Procurement strategies: Affordable and quality public infrastructure

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What is a procurement strategy?

Procurement phases	Principal activities (ISO 10845-1)		International Organisation for Standardization (ISO 21502:2020, Guidance on project management)
	No	Description	
Planning	1	Establish what is to be procured	**Planning procurement** Define a procurement strategy, taking into account: • the project's "make or buy" decisions; • the delivery practices; • the type of legally binding agreements; • the procurement process to be used
	2	Decide on procurement strategies	
Acquisition	3	Solicit tender offers	**Evaluating and selecting suppliers** Select suppliers. based on selection activities in accordance with stated evaluation criteria.
	4	Evaluate tender offers	
	5	Award the contract	
Contract management	6	Administer the contract and confirm compliance with requirements	**Administering contracts** **Closing contracts**

procurement strategy: selected packaging, contracting, pricing and targeting strategy and selection method for a particular procurement

delivery management: the critical leadership role played by a knowledgeable client to **plan, specify, procure and oversee the delivery of projects** including knowledgeable leadership, consistent governance and systematic administration of procurement, contracts and project finances.

Procurement strategy is an integral part of project delivery

Approach to developing a procurement strategy (ISO 22058)

ISO 22058:2022 Construction procurement — Guidance on strategy and tactics

Gather and analyse information (conduct spend, organisational, market and stakeholder analyses)

Formulate **primary and secondary procurement objectives**

The primary objectives relate to the delivery of goods, services or works including tangible and intangible objectives

Secondary objectives typically relate to the **promotion of developmental objectives**

Package required work into contracts or orders linked to a framework agreement

Determine **contracting strategy** (identify form of contract and pricing strategy)

Risk allocations

Type of contract
Construction contract
Design, build and operate contract
Professional service contract
Design, build and operate
Service contract
Supply contract

Pricing strategy
Price-based
Activity schedule
Bill / schedule of quantities
Lump sum
Price list or price schedule
Cost-based
Cost reimbursable
Cost plus
Target cost
Time based
Percentage of cost of construction
Performance-based
Performance metrics

Decide on targeting strategy

Targeted procurement / preferential treatment

Decide on selection method to solicit tender offers

Document procurement strategy

Risk in infrastructure projects

Risk - exposure to the chance of loss, harm or failure to achieve objectives

- Risk can be **retained or transferred**

- The focus in the distribution of risk is on the **payment and responsibility for the cost of the event, should it materialize**.

  - The contractor tries to **limit liability** in contracts to a foreseeable figure.
  - If the client **retains risk** (and uncertainty), it only pays for risks that materialize.

The more risk that is transferred through contracts the fewer the firms that are willing to submit tenders ie it reduces competition.

Reducing uncertainty for new entrants **increases the competition in the local market**.

The **higher the uncertainty, the higher the risk pricing.**

An **underestimate of risk results in the "winner's curse"** (tenderer who least overestimates the risk) which can lead to a failure to deliver on contractual obligations.

The sources of risk associated with the delivery of infrastructure include those relating to:

- client / owner behaviour,
- human behaviour,
- community opposition / unrest,
- design (omissions/ interfaces / changes),
- economic circumstances,
- finances,
- force majeure,
- political and regulatory frameworks,
- project governance,
- technical aspects,
- technology,
- third parties (subcontractors / suppliers),
- environmental safeguards,
- natural events,
- weather and inherent site conditions.

Risk taking is necessary in infrastructure delivery.

Value for money is achieved when the efficiency gains by transferring risk are higher than the losses from inefficient risk pricing.

Risk and complexity in infrastructure projects

Project complexity is a function of :

- **Scope complexity** which occurs where the individual pieces in a single project have no value without every other piece being successfully completed or where new technology is central to a project
- **Organisational complexity** which grows as the number of organizations and individuals involved in a project increases and line-of-sight management to individual teams becomes impracticable and a different style of management involving a leader of leaders becomes essential to success.
- **Shaping complexity** which relates to the array of challenges emanating for internal and external stakeholders

Packaging can reduce risks associated with complexity

Drivers of inefficient risk pricing include
- excess transfer of risk,
- lender requirements which require a high degree of certainty,
- availability of sufficient and reliable information and sufficient time for bid preparation.

