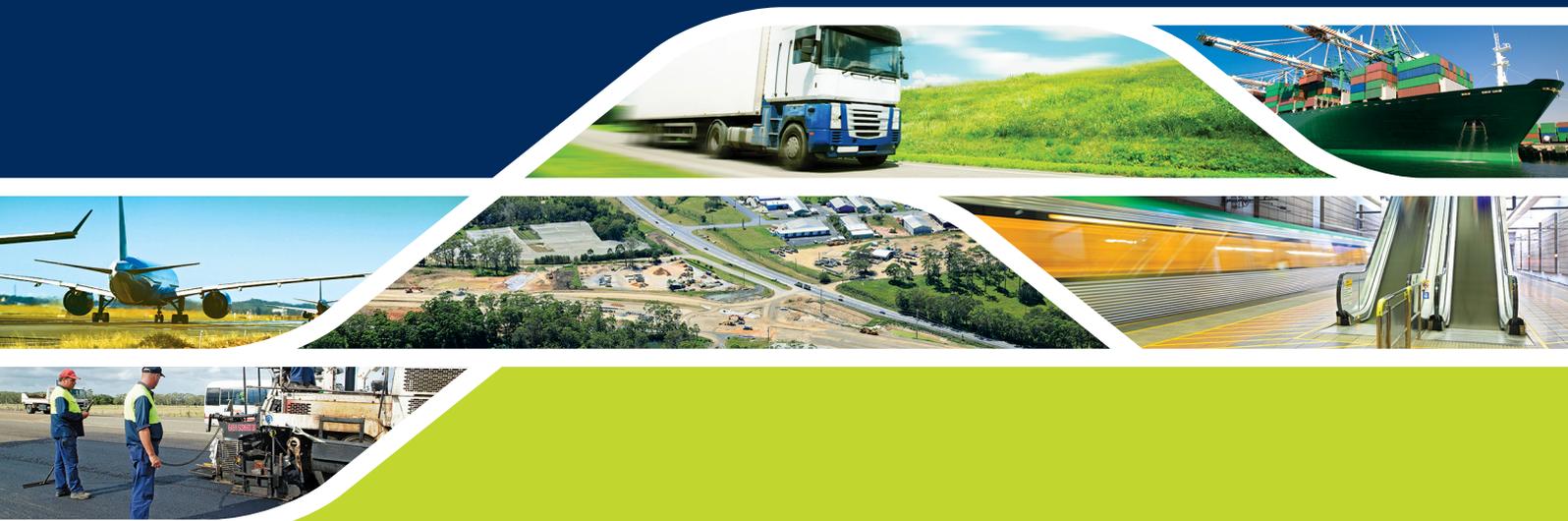




Australian Government

Department of Infrastructure and Regional Development



National Framework for Traditional Contracting

The Guide
Good Practice and
Commercial Principles
for Traditional Contracting

September 2015



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Note

Governments in each jurisdiction will have their own individual approval processes for capital investment projects, as well as policies (e.g. probity) and legislation that will impact on all capital works delivery. These overarching jurisdictional requirements are precedent to the practices covered in this document.

Acknowledgement

This document has been prepared under the sponsorship of the Inter-jurisdictional Steering Committee for Alliancing & Traditional Contracting with membership from:

- Department of Treasury and Finance, Victoria (Chair)
- Treasury, New South Wales
- Treasury, Queensland
- Department of Treasury and Finance, Western Australia
- Department of Infrastructure and Regional Development, Commonwealth of Australia

The preparation of this document was led by the Victorian Department of Treasury and Finance with Evans & Peck Pty Ltd Level 2, 555 Coronation Drive Toowong, Queensland 4066.

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1 Introduction to the Framework

This Chapter describes the purpose and structure of the Framework for Traditional Contracting of Infrastructure and this Guide as the overarching document in the Framework.

1.1 Purpose

The purpose of the National Framework for Traditional Contracting of Infrastructure (the 'Framework') is to assist Clients using Traditional Contracting to procure infrastructure to deliver on government's expectations and to engage the market in the most effective and efficient way.

This framework will assist practitioners in understanding and applying good practice, however these practices are not mandatory. Each practitioner is expected to apply their own judgment within the requirements of their jurisdiction when tailoring the practices to each specific project.

For many years, Traditional Contracting has been the dominant method used to procure infrastructure projects with the primary characteristic being the transfer of construction, and sometimes, design risk to the Supplier. As the construction industry evolved, other procurement models such as Public Private Partnership (PPP), Alliance and other forms were developed and used, hence the term 'Traditional Contracting'. Some have held a misinformed view that Traditional Contracting was an undesirable procurement model that resulted in adversarial behaviour and disputes. However, just as PPP and Alliancing evolved, so too has Traditional Contracting, and it continues to be a very effective procurement model when used properly.

During 2011, the Victorian Department of Treasury and Finance undertook research resulting in the publication of *'Towards Agreed Expectations – Tender strategies to improve D&C infrastructure outcomes'*¹. This research identified the following five (5) improvement areas that would make a significant difference to outcomes achieved by public sector Clients undertaking Traditional Contracting for infrastructure projects:

- Consistency of Client practices across jurisdictions, particularly in the Tender Phase;
- Project Definition and Scope parameters;
- Project Budgets in Business Cases;
- Governance and contract management, with a focus on the relationship between the Client and the Supplier; and
- Continuous improvement and performance.

¹ Refer to: www.dtf.vic.gov.au/project-alliancing

The principles and practices described in this Guide are written from the perspective of a standalone major infrastructure project (say \$50M or more) procured through traditional contracting models.

Nevertheless, many principles and practices also apply to infrastructure programs, and some will apply to other procurement models (ie non-traditional contracting and indeed to non-residential building projects).

Similarly, principles in the Guide will apply for less complex, lower value projects, however, the practices described may be sensibly scaled down to a level appropriate to the project.

This research was further informed by a study tour to the United Kingdom where Supplier, Client and Investor practices were assessed and provided the additional concept of the importance and benefit of the Client acting as an ‘intelligent Client’². For example:

- Achieving best in market tender prices through good tender preparation and practices that attract the best Suppliers and avoid any ‘bad Client premium’;
- Delivering project outcomes that meet the expectations set with the government at Business Case approval and Contract Award; and
- Improving industry productivity and sustainability.

The Framework is characterised by practical guidance that is ‘implementation ready’. The research is based on qualitative analysis through in-depth interviews and workshops to identify causal factors and practices. The analysis was followed by synthesis of best practices and tested in workshops and projects with practitioners from government delivery agencies, government ‘investor’ agencies and service providers, industry, and advisors. This synthesis relied on the best available evidence, the requirements of decision makers; and the knowledge, understanding and wisdom of experts in the area.

This Guide addresses...	This Guide does NOT address...
<p>Traditional contracting using Design & Construct (D&C) is the default method addressed in this Guide as it is the most commonly used for large infrastructure projects; and secondly the Construct Only (CO) method by exception where a different practice may be required.</p>	<p>Traditional contracting models other than D&C and CO are not addressed comprehensively, however differences are highlighted where material and relevant.</p> <p>Project selection and cost-benefit analysis.</p> <p>Procurement options analysis.</p>
<p>Infrastructure Projects</p>	<p>Building Projects</p>

² The expression ‘intelligent Client’ is often used in the UK, although one common definition is not evident. The discussion in this Guide picks up on the themes frequently used in the context of UK procurement discussions.

1.2 Who should use the Framework

This Guide is intended to be used primarily by government practitioners, either in delivery agencies (Clients); or central government departments (Investors) when developing intra-jurisdictional guidelines and policies. Additionally, it is expected that industry (Suppliers) will also benefit from more consistent practices by Clients across jurisdictions.

The target audience is both experienced and new practitioners and does not presume significant knowledge.

In using this Guide, practitioners should note that a primary objective of the Guide is to establish consistently good practices across jurisdictions. Consistency can only be achieved through a common understanding of foundation concepts (and terminology) and these are explained to ensure that all readers have this common understanding.

1.3 Structure

This section describes the structure of the Framework and the structure of this overarching Guide.

