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| Report to | Cabinet |
| Date | 29 September 2022 |
| Report By | Director of Communities, Economy and Transport |
| Title of Report | Highways Services Re-procurement Project |
| Purpose of Report | To inform Cabinet of the outcomes and recommendations from the procurement stage of the Highway Services Re-procurement Project |

RECOMMENDATION: Cabinet are recommended to consider the process and outcomes from the procurement stage of the Highways Services Re-procurement Project and agree to award the Highways Infrastructure Service Contract to the preferred bidder, tenderer (A).

1. Background Information

1.1 The purpose of this project is to procure a new highway maintenance contract to replace the existing contract arrangements that end on 30 April 2023. The contract is designed to enable delivery of the five service outcomes agreed by Cabinet in July 2021 included in Appendix 1.

1.2 The project has adopted the Council's Strategic Commissioning approach to determine the service and outcomes required. In January 2021 Cabinet approved the recommendations from the Outline Business Case (OBC) that had been developed from the first stage of the commissioning approach, the 'analysis' stage. This provided two options for further consideration, Option 1 – Separate Works Contract and a Separate Designer Contract or Option 2 - an Integrated Single Provider Works and Design (current Service Delivery Model).

1.3 In July 2021 Cabinet approved the recommendations from the Detailed Business Case (DBC), developed during the 'Analyse' and 'Plan' stages of the commissioning approach, to develop Option 2 - an Integrated Single Provider Model. Cabinet authorised the Director of Communities, Economy and Transport to develop the contract model and undertake the procurement process to determine the preferred tenderer to be awarded the contract (the 'do' stage of the commissioning approach).

1.4 This report summarises the contract that has been developed, the procurement process followed, the tender evaluation, the key outcomes (including affordability), the recommendation for award of a new contract, and the arrangements to be put in place to manage the new contract (changes to the client Contract Management Group).

2. Supporting Information

The Contract

2.1 Section 2 of Appendix 1 summarises the documents that form the basis of the new Highways and Infrastructure Services Contract 2023-30. The contract is an initial term of seven years (2023-30) with an optional extension of a further seven years (2030-37). Award of the extension is not mandatory; it is discretionary. A further report will be presented to Cabinet at the appropriate time prior to the decision on whether or not to utilise the extension option. This decision will need to be taken at the end of Service Year 5 (March 2028) in order to allow sufficient time for a re-procurement to take place if the extension option is not taken up. A key benefit of this approach, should an extension be awarded, is that the Council only pays out once for direct re-procurement project costs (mobilisation, demobilisation, internal procurement costs and tenderers costs); the total of these can be between £3m-£4m. In the event that the adjusted prices (extension business case) are unaffordable, the parties do not agree or the agreed performance criteria are not met, a re-procurement exercise would then need to be carried out.

2.2 The contract includes the services in section 2.4.3 of Appendix 1 and includes (1) Core Activities, priced as lump sums (fixed annual price with annual inflation uplift applied per service year), (2) improvement works commissioned as actual costs with target cost (only actual cost is paid) and (3) un-planned works as cost reimbursable actual cost works.

2.3 The contract is based on current ESCC highways policies (e.g. intervention levels) and the contract terms and conditions are based on the industry standard NEC4 Engineering and Construction Contract, modified as appropriate, with output focused specifications designed to enable delivery of the five service outcomes agreed by Cabinet in July 2021 included in Appendix 1.

2.4 The contract includes the transfer of approximately 190 of the existing contractor's staff to the new provider. The contract also includes 17 specific performance indicators, and 7 key performance indicators, with targets linked to contract payments that incentivise the contractor to deliver works for more value in order to access a potential share, generated from any saving if a required performance level is achieved. If the performance level is not exceeded there is no access to the incentive payments from the 'clients share'. In addition, poor performance entitles the Council to remove part, or all, of the contractor's share, profit or works from the contract.

2.5 The contract includes protection for timely payment of the supply chain by use of a project bank account, specific social value requirements to invest in local communities through apprenticeships and 10% of bonus share committed being delivered to local communities through resources or cash to support ambitions for their local network.