Risk pricing inefficiency can be reduced though
- design clarity and flexibility,
- following established risk allocation principles where the key objective is to contain the cost of the risk,
- considering the benefits of joint risk management. (relational / collaborative contracting, early contractor involvement and alliancing / partnering)_

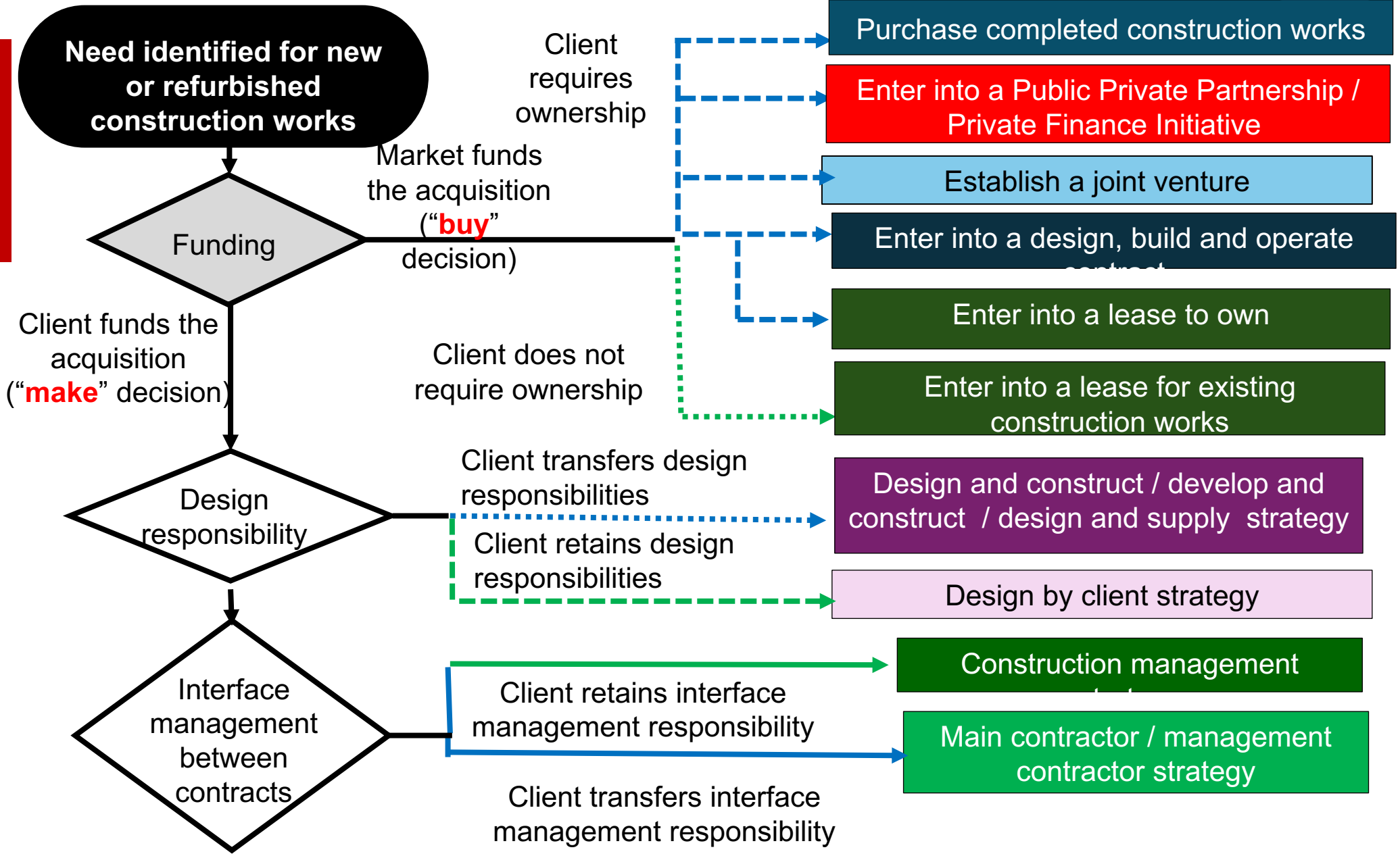
Risk pricing and competition determine the **total cost of risk transfer** from the public to the private sector and the **differential between public and private sector finance**.

Options for construction works projects (ISO 22058)

ISO 22058:2022 Construction procurement - Guidance on procurement strategy

The choice as to **how the market is to be engaged:**

- determines the **number of contracts** that need to be procured and overseen
- determines the **capacity and capabilities of the client delivery management team**.
- informs the **procurement strategies** that are adopted



Infrastructure delivery models

Infrastructure delivery models **are framed around the retention of risk by the client and the transfer of risk** to the contractor. Procurement strategies and tactics **influence project outcomes.**

Differentiators between delivery models include:

- the **treatment of risk** (risk allocation and / or risk sharing);
- the **mitigation of risk** through collaborative approaches and making use of competitive dialogue / negotiations to address uncertainties in tender processes;
- how much externalised project activities are bundled;
- the associated scope of the project contracts;
- the approach to remuneration (fixed price, reimbursement or target price) within these contracts;
- positive / negative **incentives such as pain/ gain share regimes** (target contracts) and performance bonds; and
- how contractors get involved in the design process (e.g. early contractor involvement).

