common law and/or legislation for a great number of years.

In the interviews conducted, the common view was that the effort required to produce an agreed national policy position was out of proportion to the potential benefits that could be derived. A national consensus on policy, if ever judged desirable, may be more manageable once national support for a set of national good practice principles is achieved.

Therefore, a different approach to that taken for PPPs and Alliance Contracting (which are underpinned by policy) should be considered in developing a national framework for traditional contracting.

These principles would:

• Set out good practice commercial principles for the various forms of traditional contracting outlined in Towards Agreed Expectations.

  These might include:

  - the development of model business rules that ensure streamlining of activities to maximise efficiency of transaction costs for all parties having a mind to certainty of outcome (including consistency regarding timelines)

  - establishing the tender strategy and processes; and setting expectations among tenderers

  - clearly identifying the objectives for using traditional contracting (eg is the primary purpose risk allocation? or is the emphasis on allowing the D&C relationship to work to the benefit of the client by removing the potential disconnect between ‘D’ (design) and ‘C’ (construct)?)

  - providing guidelines on the documentation and activities requested of tenderers (avoiding excessive information requests)

  - promote where sensible the use of tested precedent documentation (as appropriate for generic aspects of projects) to reduce costs and minimise unnecessary new documentation

  - promote the development of well targeted EOI and RFT up to a benchmark standard of documentation that attracts the most appropriate bidders and generates confidence

• incorporate the project’s whole-of-life requirements, from the planning phase through to operations and maintenance;
• develop principles and a framework for undertaking post build evaluations, including a “feedback loop” into the planning and management (e.g., business case preparation, procurement options analysis, tender documentation and strategies, contract management etc) of future projects;

• adopt different approaches as may be required for “complex” or “mega” projects to accommodate their specific project characteristics i.e., multi-discipline, complex stakeholders, never been done before, etc. (This would draw on research work current in the UK, along with other research into ‘mega’ projects and recent Australian industry learnings);

• incorporate best practice advice on developing the tender selection criteria and the tender evaluation approach (this being critical to the success of the tender process);

• incorporate the use of probity as an enabler in achieving the optimum tender and project outcomes (this will ensure probity requirements are applied appropriately and do not unnecessarily inhibit the tender process, collaboration and ultimately the project outcome and that probity supports new approaches to procurement); and

• explore commercial innovations in traditional contracting, for example the use of performance pools.
RECOMMENDATION 2—

CONSISTENCY IN CONTRACTUAL ARRANGEMENTS WITHIN JURISDICTIONS

**Objective:** to increase transaction efficiency (and hence lower costs to all), promote best practice, and assist alignment of expectations within a jurisdiction.

Practitioners interviewed (both clients and contracting parties) had little appetite for national standardised contractual arrangements. However, contracting parties expressed the view that value could be obtained from individual intra-jurisdictional consistency in contractual terms and conditions; and equally important consistency of application of those contractual terms and conditions.

These views reflect the industry being structured along jurisdictional boundaries or regions; with state-based offices having a depth of knowledge and expertise of local practice. A national perspective was evident in senior executives with national corporate responsibilities.
RECOMMENDATION 3—

IMPROVING THE CAPABILITY OF THE PUBLIC SECTOR

Objective: to improve the capability of public officials engaging in traditional contracting by developing a national framework of nationally available training courses and capability strengthening activities for public officials

A clear message from all practitioners interviewed is that the capability of people to manage and execute the planning and project delivery activities required of them is critical for good public outcomes. This view has been expressed for many years across many forums and both the PPP and Alliance Contracting models have established training courses that are available nationally.

An opportunity exists to develop a suite of nationally available training courses for public officials. This initiative would also incorporate a structured “knowledge sharing” framework.

Improving knowledge sharing between procurement/tender teams and the project delivery teams (for both buyers and sellers) would support continuous improvement and better outcomes for both industry and government. This could include the transfer of knowledge from completed projects to future projects.

This recommendation would:

• provide for public officials a training program that develops their capability, including thought and commercial leadership, in the planning, tendering and delivery of traditional contracts;

• promote a practice of contracting which should achieve optimal outcomes for taxpayers, agencies and industry generally;

• promote a commercially astute approach by public officials to the structuring and practice of traditional contracting; and

• promote a “community of practice” amongst public officials nationally that will encourage and enable the sharing of lessons learnt and ‘good practice’ between practitioners nationwide.
RECOMMENDATION 4—

A GUIDELINE FOR PROJECT AND DESIGN DEFINITION PARAMETERS

Objective: to increase the quality of tender documentation, giving greater certainty to all parties on the sustainability of tender outcomes.

In the interviews conducted, tenderers and clients across all jurisdictions strongly supported the need to improve both private and public sector understanding of the importance of design definition. All parties agreed that better design definition in the planning and procurement phases would offer significant benefits to traditional contracting; particularly in construct only projects.

Establishing and defining clear and comprehensible design requirements is identified as one of the foundation success factors that ‘we should aim to get right every time’ in Towards Agreed Expectations. Interviews conducted also found that tenderers were more likely to have better confidence that they are dealing with a desirable client when provided with high quality project definition. The consensus was that better confidence in project definition and design parameters would consequentially lead to and support effective collaboration between clients and tenderers; resulting in better project outcomes with a minimum expectation gap.

A guideline would promote standards across jurisdictions on minimum levels of design; and a common ‘language’ that can be used by both clients and tenderers in tender documentation (eg “fit for purpose”). In addition, this guideline would address the dimensioning of project risks to ensure the optimum transfer and pricing of project risks.