1.3.1 Framework

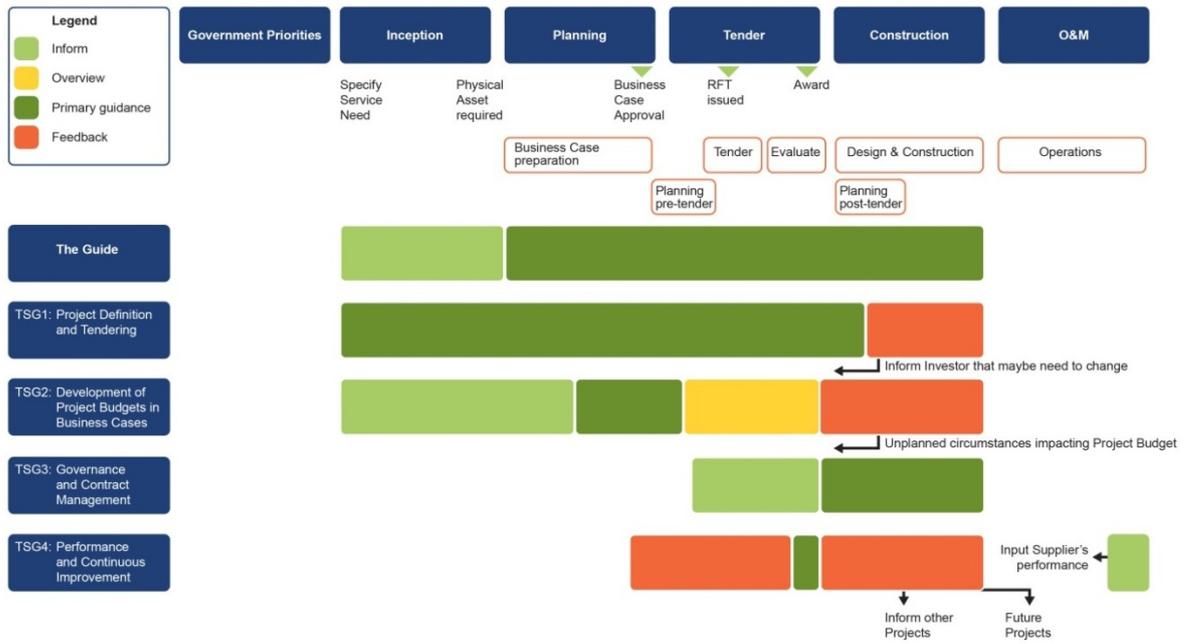
The Framework comprises 5 documents:

1. The Guide: Good Practice and Commercial Principles for Traditional Contracting.
2. Topic Specific Guide 1: Project Definition and Tendering
3. Topic Specific Guide 2: Development of Project Budgets in Business Cases
4. Topic Specific Guide 3: Governance and contract management
5. Topic Specific Guide 4: Performance and continuous improvement

Collectively, these 5 tasks are published as the '*National Framework for Traditional Contracting of Infrastructure*'.

The structure of the Framework and the relationship of the Topic Specific Guides to the key activities undertaken through the typical project lifecycle are depicted in Figure 1.

Figure 1 Structure of Framework and relationship to project lifecycle activities



1.3.2 Structure of this Guide

This document (the 'Guide') provides guidance on selected good practice and commercial principles to achieve improved project outcomes. This Guide forms the overarching document in the *National Framework for Traditional Contracting of Infrastructure*. It is intended to provide high level principles and commercial practices with more detailed and focussed guidance provided through the supporting four Topic Specific Guides.

This Guide is structured as follows:

Introduction to the Framework and Traditional Contracting

- Chapter 1: Introduction to the Framework
- Chapter 2: Traditional Contracting Fundamentals

The Government's Expectations at the Portfolio level

- Chapter 3: Industry productivity and sustainability

The Government's Expectations at the Project (Business Case) level

- Chapter 4: The Four Critical Success factors

Appendices

Key points are highlighted by two types of text boxes:



Overview of chapter



Practice and commercial insights

1.4 How and when to use this Guide

Whilst there is no ‘one size fits all’ solution to the delivery of complex infrastructure projects, the principles and practices set out in this Guide provide a basis for optimising project outcomes when using Traditional Contracting, with an emphasis on meeting governments’ expectations.

This Guide has been developed on the basis that practitioners apply their own general jurisdictional policies and guidelines to procurement planning, infrastructure delivery and government decision making. It does not seek to be an encyclopaedic documentation of the subject matter, rather a ‘deep dive’ into specific topics which have been identified through the research as those that will have the most material impact on improving project outcomes in the contemporary Australian public sector context.

This Guide does not provide guidance on project selection or procurement options analysis. It is presented on the basis that the Client has already undertaken analysis of:

- alternative options for meeting the service need, including the enhanced use of existing infrastructure, pricing solutions and cheaper build options;
- appropriate procurement options for any necessary assets or services, including the appropriate contract structure (i.e., design and construct, alliance, PPP); and
- possible savings from packaging projects into smaller components.

The Guide can be applied at any point in the project planning and delivery lifecycle, however, ideally it will be used at the beginning of project planning when good practices can have the highest impact on project outcomes.

In some circumstances it may be appropriate to depart from the practices described in this Guide. A Client always has the flexibility to determine and recommend practices which are efficient, ‘fit for purpose’ and best suited to achieving a value for money outcome for their specific project.

The Guide has been prepared on the basis that practitioners already have:

- a good understanding of the terminology and general principles set out in the following chapters;
- familiarity with the relevant Acts and other jurisdictional policies and guidelines;
- some exposure to procuring and managing traditional contracts;
- an understanding of the practical challenges of prevailing market conditions that impact public sector infrastructure projects; and
- specialist professional service providers (sourced internally or externally) to assist them to deliver projects in accordance with this Guide.

1.5 Relationship with existing policies and guidelines

The Framework provides best practices (not policy) as a resource that individual Australian jurisdictions can use to inform their policy and guideline development for Traditional Contracting of infrastructure; or for project client agencies to reference as a benchmark for their practices where corresponding jurisdictional guidelines do not exist. Where there is a conflict in the guidance of this Framework and jurisdictional policies and guidelines, the jurisdiction's position will take precedence. This Framework will sit alongside those National Frameworks already separately published in Australia for PPPs and Alliance Contracting.

It is expected that practitioners are familiar with their relevant jurisdictional policies and guidelines which are not repeated or referenced in this document.

1.6 Updates to the document

Updates to this Guide will be published from time to time on the Department of Infrastructure and Regional Development website:

<http://www.infrastructure.gov.au/infrastructure/nacg/index.aspx>

2 Traditional Contracting Fundamentals

This Chapter describes the fundamentals of Traditional Contracting as a context for the principles and practices described in the Guide.

2.1 Overview

Across Australia, there are a variety of organisations involved in the contracting of a range of infrastructure projects; consequently there is a broad range of terminology in use. Whilst acknowledging the necessity for industry and jurisdiction specific language, the following sections provide the definitions used for the purposes of this Guide.

A highly valued form of contracting

“Traditional Contracting always offered great value for Investors, Clients and Suppliers. Over many years we have experimented with different contract models which have risen and disappeared but Traditional Contracting endures and is commonly the best way forward for most infrastructure projects.”

UK Senior Industry Executive
October 2012

2.2 Key concepts

2.2.1 Traditional Contracting

In the context of the Framework, Traditional Contracting refers to those contracts that to varying degrees allocate construction and design risk to the Suppliers (but are not Alliances or PPPs). The two primary categories of Traditional Contracting are Construct Only (CO) and Design and Construct (D&C). Whilst recognising the myriad of variations in use for individual contracts, the salient features are:

- **Construct Only (CO):** the Design has been undertaken by the Client and the Supplier is responsible for constructing the works to the Client’s design. The tender process is primarily focused on achieving the best (outturn) price for constructing the Client’s design. Design innovation by Suppliers is not a primary consideration however construction innovation may be possible. The contract takes the form of a Schedule of Rates or a Lump Sum contract. Generally the Supplier is allocated the construction risk only.
- **Design & Construct (D&C):** generally a limited design has been undertaken by the Client who then invites potential Suppliers to tender on the basis of completing/improving the Client’s design and constructing to that design. The tender process is usually directed to encouraging innovation by Suppliers and thereby achieving the best outturn price for the same functional performance as the Client’s limited design. The D&C tender process aims to minimise interface risks between design and construction processes. Typically all design risk as well as construction risk is allocated to the Supplier.

