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To: Cabinet – 23 May 2011.

Subject: Appointment of 'Preferred Bidder' on new Kent Highway Services Contract

Classification:

Summary

Over the last 13 months Kent Highway Services, supported by corporate procurement and key Members, have been engaged in a national search for a new, high quality, good value, highway contractor.

The key objectives for this procurement have been:-

To improve quality of work - by placing the risk with the contractor

To improve value for money - by procuring from a competitive market, placing performance risk with the contractor, reducing costs year on year to ensure ongoing value for money

Ensuring complete procurement flexibility through the life of the new contract

Ensuring a service provision that delivers against Bold Steps for Kent, Growth without Gridlock and other key KCC objectives and initiatives.

This report provides an overview of the extensive and robust process that has been undertaken and seeks the Cabinet's support in approving Enterprise as KHS' 'Preferred Bidder' and that the Corporate Director of Enterprise and Environment and the Director of Governance & Law be authorised on behalf of the County Council to enter into the contract with the 'Preferred Bidder'.

Existing Service

1.0 Kent Highway Services provides highway services to the residents, businesses and visitors of Kent. It currently consists of 4 main parties:-

- KCC Highways (the client and statutory responsible authority)
- Ringway (Term maintenance contract) – contract ends 31st August 2011
- Jacobs (highway design)

- Telent (traffic signals & intelligent transport systems) – an extension to 31st March 2016 has been negotiated and agreed. The revenue savings to KCC as a direct result of these negotiations are in the region of 20%. NB. *These savings have been included in the current and future years budgets.*

1.1 Other stakeholders are involved in service provision, such as KCC Commercial Services, district councils, an annually tendered machine surfacing contract and a variety of small local companies. Separate cost reduction exercises are currently being undertaken for these and all other suppliers.

1.2 This report is aimed specifically at seeking approval for the **replacement for the Term Maintenance Contract**.

<u>The current term maintenance contract</u>

2.0 The current contract started on 3rd July 2006. It was regarded as an innovative contract and was designed to remove incentives for the contractor to cut corners, whilst limiting profitability but providing a framework for all to celebrate success together.

2.1 The key features of the contract were:-

- Based extensively around partnership working
- A 'true' cost plus payment mechanism
- Depots provided to contractor at £0 cost
- Achievement of jointly owned performance indicators which could have led to an additional performance payment
- No penalties (financial pain) for poor performance
- Possible contract extensions until 31st March 2016

2.2 This contract has had an annual turnover of £66m (averaged since its commencement) and covers the majority of all highway maintenance and improvement services.

2.3 The scope of service included:-

- Routine Maintenance, i.e. carriageway, footway, structure repairs;
- Winter Service;
- Emergency and Out of Hours Response;
- Drainage, Gulley Emptying and Repairs;
- Signs, Lines and Barriers Maintenance;
- Highway Improvement Schemes (small to medium in size);
- Street lighting routine maintenance, replacement of asset and emergency response;
- Annual programmed resurfacing, highway surface treatment and smaller patching / small resurfacing works (annual programmed resurfacing removed post 2009)

2.4 The main exclusions being:-

- Carriageway machine surfacing (post 2009), approx. £5m pa – tendered on a separate annual contract.
- Major new build capital projects – these are externally tendered on a scheme by scheme basis.
- Soft landscape – this is undertaken by a combination of district councils, KCC Commercial Services and small local companies.
- Find and fix patching – undertaken in the last 2 years by SMEs.

Why change the contract

3.0 Whilst the theory of a partnering cost plus works contract appeared attractive six years ago, it has not delivered the necessary value for money, quality, responsiveness or strategic vision that was intended.

3.1 Since early 2010, the Corporate Director of Enterprise & Environment has chaired a Highways Strategic Procurement Board, to agree the best way forward and to oversee delivery of the required outcomes. The Board has been attended by the Cabinet Member, Director of Highways, Interim Director of Procurement and other service key officers. The areas for improvement from the existing contract were:-

- Performance/productivity risk
- Quality risk
- Payment mechanism
- Measuring actual performance
- Clarity of responsibility and accountability
- Costs/performance to be benchmarked with other highway authorities
- Cost estimating, control and certainty
- Administrative burden.