The Procurement Process

2.6 Section 3 of Appendix 1 sets out the process followed to select the preferred bidder on the basis of the Most Economically Advantageous Tender (MEAT). This included a five-stage, 19-part evaluation process using a 45% quality, 7.5% carbon, 7.5% social value and 40% price model.

2.7 The selection questionnaire (SQ) stage (Stage 1) was with 6 candidates (detailed in section 3.1.3 of Appendix 1). Following evaluation of the SQ stage, the top three highest scoring candidates were invited to submit detailed tenders (price and quality) at Stage 2. The detailed tender period (Stage 2) lasted 13 weeks, during which 301 tender clarifications were received.

2.8 Following completion of Stage 2, the project board met twice on 27 May 2022 and 10 June 2022 to determine if the project should progress to the optional Negotiation Stages 3 & 4 or Stage 5 as set out in the Instructions for Tendering (Volume 0). A decision was made to progress to Stage 5 – Tender Validation. The three tenderers were informed of the decision through the Intend tendering system on 17 June 2022.

2.9 The decision to not progress to Negotiation Stages 3 & 4 was based on members expectations around quality and any descoping compromising the achievement of the agreed service outcomes. It was also considered that a complex negotiation stage could increase the potential for the process to be subject to challenge, and the Project Board were also mindful of the risk that tenderers may recalculate prices, given the increased inflationary pressures since tenders were submitted. Finally, time pressures on the project timeline were noted and the Project Board expressed a preference not to have to extend or negotiate with the incumbent should the project timeline slip at any point.

Tender Evaluation Process

2.10 The three remaining tender submissions, from Stage 2, were assessed by dedicated independent quality and price evaluation panels from the Project Team and subject matter experts from across the Council. Evaluation of the quality submissions was undertaken against four key themes: General, Strategic, Service Delivery and Contract Management, consisting of 27 individual quality statements (Table 2, page 21 of Appendix 1) using a scoring matrix (Table 1, page 20 Appendix 1).

2.11 An evaluation of Tenderers' price submissions was undertaken against three pre-determined price evaluation models, consisting of core activities, Contractors Total of Prices (seven-year contract totals) and a fee assessment (Table 5, page 25 Appendix 1). Only the prices for core activities (lump sums) represented the actual price to be paid for services. There is no tendered schedule of rates for capital works. Any capital works that are commissioned over the contract duration will be paid for at the actual cost of works with the tenderers' fee percentage applied. Various NEC4 payment options (Target Cost, cost reimbursable or Lump Sum) will be utilised depending on the complexity of the works.

Tenderer Withdrawal

2.12 Following notification to proceed to Stage 5 – Tender Validation and not Stage 3 – Negotiation, all three Tenderers were asked to confirm that, should they be awarded a contract, they would be willing to enter into a contract based upon: the issued terms and conditions (Volume 1, Contract Data Part 1), their quality offering submitted (Volume 5) and their submitted Price offer (Volume 4).

2.13 Both Tenderer A and Tenderer B confirmed their acceptance. However, Tenderer C qualified their response, which would require an amendment to the Contract, specifically requiring the Council to take on more financial risk, underwriting the Contractor's failure.

2.14 The Council wrote to Tenderer C setting out that their qualification meant their tender was not compliant and therefore did not pass the Stage 5 – Tender Validation. This is because the qualification would have fundamentally altered the intention of the Contract. However, Tenderer C was given the opportunity to remove their qualification unconditionally.

2.15 Tenderer C notified the Council on 19 July 2022 that they were unable to remove their qualification and therefore confirmed they would be withdrawing from the tender process. Acknowledgement of their voluntary withdrawal was sent on 20 July 2022.

2.16 The withdrawal of Tenderer C meant that the five activities (N-R) to be completed under Stage 5 Tender Validation (section 9, page 12, Appendix 1) were only completed on the remaining two compliant Tenders, from Tenderers A and B.

Stage 5 – Tender Validation Results

2.17 The final validated combined scores for quality, carbon, social value and price are shown on page 15 of Appendix 1. Tenderer A and Tenderer B were required to articulate their bids during a 45-minute presentation, 1 hour Question and Answer session and a series of interviews with a number of their proposed key people (senior management team). The initial scores from Stage 2 could be adjusted, if necessary, should the tenderer not be able to adequately address any questions raised by the Project Team.