Collaborative procurement models (e.g. Early Contractor Involvement or 'ECI')

Models such as ECI use a collaborative Tender Phase in which the Supplier collaborates with the Client (to varying degrees) to develop a tender response for the Construction Phase of a project. Generally the Construction Phase is then undertaken using Traditional Contracting such as D&C with a risk adjusted lump sum contract. ECI is dealt with under the National Alliance Contracting Guidelines and is not addressed in this Guide.

Traditional Contracting does not require close 'joint management' between the Client and Supplier nor decision and risk sharing (as in an Alliance) nor does the Supplier need to secure funding and provide a service following project completion (as in a PPP). On completion the Client is responsible for the operation and maintenance of the asset. These high-level differences in procurement models are summarised in the following table. Traditional Contracting, especially D&C, can be used and is used for large complex projects.

Whilst collaboration in traditional contracting processes is strongly supported³, the practice of combining elements of collaborative contracting models into traditional forms of contract should only be done with great caution given that it involves untested practices which are isolated from the core contracting context and dynamic and may have unintended consequences. This should be done as an exception requiring mature and experienced analysis to ensure that there are net benefits. In particular, the Client should be cautious of accepting greater exposure to design and/or construction risks compared to past practice without a compensatory reduction in tender price.

³ See section 2.2.5

Table 1 Comparing the primary contract options for infrastructure contracts

	Alliance	Traditional Contracting (D&C)	Public Private Partnerships
<i>Caption</i>	Risk sharing for procuring capital assets	Risk transfer* for procuring capital assets	Risk transfer* for procuring services
<i>What risks</i>	Not all risks can be dimensioned upfront and are best managed jointly	Clear and enforceable risk allocation	Clear and enforceable risk allocation
<i>Who takes what risks</i>	Risk exposure is 'shared' (the Government's financial exposure is uncapped; the private parties often have capped exposure)	Risk for design and construction is largely allocated to the Supplier together with the interface risk between design and construction.	Supplier exposed substantially to risks of design, construction, capital assets ownership and service KPIs (& sometimes demand risk)
<i>Who takes ownership risk of the asset</i>	Following construction, the government owns and operates the facility to deliver the service promised in the Business Case.	Following construction, the government owns and operates the facility to deliver the service promised in the Business Case.	Following construction the Supplier owns & operates the facility for a defined concession period and delivers the services promised in their tender.
			
	Risks are undimensionable & shared		Risks are well known & mostly transferred

*Risk transfer based on risks allocated to the party best able to manage and control that risk at the least cost.

For clarity, the principles and practices described in this Guide will use D&C rather than CO as the example model when discussing Traditional Contracting, with any unique requirements of the CO model identified by exception. Generally, the practices and principles represent good practice when using any of the Traditional Contracting models and in many cases has application in all procurement.

Traditional Contracting

Like many terms in the infrastructure industry, the term 'Traditional Contracting' may have different meanings for different people. It can mean:

- Traditional – in the sense that traditionally Suppliers (Contractors) self-performed the majority of their work;
- Traditional – in the sense of any contract other than Alliances and PPPs (including, for example, Construction Management, EPCM, Project Management, as well as CO and D&C);
- Traditional – in the sense of those contracts based on long standing (traditional) forms of contract (e.g. AS2124).

For this Guide the use of the term 'Traditional Contracting' refers to D&C and CO forms of contract as these together with Alliances and PPPs collectively account for the delivery of the majority of significant infrastructure projects.

2.2.2 Infrastructure

The term 'infrastructure' can be applied to a wide range of project delivery services or systems required for a community and wider society to function.

In the public sector, the term 'infrastructure projects' generally refers to non-building projects and almost always involves major organisations in their delivery. These assets are generally integrated in a network of other infrastructure assets (in both urban and rural environments). There is usually a high interface with the natural environment and use of naturally occurring materials which makes defining and managing them highly variable. This inevitably gives these projects a comparatively high risk profile. They are largely heterogeneous and often have not been done before or have uncommon critical elements; consequently benchmarking costs can be difficult.

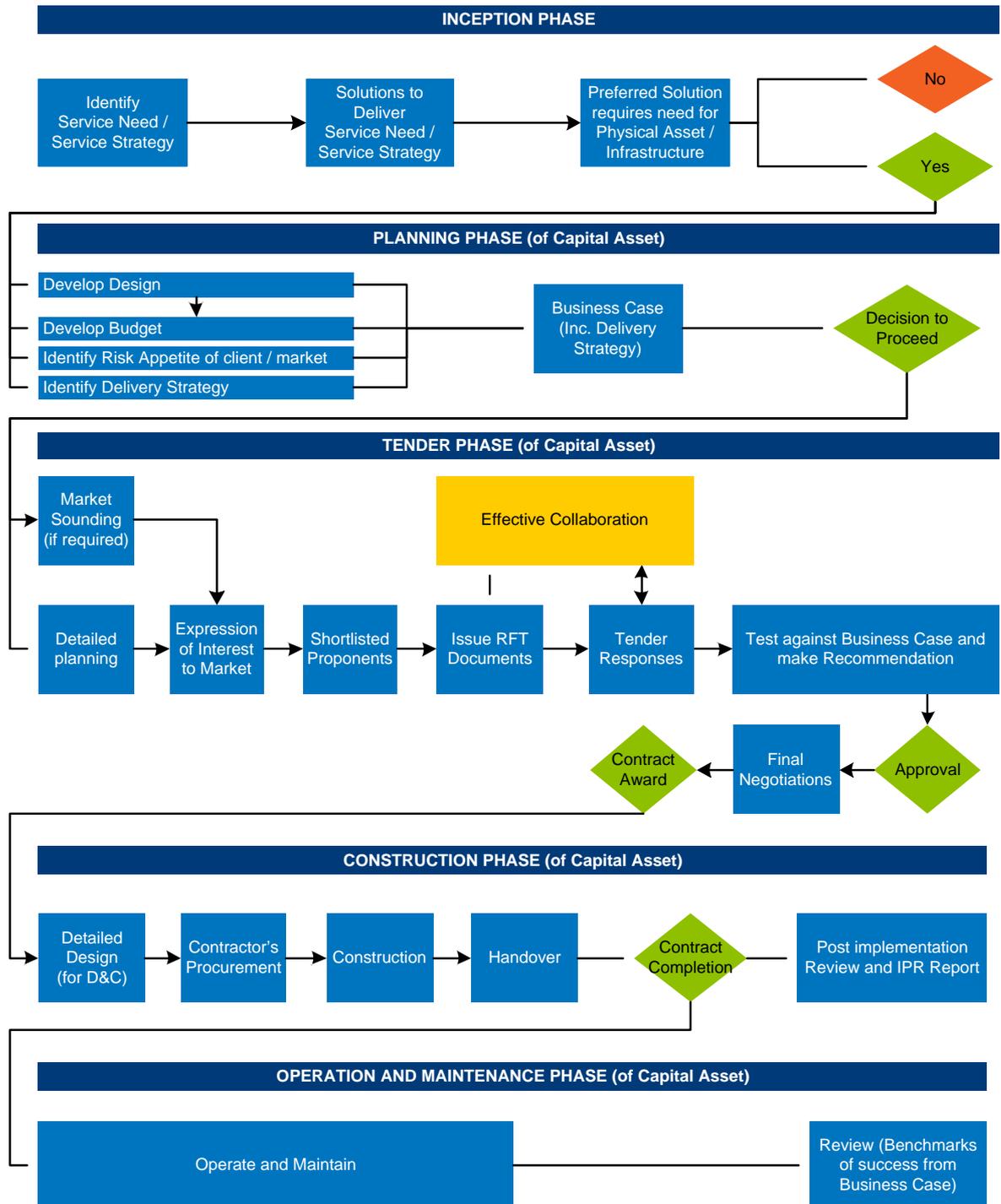
These factors require that if the Investor's expectations (described in the Business Case) are to be met, much rigour must be applied to the planning of infrastructure projects (particularly at Business Case stage).

2.2.3 Project Lifecycle

Every project is developed through a number of defined phases from the very early identification of the need for a service, through to operation of a finished asset.

