

# Public Document Pack



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DATE: 4 April 2017

OUR REF:

YOUR REF:

Dear Councillor

## **CORPORATE OVERVIEW AND SCRUTINY COMMITTEE - THURSDAY, 6TH APRIL, 2017**

I am now able to enclose, for consideration at next Thursday, 6th April, 2017 meeting of the Corporate Overview and Scrutiny Committee, the following report, which was unavailable when the agenda was printed.

### **Highways Contract Procurement (Pages 3 - 18)**

Yours sincerely

Scrutiny Manager

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## Cheshire East Council

### Cabinet

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**Date of Meeting:** 11 April 2017

**Report of:** Frank Jordan, Executive Director of Place

**Subject/Title:** Highway Service Contract Procurement

**Portfolio Holder:** Cllr David Brown

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#### 1. Report Summary

- 1.1. At the meeting of 17 January 2017, Cabinet approved the following recommendations:
  - That the Executive Director for Place progresses the process for procuring a new Highway Service Contract for the Council in consultation with the Deputy Leader and Portfolio Holder for Highways and Infrastructure.
  - That they approve the establishment of a pre-procurement advisory cross-party Member Panel to make informal recommendations to the Portfolio Holder in respect of priorities for the Contract.
- 1.2. Cabinet also noted that the Procurement Strategy, incorporating the contract model, duration and value and procurement route, would be brought back to Cabinet for approval.
- 1.3. This report summarises the work of the Council officers, in consultation with the Portfolio Holder and the Member Panel since January 2017 and makes recommendations on the proposed Procurement Strategy for the next Highway Services Contract.

#### 2. Recommendation

- 2.1. It is recommended that Cabinet:
  - Approves the Strategic Aims and Contract Objectives for the next Highway Services Contract as set out in Section 4.3 and 4.4.
  - Approves the Procurement Strategy for the next Highway Service Contract to include:
    - An Integrated Services Contract model.
    - A full 15 year contract period with a pre-defined mid-term break clause (Year 8) linked to the performance framework and an upper limit on individual schemes through the Contract of £5M.

- A Competitive Procedure with Negotiation as the procurement route.
- Notes that all the recommendations have been informed by the cross-party Member Panel and the procurement route by Corporate Overview and Scrutiny Committee.
- Authorises the Executive Director for Place, in consultation with the Deputy Leader and Portfolio Holder for Highways and Infrastructure to commence the process for procuring a new Highway Services Contract for the Council, including finalising its scope.
- Notes that following completion of the tender process, Cabinet will be requested to approve the award of contract to the preferred bidder.

### 3. Other Options Considered

- 3.1. Following the establishment of the Project Board and Member Panel, the entire range of highway delivery models open to the Council have been assessed and evaluated. The assessment followed the Highway Maintenance Efficiency Programme guidance (*HMEP is the Department for Transport's transformation programme*) and tested all the options against the Council's strategic aims and objectives for the Highway Service.

### 4. Reasons for Recommendation

- 4.1. The process of determining the future delivery of highway services has followed the Council's 'best fit' approach to the commissioning of Council services.
- 4.2. The process to determine what the Procurement Strategy should be included four key areas:
- Strategic Aims and Objectives
  - Contract Model
  - Contract Duration and Value
  - Procurement Route

#### Strategic Aims and Objectives

- 4.3. Officers in consultation with the Members Panel and the Portfolio Holder for Highways and Infrastructure have identified the following strategic aims for the next contract:
- To maintain and improve the condition of the highways network
  - To deliver value for money and savings for the Council
  - To improve customer satisfaction
- 4.4. It is recommended that the future contract model needs to promote the achievement of the following objectives:
- To generate market interest in the proposed contract

- To enable the Council to secure the required capability and capacity to deal with potential increases in capital investment
- To deliver efficiencies and ongoing savings for the Council
- To give the Council flexibility to respond to changing customer needs and national priorities
- To promote innovation and continuous improvement
- To focus on Asset Management
- To focus on long term planning
- To retain the ability to collaborate with other public bodies and the supply chain

See Appendix 1 as to how the Objectives align with and support achievement of the Strategic Aims.