2.18 During Stage 5, the evaluation panels satisfied themselves that the two tender submissions, for quality, carbon, social value and price had been substantiated and demonstrated by the tenderers. Consequently, there were no adjustments made to the overall evaluation scores awarded at the end of Stage 2, resulting in Tenderer A scoring the highest validated combined score of 84.8% compared to Tenderer B scoring 56.2%.

Awarding the Contract

2.19 Following the tender evaluation process, and in accordance with the criteria set out in the tender documents, it is recommended that the Highways and Infrastructure Services Contract 2023-30 is awarded to Tenderer A (a synopsis of their bid is set out in Annex 2 of Appendix 1).

2.20 Tenderer A's submission scored the highest quality score (best overall approach to service delivery), highest carbon score (most proactive carbon emission management), highest price score (lowest priced) and second highest score on social value. Of the 23 quality questions that were scored 0 to 10 marks, Tenderer A scored full marks on five occasions (the only tenderer to score 10/10), demonstrating an excellent response that exceeds the Council's requirements and a commitment to additional added value.

2.21 The overall tender response demonstrates, with a range of examples as evidence, that Tenderer A will ensure key services are delivered on time and, as a minimum, a safe and usable network is provided. In addition, the response demonstrates: transparency of prices and actual cost for planned works with the opportunity for additional value from an incentivised target cost approach; the benefit of the expertise in asset management with the ability to support our outcome to have the best network area network condition for the investment available; the introduction of new market leading customer management and mobile technologies to manage the service and provide real-time and timely information for Councillors and stakeholders; ability to reduce third party claims through proactive management of the network; a demonstratable approach to collaborative working and customer focus with commitment to invest in our communities and to promote the economy of East Sussex through the use of local supply chains and local employment.

The Contract Management Group (CMG)

2.22 In addition to developing a new contract and identifying and appointing a new service provider, a review has been completed of the current client structure (the Contract Management Group (CMG)) who will manage the contract on behalf of the Council to ensure good contract management and value for money is delivered throughout the life of the contract.

2.23 The proposed CMG structure is shown in Appendix 2. This will provide four key functions to ensure the contract and the service is managed and delivered correctly. The structure reflects the Scrutiny Member Reference Groups (SMRG) needs regarding greater quality assurance and more focused stakeholder management. The review has reduced the total number of posts from 36 to 32 (4 of which are currently vacant), providing a total saving of £0.198m of which £0.129m is revenue. The Council will work with the new Contractor and the ESCC Property team to complete an accommodation review in Service Year two to ensure the implemented depot strategy is providing the most efficient and effective service delivery. This review may identify potential savings and/or release of surplus buildings.

2.24 The new structure puts a restructured Asset Management team at the centre of our approach in managing our network and enables us to understand our asset needs and ensures the service is functional and sustainable. Strong Commercial and Contract Management will ensure the solutions proposed by the contractor present value for money and ensures professional contract administration and risk management. The Contract and Commercial team have a strengthened Supervisory function that will complement the new Contractor's responsibilities in providing greater quality assurance for works completed across the network.

2.25 A dedicated team to monitor and benchmark Performance & Service Development will inform and evidence our approach and will enable us to measure our success against the service outcomes and the Council's key priorities. The Performance & Service Development Team will promote a 'one organisation' approach working with our members, communities and contractor to develop the culture, reputation, funding and services people want, whilst also supporting our local communities and economy.

2.26 The Stakeholder and Engagement Team will provide dedicated focus, working collaboratively with the new contractor's Stakeholder Manager, to support members to deliver Effective Stakeholder Engagement (a key service outcome), which is about engaging effectively to understand and meet the needs of our stakeholders to deliver a 'right first-time' service delivery.

Affordability Assessment

2.27 At Stage 2 of the tender process, the price evaluation team and corporate finance completed an affordability assessment of the three tenderers' (prior to Tenderer C withdrawal) prices in comparison to current budgets and forecast costs made within the financial case of the DBC. The purpose of this activity is to confirm financial implications and financing requirements for the duration of the contract. A copy of the complete affordability assessment is set out in Annex 3 (pages 37-41), of Appendix 1.