The guideline would seek to promote consistency of tender documentation between and within client agencies by use of tested precedent documentation as appropriate for generic aspects of projects. Tenderers familiar with the documentation from an agency/across agencies can build confidence, simplify the task of responding to EOIs/RTFs, reduce uncertainty in what the client requires and minimise unnecessary documentation requests.

This recommendation would:

- develop the link between the Business Case service need and the project’s physical specifications;
- establish a detailed best practice framework for the development of project definitions and the development of optimum levels of design and risk analysis in the procurement process;
- establish a best practice standard for the level of project definition and design to be used in the EOI and RFT documentation;
- establish a best practice standard to inform the dimensioning of project risks that are to be transferred to tenderers; and
- analysis information from tenderers the transaction costs of participating in public infrastructure tender processes and the opportunity to ameliorate these costs through appropriate project definition and reference designs.

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RECOMMENDATION 5—

A GUIDELINE FOR DEVELOPING AND BENCHMARKING PROJECT BUDGETS AND OUTTURN COSTS

Objective: To establish robust (but achievable budgets) that reflect leading practice.

Application of a consistent standard in the preparation and presentation of capital project budgets may assist in providing comparability across projects undertaken by single agencies and across jurisdictions.

A new general purpose national guideline would build on the work already undertaken in this area by the Australian Government (Best Practice Cost Estimation Standard for Publicly Funded Road and Rail Construction, May 2011) and by the Victorian Government (Determining Project Budgets in Business Cases, Exposure Draft August 2011). Further, the guideline would lay the foundations for the possible future development of a nationally consistent framework for establishing project budgets and to compiling a national cost data base that over time will incorporate actual cost outcomes.

Importantly, this work would focus specifically on how Australian public infrastructure transaction costs compare with other jurisdictions and identify opportunities for improvement. The ability to use ‘benchmark’ data in negotiation and performance management would be of significant benefit in evaluation and negotiation. In ensuring usefulness of the data, it will be important to ensure the data reflects leading practice rather than merely historical outcomes.

This recommendation would:

• establish the overarching linkages from the business case’s investment rationale for addressing service needs to the physical scope of required capital assets and to the development of a project budget;

• establish an understanding of how methodologies to develop project budgets have generally evolved and specifically for the style of current traditional projects;

• develop best practice guidelines for developing project budgets, including definitions and standards for developing base cost estimates and estimates for project risks building on Best Practice Cost Estimation Standard for Publicly Funded Road and Rail Construction, Determining Project Budgets in Business Cases and other jurisdictional guidelines;

• develop a standard template for presentation of project budget cost breakdowns that allows for inter-jurisdictional benchmarking of project costs;

• define project budget objectives in capital and infrastructure projects from a government (rather than project office perspective);

• identify lessons learnt from recent project budget and outturn costs outcomes and recommend policy positions and guidelines that reflect those lessons learnt to optimise value for money;

• establish best practice guidelines for the management of project budgets during the construction phase; and

• provide a sound basis for potentially establishing a national database of actual costs incurred using Best Practice.
RECOMMENDATION 6 –

A GUIDELINE FOR GOVERNANCE AND CONTRACT MANAGEMENT DURING CONSTRUCTION

Objective: to improve the quality of decision making during the construction phase by increasing empowerment, accountability and clarity of authority.

There are many examples and models of project governance and contract management across jurisdictions. Best practice governance structures empower the client’s project team to support effective and efficient decision making to achieve project delivery objectives. Similarly, best practice can be researched and documented to deal with contract management and dispute resolution across the project life cycle in traditional contracting.

This recommendation would:

- develop best practice models for project governance in traditional contracting;
- provide governance models for complex or mega projects (which limit the extent which authority can be delegated);
- investigate and provide best practice based on current and emerging practices in contract management and dispute resolution specific to traditional contracting and lessons learned from other complementary and variant procurement methods;
- investigate and provide best practice on commercial principles and processes for dispute resolution; and
- develop guidelines which demonstrate best practice principles in the contract management of traditional infrastructure projects.
**Recommendation 7—**

**Using a tenderer’s past performance as a key tender selection criterion**

**Objective:** to improve project delivery and reward tenderers who have performed well in the past.

Governments have a large program of capital projects that are tendered and completed on a regular basis. Practitioners consulted during this investigation (both agencies and tenderers) see merit in the assessment of past contract performance when selecting the winning tenderer on new contracts being offered. This is undertaken widely (albeit informally) by private sector clients but infrequently by the public sector.

The objective of developing such a framework would be to normalise the use of the assessment of a contractor’s past performance when making decisions on awarding future contracts. Such a framework needs to be developed carefully and prudently and in a way that is consistent with good government procurement practices.

In developing this framework, the following matters would need to be considered:

- making provisions in current tender conditions to allow assessments of past performance for use in the tender selection criteria of future tenders;
- such provisions to include the acceptance of the client’s properly formed judgement of the contractor establishing a cooperative and productive relationship with the client’s contract management team, and delivery of the subject project as per the client’s explicit expectations at contract award;
- determine a suitable assessment criteria for performance in a current contract;
- the use and content of “company score cards”, and the development of an appropriate tender selection criterion;
- the feasibility of using such a framework across agencies and even across jurisdictions;
- the nature of guidance/training to be given to the client’s project management and tender evaluation teams to implement this framework;
- relevant mitigation strategies and processes to avoid probity risks; and
- international experience in the use of this approach.