

Making competition work for you

A guide for public sector procurers of construction



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Why this new guide?

To help you achieve value for money by making the most of competition

Competition:

- increases the choice of suppliers
- provides suppliers with incentives to submit bids that match your needs
- creates incentives to deliver construction projects to time, quality and cost
- creates incentives to innovate and invest in future capacity.

This guide focuses on practical steps you can take, pitfalls you should avoid and risks you can mitigate in order to make competition work for you.

The guide also recognises the risks of suppliers engaging in anti-competitive behaviour, such as bid rigging. It highlights some of the practical steps you can take to mitigate these risks and shows how the Office of Fair Trading (OFT) can help.

- 01.** The aim of this short guide is to spread best practice among organisations responsible for the procurement of public construction projects and to encourage effective competition.
- 02.** This is significant because the public sector is a major player in the construction market – growing by a third between 1999 and 2003, to an annual output of £33.5 billion. Capital investment by the public sector is set to continue expanding over the next three years in key sectors, such as schools, hospitals, roads and social housing¹.
- 03.** Efforts to achieve effective competition in the construction sector are now focusing in on whole-life costs and value, plus long-term partnerships between the public and the private sector.
- 04.** The competition challenge is to sustain what the National Audit Office (NAO) calls “competitive tension”, while reaping the benefits of a partnership approach.
- 05.** The Office of Fair Trading (OFT) research on public procurement and competition² and the Office of Government Commerce’s (OGC’s) First Kelly Market³ project both identified a need to raise awareness of the impact of public sector procurement policies on competition for construction projects.
- 06.** You should use this guide alongside the existing suite of OGC procurement guidance, particularly the Achieving Excellence in Construction⁴ initiative and the OGC Successful Delivery Toolkit⁵.
- 07.** This guide was prepared by PricewaterhouseCoopers LLP, in collaboration with OFT and OGC, and is based on a wide range of interviews with stakeholders (see Annex A for details). The OFT and the OGC would like to extend their thanks to everyone who has contributed to the development of this guide.

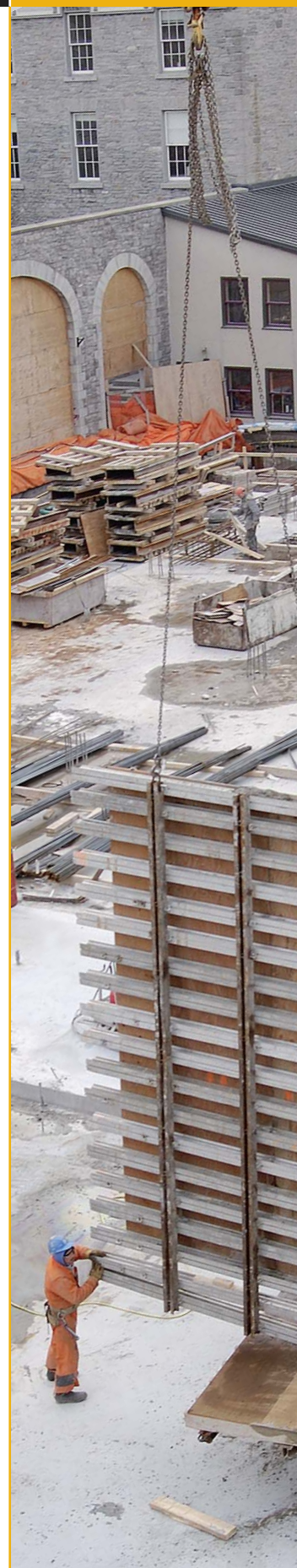
¹ NAO (2005), “Improving public services through better construction”, Her Majesty’s Stationery Office (HMSO).

² DotEcon (2004), “Assessing the impact of public sector procurement on competition”, OFT (www.oft.gov.uk).

³ Construction was the first market to which the recommendations of the OGC report of 2003 to the Chancellor of the Exchequer, *Increasing competition and long-term capacity planning in the government market place (the Kelly report)*, were applied.

⁴ OGC launched *The Achieving Excellence in Construction* initiative in 1999 to improve Government’s performance as a client of the construction industry.

⁵ www.ogc.gov.uk



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- 08.** There are many practical steps that you can take to get the most out of competition. Indeed, as a procurer you are already influencing the nature of competition in the market for your project, be it national, regional or local, by the actions you are taking – from the preparation of the initial business case through to providing feedback to suppliers on their delivery performance.
- 09.** In this guide, we focus chronologically on a number of different stages of the procurement process, where the actions of public procurers can affect competition:
- Making sure you have enough credible suppliers
 - Capitalising on European Union (EU) procurement arrangements
 - Aggregating contracts
 - Working strategically with other public sector procurers
 - Defining your requirements clearly
 - Choosing your selection criteria
 - Incentivising, measuring and rewarding good performance
 - Managing the supply chain
 - Mitigating the risks of anti-competitive behaviour.
- 10.** Key sources of further guidance in each of these areas are summarised in Annex A.