2.28 Within the DBC it was highlighted that there was a significant risk that the tenders for the new contract will result in higher prices (core activity lump sums) due to the current contract with Costain not reflecting inflationary increases each year (by design). Costain made an assessment in their bid of the anticipated level of inflation over the seven-year contract period and fixed the cost to the Council based on those assumptions. Their allowance within the lump sums is lower than the actual level that has occurred leaving an expected inflation gap that would be reflected in the tender prices for the reprocedured contract. Costain further discounted their bid prices and their percentage management fee at the time of tender (as a new entrant to the market) resulting in both the current lump sum prices and percentage management fee being very competitive. Additionally, there was risk of the core activity lump sum prices increasing should the current commercial discount applied by Costain not be replicated by the tenderers.

2.29 When completing the DBC it was very difficult to predict how the market might react. Much was dependent on market prices (which we know have risen), but also on how the market perceives the Council's opportunity and the scope for commercial adjustments that tenderers are prepared to make to their bids.

2.30 Based on current contract spend for the lump sum prices (charged to the revenue budget), a mid-point estimate of £1.375m pressure per annum has been included within the MTFP as part of the contract inflationary pressures protocol approved by CMT in September 2020.

2.31 Following completion of the affordability assessment (Annex 3, Appendix 1), the financial environment has changed rapidly and the impact on the contract prices is an additional annual pressure of £1.794m, providing a cumulative pressure of £3.169m per Service Year of the new contract on the Highways revenue budget. This includes £0.8m for an estimated 8% increase from bid to Year 1 prices, though this could vary as it is based on the actual contract indices at February 2023.

2.32 The Highways capital programme has an annual budget set at £27.931m for 2022/23-2031/32, as agreed by the Capital Board. Capital works are commissioned at actual cost as per paragraph 2.11, therefore any cost increases, including the increased management fee percentage (approximately 3.5% estimated at £0.930m) needs to be managed within this budget envelope.

2.33 In addition, the total lump sum prices (revenue budget) are subject to an annual uplift for inflation over the seven-year contract duration, to be managed through the RPPR process. Based on latest guidance (March 2022 update) from the Office for Budget Responsibility, the annual increase is modelled on an average of 2% per service year which equates to £0.164m. This value will be adjusted when contract indices become available.

2.34 By design in the tender pricing model, in addition to pricing the core activity lump sums, tenderers were required to price for one off contract mobilisation costs. This is an additional revenue cost to paid to the Contractor in 2023/24 (Service Year 1) as they complete the activities set out in the mobilisation plan. Tenderer

A's mobilisation costs total approximately £2m (includes an estimated 8% allowance for inflation uplift). A full cost breakdown of the mobilisation costs was provided by Tenderer A as part of the Stage 5 – Tender Validation activities. The £2m is in line with the Project Team expectations; however, it was unclear what commercial approaches the tenderers would take and so it was difficult to model what the final value would be within the DBC.

3. Conclusions and Recommendation

3.1 The tender received from Tenderer A meets the requirements of the tender process and the proposals for managing and delivering the service set out in the contract. The Project Team have assessed their prices and validated the full build up and determined that they are accurate and sustainable (subject to funding availability). The Project Team have also satisfied themselves that Tenderer A's organisational approach, experience and market ability meet the requirements to organise, manage and deliver our future highway services to support the Council's ambitions for the network and enable the delivery of the project outcomes.

3.2 The recommended tender increases current pressure in the MTFP by £1.794m and, in addition, under the terms of the new contract, the Contractor is entitled to an annual inflationary uplift applied to the Core Activities (lumps sums) over the life of the contract. Notwithstanding this pressure, when completing the tender evaluation, the recommended Tenderer A is the Most Economically Advantageous Tender (MEAT) offering the Council the lowest contract price and the highest contract quality.

3.3 It is therefore recommended that Tenderer A be awarded the Highways and Infrastructure Services Contract 2023-30.

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LOCAL MEMBERS

All

BACKGROUND DOCUMENTS

None