Across jurisdictions there is a range of 'lifecycle' descriptions. For the purpose of this Framework a 'generic Project Lifecycle' is used which reflects the various jurisdictional versions and provides a common basis for the content of this Guide and the Framework overall. This generic Project Lifecycle is shown at Figure 2: D&C project lifecycle (noting that not all steps are used on all projects). The Project Lifecycle includes the operational life of the asset, reflecting the whole of project aspects that must be considered at each stage of the lifecycle.

Figure 2: D&C project lifecycle⁴



⁴ Sourced from 'Towards Agreed Expectations – tender strategies to improve design and construct infrastructure delivery outcomes, Department of Infrastructure and Transport, Australian Government, June 2012

Procurement and Tender

There is sometimes confusion in the use of the terms 'Procurement', 'Tender' and 'Delivery' to describe how a capital asset is provided.

'Procurement' is an encompassing term referring to the planning, tendering and delivery stages of the project.

'Tender' is a more specific term referring to the market engagement stages commencing (usually) with the first release of tender documentation (eg Expression of Interest) up to awarding a contract for construction of the work (contract award) by the Supplier.

'Delivery' refers to the performance of contractual obligations following contract award (including design and construction activities, and where contracted, operation and maintenance).

2.2.4 Roles

The terminology used to describe the roles or participants in Traditional Contracting will depend on the context of the particular project lifecycle stage. Therefore the following definitions should be considered in the context of the situation and stage of the development.

Table 2 Definitions used in this Guide

Role	Description
Government or Investor	The entity responsible for providing and/or approving the financial outlay (and taking the financial risk) to deliver the asset and approving the investment at defined stages in the project lifecycle. The Business Case provides the basis on which the investment and funding decisions are made.
Delivery Agency or Client	The entity that is responsible for developing the Business Case and, if approved by the Investor, for managing the delivery of outcomes within the defined parameters set out in the approved Business Case. This is the entity which manages the Planning, Tender and Construction Phases , engages with the market; and is the Supplier’s contracted counterparty.
Supplier, Contractor or Tenderer	Organisations in the relevant market which may be involved in tendering for the work and subsequently the design, construction or maintenance of the asset.
Superintendent	The Superintendent may be an employee of the Client or may have a general commercial relationship with the Client beyond its role under the construction contract. The Superintendent may perform a ‘certifying role’ involving assessing and approving various claims e.g. extension of time for practical completion, adjustments, payment certificates or other functions as an agent of the Client, however, when performing its functions the Superintendent may be required by internal delegations or policies of the Client to obtain consent of, or act under the direction of, personnel of the Client or to give effect to particular policies or internal directions of the Client. The Superintendent may also give directions to the Contractor requiring the Contractor to comply with a provision of the Contract and has access to the site and the works under the Contract.
Advisors	Advisors are appointed by Investors, Clients and Suppliers to supplement their internal capability and provide market awareness and experience. Advisory support can be required in different fields and at different times in the project lifecycle and include commercial advice, specific technical support, legal advice and input or probity advice.

Refer to Appendix C: *Roles during project phases* for more detail.

2.2.5 Collaboration

To be an ‘intelligent Client’, the Client must establish a collaborative relationship with the Supplier which allows an effective exchange of ideas and information leading to a shared and deep understanding of what the Client wants and what the Supplier offers. This collaborative relationship provides a platform for early identification of any misunderstandings or issues and timely and pragmatic resolution of those issues. The Client cannot collaborate alone, and the

Supplier must also contribute to establishing a collaborative relationship with the Client. The Client and Suppliers (the shortlist) have the opportunity to establish this relationship in the Tender Phase when the Client engages the market. When the Client and Supplier have an ongoing relationship or the potential for one (in future projects), the motivation to collaborate is high and the Client should use this motivation to achieve effective collaboration. This topic is addressed in more detail in *'Towards Agreed Expectations – Tender strategies to improve D&C infrastructure outcome⁴'* and *National Alliance Contracting Guidance Note 6 – ECI and other Collaborative Procurement Models⁵*.

Collaboration Demystified

1. Collaboration is an essential feature of any effective commercial relationship between a Client and a Supplier.
2. Effective collaboration does not occur because it is required by the contract but because of the leadership and capability of both participants wishing to achieve a common outcome whilst recognising that each participant has different business objectives.
3. Collaboration is a means to achieving a mutual goal and is not an end in itself.
4. Collaboration is enhanced when the parties have an expectation of an ongoing relationship beyond a single event or project. Best for project decisions are more likely in a repeat relationship than the self-interested decisions in a single transaction.
5. Collaboration is not a substitute for competition, poor planning or inadequate Client capability; nor does effective collaboration require financial incentive or dilution of effective project risk allocation.
6. Collaboration between the Client and the Supplier does not change the nature of the underlying contract.

National Alliance Contracting Framework: *Guidance Note 6 (ECI and other Collaborative Procurement Models)*

2.2.6 Government Procurement

Government seeks to observe high ethical standards and conduct in commercial transactions. Government and public officials must be able to demonstrate high levels of integrity and transparency in processes while pursuing Value for Money (VfM) outcomes in the public interest. However, it is important to ensure that the particulars of the probity rules protecting these high levels of integrity and transparency do not unduly overly inhibit the achievement of policy outcomes.

^{4, 5} <http://www.dtf.vic.gov.au/Infrastructure-Delivery/Alliance-and-traditional-contracting>

Probity in Procurement

... excessively tight rules on probity — a form of inefficient or excessive risk aversion — can inhibit the selection of the best tender and perversely increase the risks to government. The main purpose of probity rules is to ensure that the selection process for constructors is genuinely based on merit. However, particular ways of achieving due diligence can increase the time and costs of procurement processes, and frustrate superior procurement options for some projects (page 27).

Productivity Commission Inquiry into Public Infrastructure

Final Report, July 2014

A standard requirement for the public sector when procuring infrastructure is contestability and competition. These requirements are the foundation of public procurement and the building blocks of VfM outcomes. The inclusion of contestability and competition in procurement processes strengthens incentives to innovate and provides the most effective way of ensuring and demonstrating that taxpayers get the required service outcomes at a fair cost (i.e. best-in-market pricing for the required supply at specified metrics of performance/quality).

In relation to contestability requirements, departments and public bodies are required to make reasonable attempts to seek a wide field of tenders or quotations for public construction services. In some rare cases, where it is not possible to achieve full competition or contestability, the Client may face a premium in the absence of competitive Tenderers.