Making sure you have enough credible suppliers

11. To achieve value for money you need to have a sufficient number of credible suppliers, so that they have the incentive to compete to win your business. Key to ensuring that you have enough credible suppliers is understanding your marketplace; this will help you identify and reduce any barriers to bidding that suppliers may face.
12. One way to make sure you are clear about what solutions are possible and what factors might prevent certain suppliers from bidding is to establish “communities of practice” – a network of both procurers and suppliers that actively seeks to work more effectively together. This will support you in gathering market intelligence about who the suppliers are, the solutions that they are delivering in the marketplace, and their reputation in the eyes of other buyers. It will also help you build relationships with the suppliers themselves.
13. Such approaches to the market have been particularly beneficial in:
 - Encouraging participation of sufficient and capable bidders by understanding, and then reducing, any barriers to suppliers bidding for the work
 - Introducing new ideas to the project that challenge and develop the procurer's initial concepts. Innovation is not limited to design aspects; it may include using new building techniques or materials, as well as innovative financing and operational solutions that minimise whole-life costs
 - Identifying possible risks to delay in advance and seeking design solutions that would allow quicker construction
 - Alerting procurers of post-build operational issues and the implications for ongoing maintenance costs
 - Identifying any supply-side constraints and bottlenecks – particularly in the capacity for certain types of projects, skills or long material lead times – which might exist or be anticipated in the market, and could reduce the number of firms able to bid for a particular contract.
14. Procurers often have a choice either to stagger contracts or to let them all at one time. Letting contracts simultaneously undermines the scope for collusion, which is generally easier when suppliers repeatedly bid against each other for similar contracts.
15. A key rationale for staggering contracts is to smooth demand and so avoid capacity constraints, as well as to avoid placing large amounts of work at times when there is a lack of competitive pressure among suppliers, which may stifle innovation and/or result in poorer value for money. Staggering contracts also allows suppliers the time to adjust to meet your demands, as well as developing alternative and new solutions and, indeed, to learn from the innovations of others and over time. As a procurer, you can take advantage of staggering contracts to obtain and act upon the performance of suppliers, as well as to allow opportunities for new bidders to emerge. It can also allow you time to improve the design of the procurement and contracting processes.
16. However, this is only likely to be successful if you have understood the capacity of suppliers to meet your needs through early discussions, and where your work programme is well publicised, enabling suppliers to anticipate your needs for work. The experience of the Water Service (Northern Ireland) in the box on page 6 provides a good example of this.

Listening to suppliers avoids capacity constraints – Water Service (Northern Ireland)

The Water Service is an Executive Agency within the Department for Regional Development that provides water and sewerage services to over 730,000 domestic, agricultural, commercial and business customers throughout Northern Ireland. It has an annual budget before capital charges of £302 million, and fixed assets valued at £4.9 billion. To provide its services, the Water Service (Northern Ireland) procures goods/materials, services and construction works.

At the planning stage, it was intending to schedule Public Private Partnership (PPP) water services deals at 3-6 month intervals. However, discussions with potential suppliers revealed that capacity constraints and skills shortages would make it difficult for suppliers to bid for more than one project at a time. Staggering the contracts to longer 9-month intervals allowed suppliers to have sufficient capacity to bid for each project. This increased the number of bidders and allowed suppliers the possibility of bidding for follow-on work.

Source: www.waterni.gov.uk

17. Some practical steps to consider include:

- Consulting with suppliers at the feasibility stage, using a “soft market sounding” approach to understand the range of services and construction options open to you, as well as being made aware of projects that have already been delivered successfully. Other procurers and suppliers may also be prepared to suggest alternative solutions or improvements to your current solution that may meet your needs better
- Publicising long-term construction and capital expenditure plans and listening to feedback from suppliers on potential capacity constraints
- Staggering, rather than delaying, work where contractors face capacity constraints. Even when the actual value of demand in any future period may be uncertain, much can be gained by clarifying the nature of that demand with suppliers. However, be aware that this is likely to enhance the ability of your suppliers to collude
- Providing feedback to suppliers on their past performance, including why they were not selected for a particular tender and what they need to do to increase their chances of future success. This will help to maintain interest among your suppliers for future projects and increase the pool of competitive bidders
- Ensuring that communication really is a two-way process – ask for objective feedback from suppliers on your performance as a client and learn from this. Compare it with comments from earlier projects and share this with the project team.