### Contract Model

- 4.5. The Highway Maintenance Efficiency Programme has identified and published a range of delivery models open to the Council.
- 4.6. The range of identified delivery Models covers:
  - In-house service provision
  - In-house service plus “top-up” arrangements with external providers
  - Establishment of Publicly-owned company (“Teckal exempt”)
  - A Public-Private Joint Venture Company
  - External service provision via “Framework” contracts
  - External service provision via multiple term service providers
  - External service provision via a single term service provider
  - Private Finance Initiative
- 4.7. A description of the key features of each Model is included in the “HMEP Procurement Route Choices Toolkit” available at: [www.highwayefficiency.org.uk](http://www.highwayefficiency.org.uk)
- 4.8. Each of the potential models has been evaluated against the proposed Contract Objectives in order to identify the best fit model. This evaluation has been tested through the Member Panel and scrutinised by Corporate Services. Even though this evaluation identified a preferred option, it was felt prudent at this stage in the process to test the top two highest scoring options through a market engagement exercise.
- 4.9. The two models ranked highest in the evaluation, with Model A scoring highest overall:
  - Model A – Integrated Services with a Single Provider

- Model B – Separate Contracts for Professional Services and Maintenance / Improvement Works.

The option of lots was not favoured in the market testing.

- 4.10. The market engagement has been undertaken through a Prior Information Notice issued via the OJEU seeking market feedback on aspects of the next Highway Services Contract via a Questionnaire.
- 4.11. A summary of the market engagement outcome is given in Appendix 3 of this report. What this has demonstrated is that in broad terms either model could deliver against the strategic aims and objectives. Having said this the market responses do reveal that Model A would best deliver against the Value for Money Strategic Aim. This outcome aligned with the Councils internal evaluation process which confirmed Model A as the highest ranked option.
- 4.12. Therefore it is recommended that the Integrated Services Option (Model A) be taken forward as the Contract model..

### Contract Duration and Value

- 4.13. The duration of the Contract (the Service Period) can have a significant influence on the efficiency and effectiveness of the service and the market's appetite for the contract opportunity.
- 4.14. As a general principle, a longer service period will be more attractive to the market. A longer service period will provide greater predictability of workload and cashflow thereby enabling the Contractor to make long term investment decisions and to recover sunk costs such as tendering, mobilisation and service restructure costs.
- 4.15. A longer service period also provides the opportunity for the Council and the Contractor to develop long-term, collaborative relationships. The longer duration enables the parties to develop long-term plans for the service and the highway asset, with the opportunity to recover investments in the service.
- 4.16. A key factor is the ability to recover sunk costs, such as fleet and plant, over the service period. The largest single investment in equipment is likely to be the winter service fleet (gritters). This would avoid the contractor having to factor in the risk of redeploying or divesting of equipment that has not reached the end of its commercial life.
- 4.17. In order to balance the benefits of longer-term contracts with the risk of a loss of focus and competitiveness, it is recommended that the service period be a maximum of 15 years.
- 4.18. The market engagement exercise sought views on two principal options for the service period:
  - An initial service period that is extendable in single or multiple years based on performance up to the maximum of 15 years

- A full service period of the maximum of 15 years which is reviewed at defined intervals with the option for the Council to trigger a break-clause in the event of unsatisfactory performance
- 4.19. The Member Panel recommended an initial term, or break-clause, at year 7 to ensure sufficient focus on the performance requirements. A summary of the market engagement outcome is given in Appendix 3 of this report.
- 4.20. Given the longer term duration recommendation, it is vital that contract scope is fully assessed to allow the Council to take advantage of future opportunities and benefits which could arise during this service period. The major provision would be the inclusion of Major Infrastructure Schemes, potentially up to £5M, to be delivered through the Contract subject to robust assessment of Value for Money. The delivery of any Major Schemes is a key decision for the Council and would require Cabinet approval before progressing.
- 4.21. Therefore it is recommended that a full 15 year contract period is awarded with a pre-defined mid-term break clause (Year 8) linked to the performance framework and with an upper limit on individual schemes through the Contract of £5M.