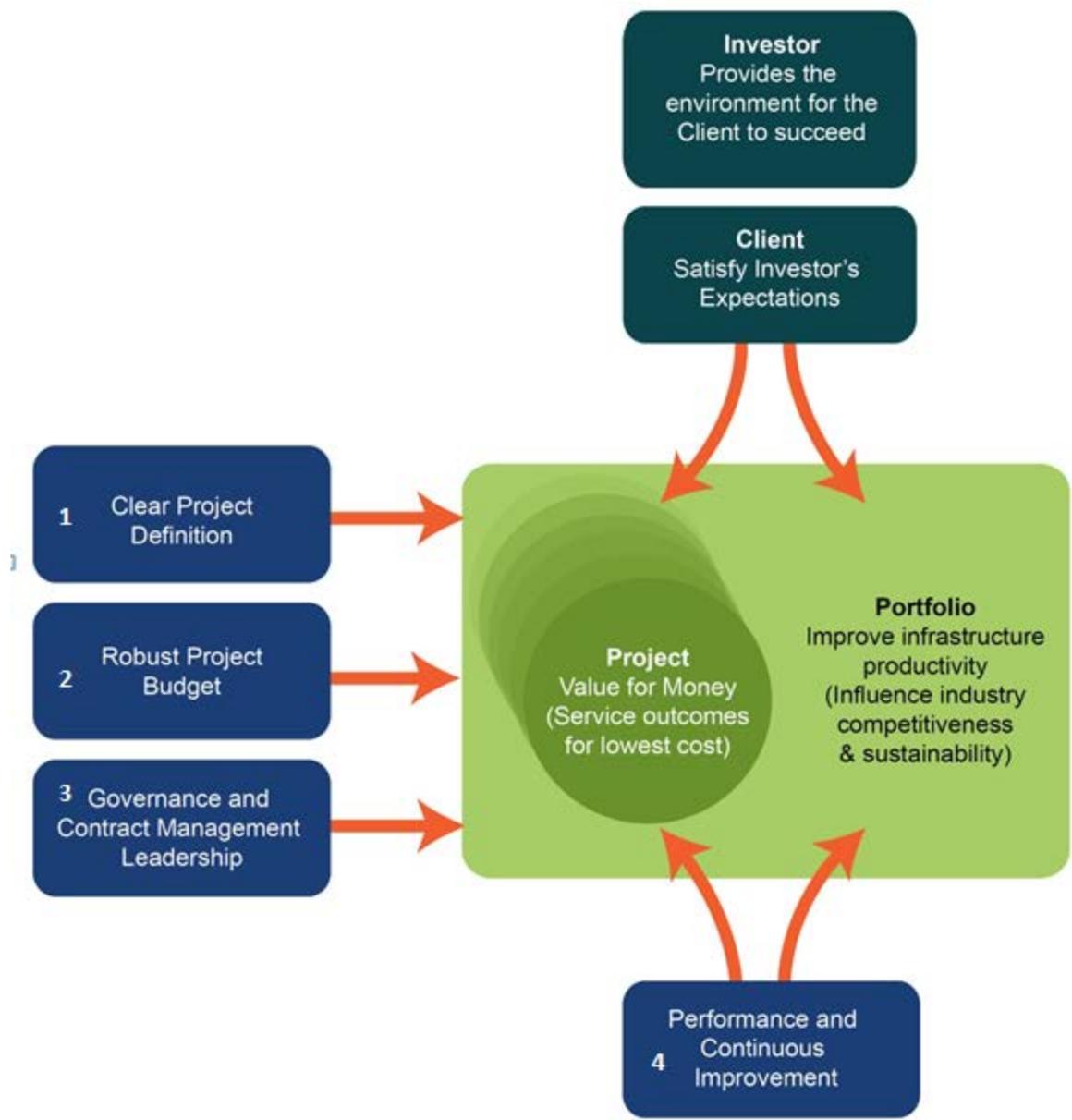
2.3 Traditional Contracting success factors

The findings from the research (Refer Section 1.1, Appendix B: References, and Appendix D: Schedule of Consultation) suggested the following ‘success factors’ that position an ‘intelligent Client’ to meet government expectations not only on a project by project basis but also on a portfolio of projects basis. These are described below:

7. On a **portfolio of projects** basis, over the longer term, the intelligent Client will attract the best performing Suppliers and reduce the cost of infrastructure to the government by positively influencing industry competitiveness and sustainability through:
 - Understanding the value of its unique market position as a blue-chip, large, repeat buyer to improve behaviours and performance outcomes for itself and its Suppliers;
 - Shaping thought leadership in how it procures infrastructure;
 - Managing long term Client/Supplier relationships; and
 - Capturing and sharing Supplier’s past performance.
8. On a **project specific** basis, where the Client’s objective is to deliver the desired project requirements for the lowest cost, the following factors have been identified as those with the greatest potential to improve project outcomes if better practices were employed more consistently by Clients:
 - Developing a clear Project Definition;
 - Developing a robust Project Budget;
 - Providing Governance and Contract Management; and
 - Driving performance and continuous improvement.

These success factors are illustrated in *Figure 3 National Framework – four critical success factors*.

Figure 3 National Framework – four critical success factors



Size and the 'intelligent client'

Being a large repeat client that dominates a market segment does not automatically translate to being an 'intelligent client'.

Indeed, such market dominant clients are sometimes exploited as 'cash cows' and their shortcomings are not openly referred to by Suppliers.

As a Senior Consultant, specialising in benchmarking the cost of civil engineering and process engineering projects stated in September 2011:

"Even experienced private sector clients with a high value project book are surprised to hear that bidders will add a premium to their contract price. Organisations that are a 'difficult to deal with client' will attract an additional special margin. This can be 20%, and in some cases even more."

3 Continuous Improvement and Sustainability

This Chapter describes the practices and principles that a Client should undertake to set the foundation for improving industry productivity and sustainability across its portfolio and across government's portfolio.

As stated above, an 'intelligent Client' is able to attract the best performing Suppliers and reduce the cost of infrastructure to the government by positively influencing industry competitiveness and sustainability.

Being a good Client and a good Supplier in long term, repeat relationships

A good Client and a good Supplier help each other to become better. In a long term, repeat relationship, both the Client and Supplier benefit by collaborating to improve. The Client will become better at engaging with Suppliers and describing what it wants. The Supplier will become better at engaging with Clients and responding to what the Client wants. Both will help each other become more efficient and effective Clients and Suppliers. In particular, Clients should not need to rely on financial incentives to get high performance from Suppliers where this potential exists.

"True success occurs when both the Client and the Supplier achieves their objectives."

Senior Officer, UK Central Agency

3.1 Understand value of being a blue-chip, large, repeat buyer

In the procurement of major infrastructure projects, government is a large, potentially attractive, repeat buyer and has the opportunity to use this position to structure high quality procurement processes.⁶

This potential for a repeat relationship can result in a shift from a transactional self-centred relationship to a strategic value relationship, where positive dealings are highly significant to both Client and Supplier success, as illustrated in Figure 4 *The positioning of Clients in market relationships*.

Figure 4⁷ The positioning of Clients in market relationships

High Value Contract	<p>Development Potential</p> <p>'Opportunity to sell'. While not seeing the organisation as one of its key Clients, the Supplier does see significant value in winning and/or growing the business and will work to this end. Supplier will negotiate and offer good deals.</p>	<p>Strategic Relationship Opportunity</p> <p>'The Client is a key to our growth and future'. Suppliers will work very hard to gain and/or retain the organisation's business and look to build strong relationships with the organisation. Supplier will be willing to give its best deal.</p>
Low Value Contract	<p>Nuisance</p> <p>'The Client is a pest'. Supplier indifferent to the organisation as a Client and gives low attention to winning its business. Supplier is not interested in negotiating on service or price.</p>	<p>Exploitable Opportunity</p> <p>'The Client is part of our bread and butter base'. The Supplier is interested and will readily accept the business from the organisation, but generally on its terms, with little room for negotiation.</p>
	Low Potential for repeat relationship	High Potential for repeat relationship

Government is often the dominant, blue chip, high value strategic Client for infrastructure Suppliers, however this does not mean all government agencies will have a strategic relationship with those Suppliers. When the Client's corporate memory does not transfer from project to project, and the Client allows itself to be treated as a 'nuisance' or as an 'exploitable opportunity' (with no adverse consequences for the Supplier's business outcomes), resulting in the Client not achieving the potential it could from its market position.

A common scenario of this behaviour is when a Supplier bids low with the intention to win the contract and then becomes adversarial and sub-performs to achieve their required profit targets. This behaviour is effectively encouraged if Clients do not hold Suppliers to account by factoring this behaviour into the selection criteria when evaluating Tenders for the next contract⁸. In the worst case scenario, the Client is effectively allowing its Suppliers to treat it as a 'nuisance' or 'exploitable opportunity'.

"I also have a nagging philosophical problem with the use of incentives in contracts, which goes beyond the simple fact that they don't work. I believe the offering and taking of incentives fundamentally disrespects the professionalism of contractors. What incentives are really saying is, "Because you, the contractor, won't do a good, honest job just for your fee, I need to bribe you with some contingent money based on whether you actually show up for this job (page 288)."

Ed Merrow; Industrial Megaprojects: Concepts, Strategies, and Practices for Success, Wiley, 2011

⁷ Figure 4 has been adapted from Department of Treasury and Finance (Victoria) *Good Practice Guidelines: Developing a State Purchase Contract Business Case*, Melbourne, 2006; and Government of Queensland, Queensland Purchasing, Department of Public Works, *Developing Supply Strategies*, Brisbane, 2005.

⁸ Performance assessments is addressed in *Topic Specific Guide 4: Performance and continuous improvement*.

Incentives should only be used when extraordinary performance is required

Generally the contract should not include incentives for the Supplier to deliver a better service or to a higher standard than specified in the contract. Rather, if a Client wants a specific (heightened) level of performance or specific outcome, then these requirements should be defined in the contract and priced accordingly by the market. (And a Client should certainly not provide incentives to reward the delivery of contract requirements as specified).