Capitalising on European Union (EU) procurement arrangements

18. The EU procurement regime is sometimes seen as a bureaucratic hurdle to effective procurement. However, it is not only a legislative requirement, but also a tool that leading procurers are using to reinforce competition and achieve value for money. A major advantage of the EU procurement process⁶ is that it opens the scope for competition to EU Member States (and other prescribed territories), at least to the extent that bidders read the advertisement you place in the Official Journal of the European Union (OJEU).
19. In addition, if you are planning to procure several capital projects over a period (usually over the course of the forthcoming year) you can issue a Prior Information Notice (PIN) in the OJEU advising the contracting community of your organisation's future procurement plans. This potentially has a number of competitive advantages:
 - Bidders who have not previously worked with the organisation may be attracted by the absolute scale, value and nature of the potential work
 - New and existing bidders may see value in developing business with you, as well as in possibly identifying opportunities for good levels of joint working, by becoming familiar with your organisation's managerial style, its business practices, needs and requirements. This is likely to be important to a bidder, because potentially it makes it possible for them to reduce bid costs, decrease build times and improve its reputation, paving the way for good levels of customer satisfaction and profitable longer term business relationships.
20. Some **practical steps** to consider include:
 - Issuing a Prior Information Notice (PIN) in the OJEU to ensure that interested parties have as much time as possible to prepare for participation
 - Developing and providing prospective bidders with a good information pack about the proposed project. The pack should ideally include an insight into your organisation's business, its vision, objectives and business constraints, a clear output specification and the flexibility around the timeframes for the proposed work, making clear any mandatory deadlines
 - Making prospective bidders aware of your PIN and OJEU Contract Notices
 - In extreme cases, where feasible, deferring the issue of the OJEU Contract Notice, based on market intelligence, until it is likely to attract better levels of competition
 - Carefully defining your needs in broad terms, accurately estimating the value of the services you wish to procure, and checking that you are not making burdensome requests for information or imposing unnecessary technical barriers to entry.

⁶ Generally, public procurements of civil engineering and building works over the prescribed variable threshold value (just over £3.6 million as of January 2006) are subject to open competition from providers in any EU member state. These procurement rules and buyer obligations are formally set out in the Public Works Contract Regulations 1991 (SI 1991/2680), together with the legal obligations for framework agreements and other forms of public sector contracting (see references in Annex A). Further details on the procurement directives are available on the OGC website – www.ogc.gov.uk – in the Procurement Policy and Application of EU Rules section.



Aggregating contracts

21. An important choice to make in any construction procurement is whether to obtain all of your requirements from one or a number of suppliers. For example, a national client could aggregate all its contracts and choose one supplier to meet its requirements, or it could award contracts to one supplier for a particular region. A local client could choose one supplier to meet all programme requirements for a particular length of time, or choose separate suppliers for different projects.
22. Aggregating or disaggregating contracts can affect competition in a number of different ways. Where there are genuine synergies, such as significant economies of scale, aggregation can enable suppliers to be more efficient and therefore help you to achieve better value for money. Aggregation could also increase the number of bidders because these larger contracts are more attractive to potential suppliers. It may even attract different types of suppliers, as the experience of the Partnership for Schools programme shows (see box below).

Aggregating Contracts to Encourage New Entry – Partnership for Schools (PFS)

Partnerships for Schools (PFS) is responsible for delivering the government's secondary school renewal programme, Building Schools for the Future (BSF).

It works with local authorities and the private sector to rebuild or renew every one of England's 3,500 state secondary schools during the 15-year lifetime of the £40 billion programme.

Local authorities (LAs) aggregate their requirements into a single long-term contract and enter into a Local Education Partnership (LEP) with a private sector provider and PFS. The LEP partner has exclusivity to deliver secondary school capital investment through its supply chain for a period of up to 10 years, subject to meeting a number of Key Performance Indicators (KPIs).

PFS believed that the larger scale of projects would be more attractive to the construction industry and that both the public and private sector would have proportionately lower bid costs. In the initial ten schemes that were put out to tender there was a full open competition to appoint the LEP partner. There were 20 bidders in total for these tenders, including a number of new entrants, such as specialist management companies.

For future investment requirements, not defined in the initial competition, providers will be benchmarked and required to demonstrate that proposals provide value for money. Contracts will be periodically re-competed to ensure value for money in the long term.