### Procurement Route

- 4.22. There are a number of procedures that can be utilised, listed below, which fall under the Public Procurement Regulation 2015:
- Open Procedure
  - Restricted Procedure
  - Innovative Partnership
  - Competitive Procedure with Negotiation (CPwN)
  - Competitive Dialogue Procedure
- 4.23. Each of these procurement route options has been evaluated against the requirements for the Highway Services Contract.
- 4.24. It is worth noting that the Council has been delivering the Highway Service through similar arrangements for the last five years and it can therefore be argued that it is able to establish the technical specifications with sufficient precision. However, there are complex elements of the service which the Council may wish to negotiate with bidders in order to achieve the best commercial outcomes. These include:
- how the provider will carry out the whole life planning of the highway asset to deliver the best outcomes for the Council (i.e. this is not an input based contract)
  - the need for significant investment in the service such as winter fleet and depots
  - the need for the solution to be flexible to respond to changes in demand and requirements for the services over the life of the contract

- 4.25. The Competitive Procedure with Negotiation enables the Council to negotiate elements of the initial tenders with bidders. Crown Commercial Services supports the ability of contracting authorities to use negotiation to achieve the best commercial outcomes.
- 4.26. The Market feedback supports the Competitive Procedure which has been endorsed through the Member Panel and Corporate Overview and Scrutiny Committee.
- 4.27. Therefore it is recommended that the Competitive Procedure with Negotiation is the selected procurement route.

### **5. Background/Chronology**

- 5.1. The current contract will end on 4th October 2018 having previously been granted the two year extension to utilise the maximum 7 year duration.
- 5.2. An outline programme is shown in Appendix 2 for delivery of a new Contract by October 2018.
- 5.3. Following Cabinet approval in January 2017 to commence the project, all work streams have been managed through the established project governance arrangements including:
  - Project Board
  - Scope Workshops
  - Member Panels
  - Corporate Overview and Scrutiny
  - Market Engagement Exercise

### **6. Wards Affected and Local Ward Members**

- 6.1. All Wards and Ward members are affected by this proposal.

### **7. Implications of Recommendation**

#### **7.1. Policy Implications**

- The procurement will have a significant influence on the service's contribution to the delivery of the Cheshire East Corporate Plan outcomes:
  - Outcome 2: Cheshire East has a strong & resilient economy
  - Outcome 4: Cheshire East is a green & sustainable place
  - Outcome 6: A Responsible, Effective & Efficient Organisation
- Connectivity is an important component of delivering 'quality of place' which the Council sees as a strategic driver for the economy and character of Cheshire East.
- The Council has a suite of highway policies, which will be updated using an Environment & Regeneration Overview and Scrutiny Committee Task



and Finish group, to provide a challenge to the market to assess the most efficient way to deliver these policies.

### **7.2. Legal Implications**

- The existing Highway Service Contract will expire in October 2018 and cannot be extended further as the Council previously approved the full two year extension at Cabinet in November 2014.
- The aggregate value of the Council's requirement for highway services is such that these services must be procured in accordance with the Public Contracts Regulations 2015 and in compliance with the Council's Finance and Contract Procedure Rules. This requires a fully OJEU compliant tender exercise.

### **7.3. Financial Implications**

- The objectives of the new Contract are to maintain the condition of the Cheshire East highway assets in their current condition, and where possible to make improvements.
- Negotiation with the potential bidders will inform how services will be delivered within the existing financial constraints and determine the level of savings that can be achieved
- The financial effects of the new Contract will be reflected in future business planning rounds, for the year 2018/19 onwards.
- Funding for the procurement process is held within existing Highways revenue budgets in 2016/17 and 2017/18. It is expected that any underspend against the 2016/17 revenue budget will be carried forward to 2017/18 to match with expenditure.

### **7.4. Equality Implications**

- An Equality Impact Assessment has been undertaken and will continue to be reviewed by the Project Board on a quarterly basis as the project progresses.

### **7.5. Rural Community Implications**

- 57% of the Cheshire East highway network is classed as rural serving over half of our population. The quality and availability of the rural network is vital to the local economy, not just in rural areas. It needs to take account of the specific needs of rural residents and visitors as well as the impact on the character and connectivity of our rural areas. This in turn impacts on the Borough's 'quality of place'.
- The future Highway Service delivery will take account of the Council's strategy for rural areas, will link to other key strategies, outcomes and have a focus on quality of place. As part of the procurement the Council will seek ideas and innovations as to how to deliver services to our rural communities and businesses in the most effective and efficient manner, recognising the relative needs, characteristics and significance of the rural network and its users.

### **7.6. Human Resources Implications**

- The transfer of staff allocated to the current highway contract will require a TUPE process between service providers, and the same duties apply in any second-generation outsourcing situation.
- The Corporate Trade Unions have been briefed and affected staff will be engaged following the Cabinet resolution.