The Client should expect the Supplier to perform to the contract in an exemplary manner without any need for positive incentives⁹. The performance required should be clearly specified by the Client and included in the Supplier's proposal. It is expected that a Supplier works smart and as necessary to achieve the requirements of each project, be paid fully as per the contract and build on its track record and reputation to improve its attractiveness as a Supplier.

Financial incentives are only appropriate for rare and exceptional cases when the Client can not specify the requirement as a normal deliverable because it is so extraordinary and cannot be reasonably priced in the tender.

"Incentives and bonuses do not change contractor behaviour. Clients manufacture incentives and bonuses to feel more comfortable that they can influence delivery. If we are providing a client our top people with the aim of producing a top quality project for a fair price, then I don't know why clients need to offer 'incentives or bonuses' to get a great outcome."

UK Contractor, October 2012

"The Industry has changed over the years. We work to the highest professional standards and with integrity. Clients do not need to provide us with incentives to deliver on our contractual obligations in full and to the quality and performance levels specified and promised in our tender response. Instead of positive incentives, Clients should ask bidders to nominate a percentage of their margin to put at risk for non-performance. We certainly would be happy to do this."

Australian Contractor, April 2013

Manage long term Client/Supplier relationships and new entrants

Public sector infrastructure Clients can benefit significantly from long term repeat relationships that are developed in the normal course of delivering an annual program of projects. These relationships will develop with Suppliers who are high performing and careful to ensure they understand the Clients' drivers, processes, practices and culture. The Client should also invest in understanding the Supplier to the same extent. This long term view on commercial relationships and deep mutual understanding will promote the development of good competitive relationships for the benefit of future projects and the public interest.

However, such relationships are never established at the cost of fundamental government procurement outcomes of competition and contestability, in particular the ability of new Suppliers to enter the market (and in turn also start developing long term relationships).

⁹ Some practitioners will also view penalties and 'at risk' components of the Supplier's fee as incentives to ensure or promote performance. Penalties are common in PPP contracts.

The development of positive 'long term repeat relationships' with Suppliers is consistent with governments wishing to encourage new entrants and promote competition for public projects. As subsidiaries of a government that is the market dominant repeat buyer, government agencies are in the position (and arguably have the obligation) to develop the leadership, culture and practices that promotes a strong and internationally competitive Supplier base; and they can do this by being efficient, effective, informed and exemplary 'buyers of choice'. This means recognising that new entrants can have both the potential and the motivation to be part of a long term repeat relationship. In practical terms, agencies should be prepared to collaborate and explain their corporate contracting practices to new entrants as well as to 'new hands' in established Suppliers. (Although in the infrastructure contracting market, it is likely that new entrants will employ both new and old hands.)

Collaborate effectively with the Supplier/Industry

At the Project level, the Client should collaborate effectively with the Supplier to ensure a good project outcome through high shared understanding of objectives between them (to minimise the expectation gap at contract award).

At the Portfolio level, collaboration is at an organisation to organisation level with a number of organisations forming the basis of an industry sector. The Client should demonstrate proactive leadership to establish deep understanding and trust between government and industry to improve outcomes for all parties. It is expected that industry would reciprocate with a similar level of leadership.

Clarity by Clients will improve industry efficiency and effectiveness by reducing waste and improving productivity.

3.2 Shape thought leadership

Governments are attractive Clients – providing industry with large, reliable, repeat projects where the credit risk is minimal. Government Clients can use this position to continuously improve their procurement strategies to deliver better public outcomes whilst still being 'good' Clients. This takes the form of deliberate planning to get the best out of every transaction through:

- **Protecting the government principles of procurement** through demonstration of value-for-money through competition and innovation and conducting exemplary tender processes that are conducted transparently and can withstand public scrutiny;
- **Seeking and delivering continuous improvement** in the procurement of major projects through better planning and preparedness for the market engagement process; better management and allocation of risk between Clients and Suppliers; transparent monitoring of performance and ex-post evaluation of outcomes; and ensuring efficient and effective tender processes result in expected project outcomes ;
- **Taking a whole of government perspective** beyond a single agency and a single project to optimise the economic and social good over the longer term including broader government policy objectives and reforms; community wellbeing; and industry competitiveness and sustainability; and
- **Looking to the future but being informed by insights from the past** by analysing project outcomes and identifying lessons learned and using that knowledge to inform new approaches, better risk management and awarding of future contracts.

The nature of a government's commercial engagement with industry will impact not just a single project, but the industry structure, competitiveness and sustainability over the longer term. When governments do not assume leadership and proactively shape their engagement with industry, there can be unintended consequences for the public interest.

Thought leadership in the context of this Guide is the effective ability to influence how others define and perceive best practice and project success. Thought leadership, along with general leadership style and an appropriate skill base, is a key attribute of an intelligent client. Leadership is paramount, and Clients need to lead the thinking and actions on their procurement strategies.

4 The Four Critical Success Factors

The purpose of this Chapter is to describe the specific topics that are addressed in detail in the *Topic Specific Guides* of the Framework.

Research into how to improve Traditional Contracting was reported in *Towards Agreed Expectations; tender strategies to improve Design & Construct infrastructure delivery outcomes*¹⁰. This report identified a number of opportunities for improvement including the development of a National Framework for Traditional Contracting, supported by a number of best practice guidelines.

These ‘opportunities for improvement’ were the subject of a consultation paper - *Developing a national approach for traditional contracting in infrastructure* – also released in June 2012 by the Australian Commonwealth Department of Infrastructure and Regional Development. Public sector and industry consultation and feedback supported the development of this Framework.

In line with the research and consultation outcomes, the Framework focuses on four critical success factors that are the subject of four Topic Specific Guides:

1. Project Definition and Tendering.
2. Developing the Project Budget in Business Cases.
3. Governance and Contract Management.
4. Performance and continuous improvement.

Although these are not the only success factors for Traditional Contracting, research showed that these would provide the greatest benefit if good practices were applied more consistently¹¹.

4.1 Topic Specific Guide 1: Project Definition and Tendering

As described in Chapter 1, the identification of a gap in services delivered to the community sometimes leads to the need for a physical asset to be delivered. The description of this physical asset is described in the Project Definition.

The Project Definition underpins the Project Budget that is approved for the Business Case and forms the basis of the subsequent tender documentation issued to Suppliers.

Research has shown that there is significant opportunity to improve project outcomes when using Traditional Contracting by improving the standard of Project Definition for both the Business Case and Tender Phase.

¹⁰ *Towards Agreed Expectations – tender strategies to improve design and construct infrastructure delivery outcomes*, Department of Infrastructure and Transport, Australian Government, June 2012

¹¹ Whilst the principles underlining these four critical success factors will apply for less complex, lower value projects (say, under \$50M), the practices described may be sensibly scaled down to a level appropriate for such projects.

In the **Business Case Phase**, this will assist the Investor and the Client to:

- Describe how the physical asset will address the strategic goals and objectives of the Investor, the operational requirements of the Client and recognise the service impact on the community of providing the asset;
- The quality of the Project Definition directly impacts the quality of the Project Budget developed. The Investor does not assess each Business Case in isolation, but as part of a capital allocation process whereby each Business Case is 'ranked' against others based on a *Value for Money* and *Opportunity Cost of Capital* assessment. This capital allocation by the Investor, and the success or otherwise by the government in delivering the best possible outcomes for the community, is influenced by the quality of the Project Budget in the Business Case.

In the **Tender Phase**, high quality Tender documentation has a direct impact on the quality of the Tender outcome and ultimately the Project outcome. A well-developed Project Definition allows a high degree of understanding between the Client and Tenderer regarding what the Client wants. This results in:

- a high likelihood of the most suitable Tenderer being selected to deliver the Project;
- the Client/Supplier relationship being established on a sound foundation with minimal expectation gap at contract award;
- the Tenderer being able to better assess the project risks and their allocation, thereby providing opportunity to offer a best in market price;
- an appropriate balance between specifying the requirements against the potential to inadvertently stifle innovation by Tenderers; and
- a high probability that the government's Business Case expectations will be met.