3.3 It was clear that a significant change was needed, and that it was needed as a matter of urgency. Other factors that supported this view were:-

- The current construction market was depressed and rates had fallen significantly due to the increased competitiveness.
- New forms of contract and procurement process (eg. Competitive Dialogue) were available that had not been considered when the original contract was let.
- The option of changing the scope of the contract should be considered from one contractor to a greater number.
- The limitations of the existing contract form were better understood and the limited opportunities to revise them were not considered substantive enough.
- A new, more knowledgeable and focused KHS senior management team was in place under the new Director, John Burr. There was a real desire for a significant step change in performance and value.

3.4 To undertake such an extensive exercise in 18 months would indeed be a significant challenge. This timescale was, however, non-negotiable due to the constraint imposed by the provision of winter service, needing to avoid starting a new contract during the mid winter maintenance season.

Procurement options

4.0 Several options were considered at the start of the procurement process, and others were discussed and selected during the process. The decisions made prior to procurement were:-

- The existing contract would expire on 31st August 2011 and a new contract would be let to start on 1st September 2011.
- A Competitive Dialogue process would be used. This allowed KCC to 'challenge' the market to provide improved solutions to some of KCC ideas and current/future challenges.
- A cost plus payment mechanism would not be used.

4.1 Decisions to be made during the dialogue process were:-

- Duration of the contract/possible extensions
- Payment mechanism
- Contractor incentives/penalties
- Scope of contract
- Use and payment of KCC owned depots
- KCC's option to procure outside of this contract (i.e. use of SMEs)
- Ownership of recycling process
- Areas of overlap, where would they best sit (i.e. with KCC or with the contractor)
- Performance management measures and targets

Process used

5.0 It was decided to go to the market for expressions of interest and from that list the 6 most appropriate companies were selected to engage in discussions. At this stage the current contractor was eliminated from the process on appraisal of their submission.

5.2 These 6 shortlisted companies: Atkins, Balfour Beatty, Carillion, Colas, Enterprise and May Gurney, were then invited to dialogue days where KCC officers and Members (Mr Manning, Mrs Tweed, Mr Prater, Mr Cubitt and Mr Chard; Mr Christie was also invited but was unable to attend) explored with each bidder the most appropriate solution to fulfil KHS's future vision. At two stages, these bidders were required to submit written proposals that were then assessed and those companies with the lowest marks were removed from the process. At each stage KHS selected positive proposals, in essence to 'cherry pick' the best ideas. These were built into the final document of KCC's requirements that was priced by the final 3 shortlisted companies.

5.3 As well as scoring their written submissions/proposals, each of the final 3 bidders had to open up their service to scrutiny with two of their existing clients so that KCC staff could experience their actual performance and operation, and discuss each company with their existing clients.

5.4 As well as these 'sanity check' visits, each of the final 3 bidders was asked to give a 30 minute presentation to a panel of senior KCC officers and four Members (Mr Sweetland, Mr Manning, Mr Hirst and Mr Robertson; Mr Christie was also invited but was unable to attend). The presenters were the Management Team that would run the KCC contract if they were successful. The presentation was followed by one hour of 'robust' questioning from the panel and each company was then scored. These scores were added to their separate scores for their priced document and their quality document.

<u>Decisions made and derived benefits</u>

6.0 Each decision made, no matter at what stage, had a specific targeted outcome or improvement.

Decisions (and derived benefits) during the dialogue process were:-

6.1 Payment mechanism

Existing - Cost plus.

New - Traditional schedule of rates.

Benefits - Easy to understand, administer and audit. Provides cost certainty and increased levels of client cost control. It also ensures that the risk for productivity and quality sits firmly with the contractor, unlike at present.

6.2 Contractor incentives/penalties

Existing - granting of possible contract extensions, target costing mechanism to share possible savings, achievement of partnership targets leads to a small performance bonus. There are no specific penalties for underperformance other than refusal to grant further extensions, there are also no links between profit and efficiency/productivity ***NB.*** *No performance bonus has ever been paid due to missed targets.*

New - granting of future years extensions for good performance, previously granted extensions can be withdrawn, contractor's 3% profit offset each month 'gambled' against achieving mutual performance objectives, contract can be terminated for any reason by KCC giving 12 weeks notice, works can be procured outside of this contract if desired by KCC.