#### 7.7. Public Health Implications

- The highway service plays an important role regarding public health, through promotion of walking and cycling, and delivery of infrastructure to promote more sustainable travel.
- The management of the highway network plays a key role in the borough's air quality, the improvement of air quality will be a consideration as part of the procurement.

#### 7.8. Implications for Children and Young People

- The highway service delivers, and assists other Council departments to deliver, improvements and road safety training specifically targeted at our children and young people.

### 8. Risk Management

- 8.1. A risk register has been developed for this procurement and is reviewed by both the Project Team and Board on a monthly basis. All risks have assigned owners who are responsible for mitigating and managing the risks. The 3 Key Risks are:

Risk No & RAG Rating	Description	Impact	Mitigation
1	Time – contract to be awarded by October 2018.	Significant reputational risk to the Council if the new contract is not in place prior to October 2018.	Dedicated project team in place to establish the optimum Procurement Strategy. Detailed Project Plan with key milestones and activities. Critical Path defined
2	Scope of contract to be defined	A scope that is not attractive to the market place and/or partners that may want to collaborate. Scope limits future activities and could incur undue costs & delay.	Options appraisal to be undertaken.
3	Market Appetite – this is shown as an opportunity to fully engage with the market place and manage/mitigate any perceptions or conflicts of interest.	Ability to engage with the market place will inform on the potential procurement routes and optimum model(s) available.	Authority to conduct supplier engagement event. PIN & Questionnaire issued to the market with positive feedback received.

## 9. Access to Information/Bibliography

9.1. The following information is available:

- Contract Model Evaluations
- Contract Duration assessments
- Procurement Route options

## 10. Contact Information

Contact details for this report are as follows:

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**Appendix 1 – Contract Strategic Aims and Objectives**

Strategic Aim	Objectives for the Contract
Deliver Value for Money	Model needs to generate strong market interest
	Model needs to deliver efficiencies and ongoing VfM
	Model needs to promote innovation and continuous improvement
	Model should enable collaboration with public bodies and the supply chain
Maintain / Improve Network Condition	Model to enable a focus on Asset Management
	Model to enable long term planning
	Model is to have the capability and capacity to deal with potential increases in capital investment
Improve Customer Satisfaction	Model to be flexible to respond to changing customer needs and national priorities

## Appendix 2 – Outline Programme

Activity / Milestone	Indicative Date
Finalise Recommendations	March 2017
Cabinet Meeting	11 April 2017
Contract Notice Issue	June 2017
Shortlisting Completed	August 2017
Initial Tenders Submitted	October 2017
Negotiations Concluded	November 2017
Final Tenders Submitted	December 2017
Contract Award	March 2018
Contract Start	October 2018

### Appendix 3 – Market Engagement Summary

#### Background

A Prior Information Notice was issued via the OJEU seeking market feedback on aspects of the new Highway Services Contract via a Questionnaire.

The questions are summarised in the table below:

Question No	Question
1	Level of interest in Model A (Integrated), on a scale of 0-5
	Level of interest in Model B (2 separate contracts), on a scale of 0-5
	Level of interest in bidding for both contracts if Model B was selected, on a scale of 0-5
2	Details of any proposed alternative Models
3	Service Period of 15 years
4	Mechanism for adjusting the Service Period
5	Ability to provide investment in assets
6	Use of the CPN Procurement Procedure

17 Questionnaires were received via the Chest by the closing date of 14<sup>th</sup> March 2017. 2 of the Questionnaires did not provide relevant information. Of the remaining 15 Questionnaires:

- 12 were from organisations that provide highway maintenance works and services (referred to as Contractors herein for ease)
- 3 were from organisations that provide professional services only (referred to as Consultants herein for ease)

This Appendix provides a summary of the market responses. All responses are anonymised and reflect the overall market views and not those of any one organisation.

#### Question 1 – Level of Interest in Models

**Note:** For Models A and B, an interest level of 0-1 is classified as “not interested”; an interest level of 2-3 is classified as “neutral”; an interest level of 4-5 is classified as “interested”

##### Model A (Integrated)

Of the 3 Consultants, 2 were neutral and 1 was interested in Model A.

Of the 12 Contractors, 4 were neutral and 8 were interested in Model A.

##### Model B (2 separate contracts)

Of the 3 Consultants, 3 were interested in Model B.