If a Project Definition is poorly developed, Clients will pay a premium to satisfy the original service need because:

- the asset may not meet the original service need and require further investment;
- opportunities for better value for money solutions, such as use of technological enhancements, may be missed;
- the Supplier will require a premium to deliver any changes to the contracted scope of works as a result of poor definition; or
- the Client/Supplier relationship is likely to come under stress due to differing perceptions of the Project Definition, requiring (sometimes substantial) management resources.

In both the Business Case and Tender Phase, the Guide will assist Clients to ensure effective and appropriate engagement of Stakeholders to allow a better understanding of risks and opportunities.

This topic is addressed in more detail in the Topic Specific Guide 1: *Project Definition and Tendering*.

4.2 Topic Specific Guide 2: Development of Project Budgets in Business Cases

The Project Budget is based on the Project Definition, and is a key element of the VfM proposition in the Business Case.

Research indicates that there is significant opportunity to achieve greater accuracy in estimating the forecast outturn cost of infrastructure projects delivered using Traditional Contracting by:

1. Improving the preparation of project capital budgets (particularly noting that a focus on project risks must not mean less attention on and scrutiny of the base cost estimate);
2. Promoting greater transparency and accountability in managing capital budgets;
3. Reinforcing the obligation and principle that public officials manage projects to the lowest cost for the required performance, rather than to the maximum approved budget;
4. Putting in place new governance arrangements for management of project contingencies and variations; and
5. Providing clear advice to the Investor on the efficacy and veracity of the capital costs estimates.

By improving the quality and accuracy of Project Budgets, Investors will have better information on which to base their investment decision and Clients will have a greater chance of achieving successful project outcomes within the investment budget.

Topic Specific Guide 2: *Development of Project Budgets in Business Cases* provides guidance on:

- **Foundations for good Project Budgets:** an outline of the foundation points and the essentials that ensure a good Project Budget can be developed for the Business Case. All Business Cases presented to government for consideration should satisfy these foundation points.
- **Elements of a Project Budget:** an overview of the elements of a Project Budget as they should be presented in a Business Case prepared in accordance with government policies and guidelines.
- **Developing accurate base cost estimates:** a description of a base cost estimate for a project and the expected standards to be applied to its preparation.
- **Developing project risk estimates:** an overview of project risks, and the different steps/phases and techniques of developing project risk estimates; how to set the Base Risk Allocation and any other additional risk allocation (beyond P50); and undertaking a sense (or reality) check on whether the estimates are appropriate.
- **Establishing a Project Budget:** guidance on integrating the base cost estimate and project risk estimate to form the recommended Project Budget.
- **Instruction templates for professional services:** templates for engaging the professional services associated with developing the Project Budget for the Business Case.
- **Sign-off templates for professional work done:** sign-off templates for attesting to professional standard of estimation, integrity of process and fitness of Project Budgets.

4.3 Topic Specific Guide 3: Governance and contract management

Strong leadership of governance and contract management is critical to ensuring that a spirit of collaboration persists and that the natural tensions that exist between a Client and a Supplier do not 'open' the expectation gap once the Construction Phase begins. If this gap cannot be kept to a minimum the result will be poor project outcomes and failure for both the Client and the Supplier.

An intelligent client will minimise the expectation gap during Construction Phase by:

- Ensuring that the Client and the Supplier share a deep understanding of the Client's service and project requirements, the successful Supplier's tender response and the agreed contract terms and conditions. The Client must understand any implicit or explicit caveats in the Supplier's bid and the Supplier's understanding of the contract obligations.
- Providing and expecting active leadership to and by the Client and Supplier teams.
- Assuming individual responsibility and accountability for the mutual success of the project for both the Client and the Supplier:
 - through the use of a Senior Responsible Officer or similar Program level role; and
 - through identifying a single Senior Responsible Officer for each project.
- Establishing a high-performance collaborative culture by:
 - Striving for a non-adversarial relationship between the Client and Supplier but not avoiding or deferring the unavoidable hard decisions where interests diverge;
 - Promoting peer-to-peer personal relationships where decisions are made/resolved at the lowest possible organisational level;
 - Encouraging monthly face to face on-site meetings of the most senior forum for resolution of matters;
 - Cultivating an atmosphere of everyone focussing on the 'end-game' – that is satisfying the service need through delivery of the asset;
 - Avoiding a slavish reliance on processes/rules at the expense of judgement and experience;
 - Ensuring sufficient and capable team members are available; and
 - Providing a resolution path that gives access as necessary to a senior executive one level above the Project Director and outside of the Contract management team.

These topics are discussed in further detail in Topic Specific Guide 3: *Contract management and governance*.

4.4 Topic Specific Guide 4: Performance and continuous improvement

As previously reinforced, Governments, as attractive Clients, provide industry with large, reliable, repeat projects where the credit risk is minimal. Such high value strategic clients should expect excellence as a *business-as-usual* performance from Suppliers.

To promote continuous corporate improvement in the delivery of assets by the Client, and on a wider industry level, the 'corporate memories' of Supplier performance and what made projects successful must be captured. To achieve this, Clients should consider including an assessment of the previous performance of Suppliers in the tender evaluation criteria. (Although the inclusion of this criterion should not be given such significant weighting that it prevents selection of a capable and committed Supplier based on an isolated incident of lower performance than that expected.)

In preparing for the Tender Phase of the project, the evaluation criteria, and therefore the RFT documents, must incorporate a provision for the use of assessments of previous performance and measures; and the collection of new assessments.

Capture lessons learned and share knowledge across the Portfolio

The Client must understand, and where possible, address the lessons learned on similar projects. This will help to continuously improve and better tailor project definitions to the needs of new projects and devise a procurement strategy which maximises the experience and capability of the market. This will provide the greatest opportunity to achieve improved project outcomes.

To reverse the trend of constantly increasing the base and risk estimation of an asset cost or class of asset across a longer term portfolio, the Client should gather and utilise information on how project planning and contracting successfully met the service need objectives at the lowest cost. Following construction of the asset, once it is being used operationally, the Investor/Client should conduct a structured and objective assessment of the entire project lifecycle which considers:

- Was the project delivered in line with the approved business case (budget and other constraints)?
- Did the project enable the service need objectives at the lowest cost?
- Did the Supplier perform their contractual obligations to the expected standard?
- Is there anything that could have been done differently which would have had a positive impact on the project or government's wider portfolio?

Both the Client and Supplier (with a balance of people internal and external to the project delivery teams) should participate in this review so that a balanced conclusion can be reached which does not unduly praise or criticise either party but comes to a sound assessment. This Topic is addressed in more detail in Topic Specific Guide 4: *Performance and Continuous Improvement*.

Benchmark project performance

To provide context to the assessment of the Supplier's performance, it is important to benchmark the project against similar recent exemplary projects (e.g. projects that demonstrably enable the service need objectives at the lowest cost). In addition to informing the assessment of the Supplier's performance it also enables the Client to demonstrate that the proposed asset can be delivered in line with government and Supplier expectations and will address the service need. Whilst infrastructure projects have many unique features which make some benchmarking difficult, there will be some factors that are common to enough projects that there is benefit in capturing and analysing the data. This Topic is addressed in Topic Specific Guides 2 and 4; (*Development of Project Budgets in Business Cases* and *Performance and Continuous Improvement*).

Summary

The capture of project performance data is critical to identifying the greatest opportunities for improvement and being able to implement changes to realise those improvements. Project performance data can include assessment of outcomes against the Business Case and Project Definition; and Client and Supplier performance. Generally, jurisdictions formally assess the project performance in terms of achievement of the Business Case and Project Definition. However, the assessment of Supplier and Client performance is often undertaken informally and on a project by project basis.

The Framework seeks to provide practical guidance on formally capturing tender and project performance data through the use of a performance assessment framework, and using that data to:

- inform contract management and decision making at a project level;
- inform tender selection evaluations for future projects; and
- promote continuous improvement at a systemic level between industry and government.

These topics are discussed in further detail in Topic Specific Guide 4: *Performance and Continuous Improvement*.

Appendix A

Glossary and Acronyms

This glossary contains definitions of key defined terms used in the Guide.