6.3 **Benefits** - The new contract employs both the 'carrot and the stick', both in financial terms and contract duration terms. The sole purpose is to ensure that the contractor delivers a good service and continues to improve it on an ongoing basis. The more efficient the contractor is, the greater their financial return.

6.4 Ongoing value for money

Existing - Contractor's actual costs are reimbursed and KCC therefore pays what it costs the contractor. This is irrespective of levels of productivity, quality or contractor's cost control efficiency

New - each year the contractor is only awarded a set percentage (75%) of the inflation indices (compound year on year saving), KCC has the option to procure services outside of this contract if ongoing value can not be proved, easy to benchmark value against other highway authorities. Annual performance targets will be increased for contractor to achieve return of 3%

Benefits - a year on year financial compound saving, services can be procured outside the contract and value can therefore be benchmarked due to standard payment mechanism, contractor's performance must improve year on year if they are to recover their 3% profit from KCC (KCC retain profit if targets are not met).

6.5 Quantity of 'directly' employed staff

Existing - There is no current stipulation.

New - A minimum of 60% of employees engaged in providing these services must be directly employed by the contractor.

Benefits - Directly employed staff have a greater sense of ownership and accountability for the service they deliver, they are more likely to give a longer term commitment and as a result more likely to live in Kent. This requirement also reduces the amount of work that will be subcontracted thus avoiding unnecessary fee on fee situations.

6.6 Scope of contract

Existing - All highway maintenance, improvements and construction works with the exception of Major capital schemes & soft landscape, machine surfacing and find & fix has recently been undertaken outside of the contract.

New - similar to current, however machine surfacing is now formally excluded. KCC can now arrange for any works to be procured outside of this contract. KCC can also ask the contractor to undertake the design rather than just the construction (design & build).

Benefits - By letting one contract we ensure maximum buying power and value, it allows a greater amount of risk to be placed with the contractor and greatly improves works coordination and cooperation. By excluding machine surfacing the works will not be subcontracted and thus we avoid a fee on fee situation. KCC will now have a much greater procurement flexibility, thereby taking advantage of the most economic route and to support SMEs.

6.7 Use of and payment for KCC owned depots

Existing - the contractor has free use of the KCC and HA depots.

New - The contractor will use the existing KCC depots and pay rent to KCC at commercial rates.

Benefits - This ensures that the contractor will have a good coverage of the county and can respond to incidents in the appropriate time. It will be possible to benchmark contractor's rates on a like for like basis with other contractors, thus influencing our future procurement routes. KCC will not run the risk of 'subsidising' the contract should they undertake works for other clients

6.8 Recycling process

Existing - Waste and its recycling is undertaken by the existing contractor but is on the instruction and risk of KCC.

New - the contractor will be given responsibility for recycling/reusing all spoil.

Benefits - The contractor is financially incentivised to make maximum use of all excavated and waste materials, performance risk sits with the contractor.

6.9 Performance management measures and targets

Existing - A selection of OPIs are measured, these are mainly of a traditional output type.

New - These will be a combination of output and outcome targets and will be revised each year to make them more challenging.

Benefits - The contractor will share KCC's own measures of success and will be incentivised to achieve them. Success is celebrated together and continuous improvement becomes the norm.

6.10 Support KCC's apprenticeship scheme

Existing - There is no current link.

New - A minimum of 3% of the employees involved in delivering the services shall be delivered by an employee on a formal apprenticeship programme.

Benefits – Increased use and development of talent and skills**.**

6.11 Duration of the contract

Existing - 5 years, extendable to a maximum of 10 years

New - 5 year, extendable to a maximum of 10 years

Benefits - The duration is long enough to allow the contractor the opportunity to recover capital invested, but short enough for the contractor to know that end (without an agreed extension) is not very far away, and thus keep motivated to perform to a good standard. This duration is very much the industry standard.

6.12 Eligibility for extensions

Existing - at discretion of KCC. Extensions can be added.

New - at the discretion of the KCC, however extensions can be removed as well as added.

Benefits - This provides the incentive for the contractor to perform consistently. The client maintains full flexibility on whether to grant an extension, previously granted extensions can be removed for poor levels of service.