Of the 12 Contractors, 2 were neutral and 10 were interested in Model B.

### Bidding for both contracts if Model B was selected

Of the 3 Consultants, none were interested in bidding for both contracts if Model B was selected. Of the 12 Contractors, 6 were not interested in bidding for both contracts, 5 were interested and 1 was neutral.

### Conclusion and Recommendation

The market consultation indicates that both Models will be attractive to the market. However, should Model B be selected, there was reduced appetite for bidding both contracts, respondents largely indicating that they would choose one or other of the 2 contracts.

Model B (2 separate contracts) was the more attractive option to the Consultants and to those Contractors with more limited experience of local authority highway services. The key reason cited was that Model A would require them to form a Joint Venture to supplement their own service offering. Their preference therefore would be to concentrate on their core offering i.e. design or construction services respectively.

Model A (Integrated) was the more attractive model to those Contractors with more extensive experience in the delivery of local authority highway services. Of the 7 established highway services Contractors that responded, 6 preferred Model A to Model B. The reasons cited for this preference were:

- Greater efficiency resulting from:
  - a reduced number of interfaces,
  - reduced Contractor overheads,
  - the ability to design their team around the service rather than around interfaces with another organisation
  - reduced Council contract management time
- Greater effectiveness resulting from an ability to focus the Council's strategic aims and the asset.
- Greater collaboration resulting from their ability to bring established relationships rather than the partner being selected for them.

The 7<sup>th</sup> Contractor, even though their preference was for Model B, did consider that Option A provided an opportunity to be more efficient and asset-focussed.

The market consultation has confirmed that Model A has a high probability of generating significant market interest and tenders from the established local highway authority provider market.

Although the market consultation indicates that Model B would also be likely to generate market interest, only three Consultants responded to the Questionnaire. This low response rate may indicate that should Model B be selected, there is a risk that there could be a limited number of bidders for the professional services contract.

## **Question 2 – Alternative Models**

There were no alternative models proposed by the respondents and the majority considered that the Council had identified the two most appropriate Models. A number of minor amendments in the scope and / or ways of working under both Models were proposed and these will be considered during tender document preparation.

### Conclusion and Recommendation

There are no further Models to be considered by the Council.

### **Question 3 – 15 Year Service Period**

Of the 15 respondents, 12 were supportive of a 15 year period and considered that it provided an optimal duration for fleet investment as well as investment in other assets, people and the service. 2 considered that a period of 10 years would be appropriate and 1 considered that a shorter period would be preferable.

### Conclusion and Recommendation

A 15 year Service Period will be attractive to the market and has the potential to produce optimal commercial and service delivery outcomes.

### **Question 4 – Adjusting the Service Period**

Two options were put to the market for feedback. Option 1 was to award an initial Service Period (e.g. 7 years) that was then subject to extension based on performance up to the maximum of 15 years. Option 2 was to award the full Service Period, with break-clauses at pre-defined points if the Council did not want to continue for the full Service Period.

All respondents considered that there should be a mechanism to review or adjust the Service Period rather than award the full 15 years. Of the 15 respondents, 6 considered that Option 1 was preferable, 7 considered Option 2 to be preferable and 2 were neutral. Overall, none of the respondents expressed a strong preference for either Option. None of the respondents made a compelling argument for either Option or suggested there was any resultant commercial benefit for the Council.

### Conclusion and Recommendation

The market would view either Option as acceptable. Therefore it is recommended that the Council look to award the full 15 year Contract duration, with a pre-defined mid-term break clause subject to performance and the Council's needs and constraints at that time.

### **Question 5 – Investment in Assets**



Of the 15 respondents, 11 indicated that they would be prepared to invest in assets (including fleet and depots) and for the investments to be recovered during the Service Period. A number indicated that they have specialist investment arms.

Of the 4 organisations that would not be able to provide investment, 2 of them were Consultants.

### Conclusion and Recommendation

It is considered that if the Council required the tenderers to provide investment funding, it would not be a barrier to participation and a competitive tender process.

### **Question 6 – Use of the CPN Procurement Procedure**

All 15 respondents considered the use of the CPN Procedure as acceptable. A number of the respondents considered it to be the most appropriate Procedure and endorsed its use.

### Conclusion and Recommendation

It is recommended that the Council use the CPN Procedure.

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