Term	Meaning
Business Case	The vehicle that is used by the Client to obtain approval and funding to undertake the project as required by that Client's Investor and jurisdiction. The requirements for Business Cases are normally comprehensively detailed in each jurisdiction.
Client	Entity which will own the completed asset.
Tenderer(s)	Organisation(s) that respond to EOI or RFP.
Public Officials	Individuals employed by governments under the jurisdiction's relevant Public Service Act.
Value for Money (VfM)	The best outcome for the government by having its defined requirements met for the lowest total cost of ownership when considering quality, whole of life impacts, program operations and any other factors affecting the delivery and management of an asset.
Infrastructure	The capital assets needed by the community and wider society to function. Includes civil works such as road, rail or air transportation, power and utilities provision and distribution. In the context of this Guide, infrastructure refers to 'public' infrastructure – that is, infrastructure procured by the government to provide services to the community. This Guide is limited to road, rail or water infrastructure as they are the most common class of asset delivered through traditional contracts. (It should be noted that the construction of complex facilities, such as hospitals and prisons can have similar characteristics and in some jurisdictions these are also labelled as 'infrastructure'.)
Project Lifecycle	The whole of project process of delivering an asset covering the Inception, Planning, Tender, Construction and Operation & Maintenance phases.
Supplier	The organisation which enters into contract with the Client to deliver a specific scope of service, materials and labour generally to construct an asset.
Design and Construct	A contract form where the Supplier is responsible for part or all of the design as well as constructing the asset, generally for a Lump Sum fee.
Construct Only	A contract where the Client fully designs the asset and a Supplier builds the asset to that specification and standard.
Lump Sum	The delivery of contract services for a fixed value which includes the Supplier's direct costs, overhead and profit.
Procurement	The Inception, Planning, Tender, Construction and Delivery phases in the construction of an asset.
Delivery	The Construction, Operation and Maintenance phases in the delivery of an asset

Appendix B

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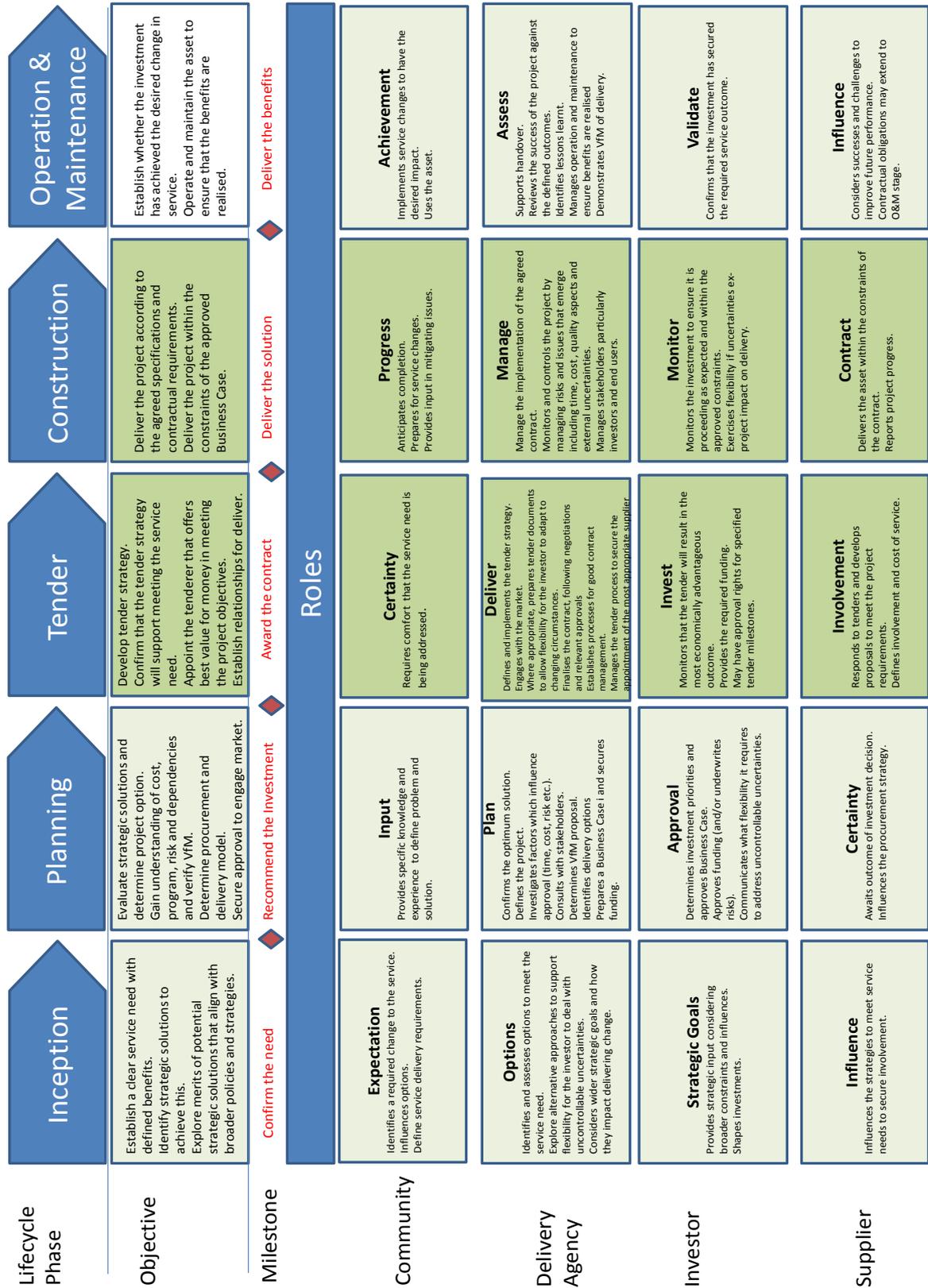
Appendix C

Roles through project phases

Objectives by project stage

Key to understanding the commercial aspects of project procurement is understanding the outcome that must be achieved at each project lifecycle stage and the varying (and sometimes conflicting) objectives of the participants. This is illustrated in *Figure 5 Objectives of participants through the Project Lifecycle* and discussed in more detail in the following sections.

Figure 5 Objectives of participants through the Project Lifecycle



Inception

It is during the **Inception Phase** that a clear service need with defined benefits is established by the Client. The service need is defined in specific and measurable terms that will be used to assess the success of the project in enabling service delivery to the community. During this Phase a range of strategic options will be identified which may meet the service need and the merits of these options explored. This includes consideration of the alignment with broader Government policies and strategies.

It is important that during the Inception Phase there is an understanding of the jurisdictional specifics of approving the capital investment. At this stage a procurement strategy is developed which best fits with the characteristics of the particular project. This strategy is refined through the Planning and Tender Phases.

This phase is documented in the Business Case.

Planning

The primary objective of the **Planning Phase** is to prepare for market engagement and commence the tendering process. To achieve this, the strategic solutions identified during Inception must be evaluated and a clear project option selected. Following this, investigative work is undertaken by the Client to develop and document the cost, program, risks and dependencies associated with delivering the asset. This information will be used to verify the Value for Money proposition of the investment, as defined in the Business Case.

This phase is partly documented in the Business Case; with greater detail, in preparation of the tender release, completed once the Business Case has been approved.

Tender

The **Tender Phase** consolidates the preparation work from the Inception and Planning Phases and establishes the foundations of a successful Construction Phase. The outcome of this Phase is market engagement with Tenderers and appointment of the Supplier that offers the best value for money in delivering the asset to meet the project objectives. This requires preparation of a detailed procurement strategy which is efficient and effective provides the foundations for a successful Construction Phase and meets the relevant jurisdictional procurement requirements.

Construction

The objective of the **Construction Phase** is to deliver the project according to the contractual requirements. The parameters of the approved Business Case (eg Project Definition, Project Budget etc) must be satisfied during the delivery of the asset with any changes approved by the Client and Investor as required by their specific jurisdiction.

Operation & Maintenance

Following construction of the asset, and once it is operational, it is important to establish whether the investment has achieved the desired uplift in service. It is important to evaluate:

- Has the asset met the expectations and requirements of the Community and government?
- Was the asset delivered within the Business Case constraints?
- Is there anything the Client would do differently in the future?
- Did the Supplier perform their services to the expected standard and would they deem working with the Client a success?

Assessing whether the desired outcomes have been achieved will provide valuable lessons and benchmarking information for future projects.