Current roadblocks within the public sector

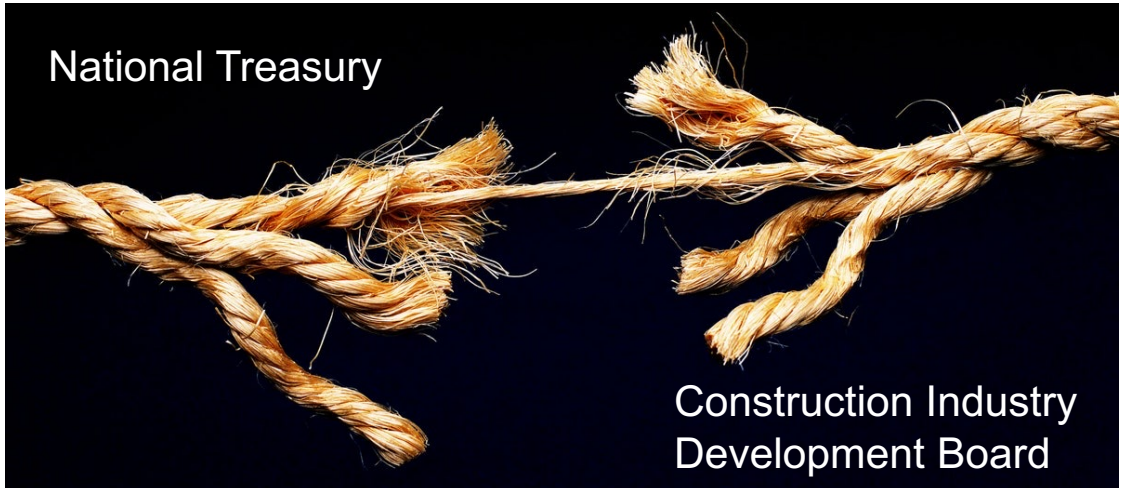
Administrative procurement driven by finance department

Procurement conceptualised as an acquisition function within a financial management system

Administrative in nature (back office) under a Chief Financial Officer

- driven by a General Conditions of Contract which excludes change management and a specification inserted into a pack of forms
- clerical function

Typically applies to general goods and services for consumption where risk is negligible



Office of the Chief Financial Office over time forced an administrative **one size fits all regime onto infrastructure procurement** which **has crippled infrastructure delivery**

Strategic procurement driven by an operations department

Procurement conceptualised as the process which creates, manages and fulfils contracts within a project delivery system

Strategic in nature **(front office)** driven by procurement strategy and tactics with:
proactive risk management and change management embedded in procedures

Typically applies to infrastructure where material risks can exist

Public sector paradigms informing systems

Administrative ?

Where do we pitch procurement reform?

Strategic?

Paradigm	Defining characteristics of the public sector	Defining characteristics of procurement system
Public administration	• **Dominance of rules** • **Highly centralised decision making**, management discretion discouraged	System is administrative in nature and rule driven **where compliance with rules and ticking of boxes is more important than project outcomes.** Highly **centralised decision making** where **management discretion is discouraged.** **System is unresponsive, inefficient, slow and incorporates inappropriate bureaucracies**.
Public Management	• Decentralisation of decision making. (**Give managers responsibility for decision** making but make them accountable) • **Emphasis on efficiency**	System **provides a wide range of options enabling a strategic and tactical approach** to procurement to be taken to improve project outcomes Decision making is **decentralised.** Emphasis is on **clear accountability, efficiency, effectiveness and project outcomes**.
Public governance	• Focus on inter-organisational relationships and **governance of processes** • **Stresses service effectiveness and outcomes**	**Governance enables alignment of choices** with **organisational strategic objectives and values**, stakeholder aspirations and collaborative relationships

The road to affordable and quality public infrastructure (NIP 2050)

National Infrastructure Plan 2050 (NIP 2050) for implementation in terms of the Infrastructure Development Act of 2014 calls for **a step change in the institutional capability that drives material progress in South Africa's infrastructure ambition.** Planning, procurement and execution systems and capabilities will be operating at the highest global standard.

Conditions for project execution to be met to achieve the 2050 vision include:

Built environment professionals – identification of work suggests that procurement is an integral part of the project stages

1 Public sector competencies must operate at a high professional level.

- *Competence to procure and deliver must be high in respect of ability, knowledge and skill.*

2 The regulatory framework must enable network infrastructure procurement and delivery

- *The regulation of SCM for infrastructure must enable integrated projects with built-environment professionals playing a significant role. SCM for infrastructure must be handled as **a strategic function**, not simply a financial one.*
- *The procurement of infrastructure **must be differentiated** from that of other goods and services.*

3) A strategic approach must be taken to infrastructure procurement.

- *Value for money must be a focus and prioritised over lowest cost.*
- *There must be trust and understanding with suppliers.*
- *Departments and entities with large infrastructure procurement budgets must have a chief procurement officer, **with sufficient built-environment professional capacity leading the procurement process.***