Balance/ownerships of risks

7.0 The decisions detailed above have a significant impact on the transfer of risk when compared to the existing cost plus arrangement. These are :-

Risk	Owner under new contract	Under Existing contract
Quality of work	Contractor	KCC
Productivity	Contractor	KCC
Profitability	Contractor	KCC
Workload/turnover	Contractor	KCC
Resource availability/suitability	Contractor	KCC
Reputation	Contractor & KCC	KCC
Accident claims	Part contractor, part KCC	KCC
Deliver to time/budget	Contractor	KCC
Inflation	Part contractor, part KCC	KCC

7.1 Risks are best placed where they can be best managed. They are useful in that they often provide incentive/reward if managed appropriately, failure to do so leads to some form of penalty (often financial or contractual).

7.2 By placing the key risks of quality and performance with the successful bidder (i.e. KCC will only pay for good quality works that meet its requirements), KCC is confident that substantial cost savings will be achieved and KCC's reputation for highway works will improve.

Assessment of the final 3 bidders (the result)

8.0 A 13 month, extensive and robust process was used. Corporate Procurement and a selection of senior Members, in addition to key EH&W and KHS staff were also used. This involvement allowed the process, at all stages, to remain focused on the paramount issues, namely improving quality at a better price, both now and in the future.

8.1 The 4 evaluation criteria (approach to service delivery, Legal and commercial, Social and price) were assessed by separate groups and were not shared until all 4 areas had delivered their scores.

8.2 **The lead bidder is 'Enterprise'**, with May Gurney and Colas coming joint second. More details are set out in the attached appendix.

8.3 **Financial benefits to KHS/KCC**. The current assessment of the lead bidder's prices confirms that they are both extremely competitive *and* sustainable.

8.4 Savings from this procurement exercise were included in the MTFP and indications are that this commitment will be met.

The next stages

9.0 Whilst the important stage of lead bidder has now been reached, this does not signify the end of the procurement process. There is still a month or so of intensive work to be undertaken to get the contract to a point where it can be signed. There will be frequent meetings with lead bidder (who will become the preferred bidder subject to the decision of Cabinet today) to discuss a variety of outstanding matters, such as:-

- The mobilisation and demobilisation plan – this is vital to ensure a seamless handover from the existing service contractor to the lead bidder on 1st September. A mobilisation duration of 6 months is normally ideal; we believe we can do it in 3–4 months. This must be achieved due to the winter maintenance requirements
- Resolve any/all small anomalies from within the bid and supporting documentation
- Agree a joint training plan and performance targets
- Formalise other agreements, such as depot leases, etc

9.1 All of this, once achieved, will allow 'stand still letters' to be issued to the unsuccessful bidders and notification to be given to the preferred bidder of the intention to award them the contract. Only after the standstill period has elapsed can KCC formally enter into the contract with the preferred bidder.

The legal implication

10.0 The process for procuring the new contract has been delivered in accordance with Regulation 18 of the Public Contracts Regulations 2006 (as amended). The Council's Legal and Procurement departments have acted as advisors on the process and to date it has been sufficiently robust and transparent and the

Council does not expect any legal challenges when appointing the lead bidder.

10.1 If the procurement recommendation were not to be accepted, the process may need to be restarted in its entirety and the current contract would need to be extended (assuming agreement can be reached) by 12–18 months to allow for this.

Conclusion

11.0 To reach this stage, the County Council has undertaken a rigorous tendering exercise in accordance with the necessary procurement procedures. Following a robust evaluation of the submitted tenders the clear conclusion is that "Enterprise" has the necessary resources and skills to satisfactorily deliver the terms of the contract and is therefore the recommended Preferred Bidder.

12.0 Background Documents - None

RECOMMENDATION

1. Cabinet is invited to confirm:

- **that Enterprise be appointed the 'Preferred Bidder' for the provision of the new Kent Highway Services Contract to Kent County Council as described in this report**
- **Subject to them being satisfied to the detailed terms and conditions, the Corporate Director for Enterprise and Environment and the Director of Governance & Law be authorised on behalf of the County Council to enter into a contract with the 'Preferred Bidder'.**

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