As contracts were aggregated on a regional basis, this ensures that there will be a number of bidders at the re-tender stage and helps guard against LAs becoming overly dependent on a limited number of suppliers.

Source: www.partnershipsuk.org.uk

23. But aggregation can also have a number of negative effects on competition:
- It might make it more difficult for smaller and specialist suppliers who only have the required expertise for part of the aggregated contract
 - It removes the ability for you to benchmark the performance of different suppliers providing similar services against each other. It also removes the scope for in-contract competition, where clients shift their requirements between suppliers at the margin, or where a supplier takes over a contract if another fails to perform (see section on Incentivising, measuring and rewarding good performance)
 - It can create incumbency advantages compared with letting multiple contracts, because only one firm will be able to draw on its expertise; for instance, it may have a better knowledge of costs when tendering for future procurements. This may result in an over-dependency on a limited number of suppliers in the longer term.
24. Disaggregation can be used to create a deal flow. This can be used to exert competitive pressure on your existing suppliers to meet their current contractual promises, by offering a strong link between a supplier's performance on past and current projects and the opportunity to win future work.
25. It is important to weigh the potential benefits of aggregating contracts with these costs. A **practical step** you can take when considering whether and how to aggregate your contracts is to consider carefully the following issues, perhaps drawing on the experience of the OGC or procurers of similar projects:
- Will aggregating contracts enable your suppliers to reap significant economies of scale or scope, and therefore offer you better value for money?
 - Will it provide good incentives to invest, by allowing firms to spread and recover the costs of this investment over more projects with a larger stream of revenue?
 - Could an aggregated contract increase the intensity of competition between suppliers for that contract, because winning the contract would result in a significant increase in the winning supplier's revenues, and a significant loss of market opportunities for the losing bidders?
 - Will aggregating contracts reduce deal flow to the extent that there will be limited competition for future work, leading you to become overly dependent on a single supplier, or a limited number of suppliers, and resulting in higher costs in the future?
 - Would the ability to benchmark contracts be a useful tool to sustain in-contract competition between suppliers? If there are significant advantages from aggregating contracts, could this be done in a way that still enables contracts to be benchmarked, e.g. by regionally aggregating contracts and benchmarking regions against each other.

Working strategically with other public sector procurers

- 26. Collaboration activities with other procurers may range from sharing information on procurement needs and the past performance of suppliers, through to running joint procurements and aggregating contracts.
- 27. If you are a relatively small procurer faced with having to negotiate with larger suppliers, by joining up with other procurers you may be able to aggregate your demands across work programmes – this will increase your negotiating strength and enable you to get better value for money. However, you need to be mindful of competition law (see box below).

Competition law in the UK

The Competition Act 1998 prohibits, in certain circumstances:

- Agreements between undertakings which prevent, restrict or distort competition (the Chapter I prohibition)
- Conduct by one or more undertakings, which amounts to an abuse of a dominant position (the Chapter II prohibition).

For example, the Chapter I prohibition applies to agreements between undertakings that directly or indirectly fix purchase or selling prices, or any other trading conditions which have as their object or effect the prevention, restriction or distortion of competition. The Chapter II prohibition provides that the conduct of an undertaking may constitute an abuse if it consists of directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions.

Guidance on the above prohibitions can be found on the Office of Fair Trading website, www.oft.gov.uk

- 28. The Association of Greater Manchester Authorities (see box below) demonstrates that it is possible for local authorities to work together.

Co-ordination between smaller local authorities – Association of Greater Manchester Authorities

The Association of Greater Manchester Authorities (AGMA) was formed in 1986 to act as a single voice for the ten local authorities in Greater Manchester. This has enabled the authorities to pool resources and allowed those authorities with smaller resources to benefit from a stronger negotiating position.

The AGMA Collaborative Services Group was established in November 2004 to exploit opportunities to develop and deliver efficiencies and service improvement through joint or collaborative procurement of provision of goods, services and projects. It is currently exploring opportunities for joint service delivery and strategic partnering in construction-related services and procurement.

Source: www.agma.gov.uk

29. Some **practical steps** you could take include:

- Purchasing jointly to reduce procurement costs, particularly if you are a smaller procurer. But be mindful of competition law, which prohibits undertakings from entering into anti-competitive or restrictive agreements, and from abusing a dominant position
- Sharing information on the costs of individual construction firms and the performance of suppliers more generally, also making use of OGC's Supply Intelligence Service.⁷

Defining your requirements clearly

30. The way in which you define your requirements will affect the number and type of suppliers that bid, and therefore whether you are able to make the most of competition in the market.

31. You need to be able to specify your needs in a way that suppliers can interpret and respond to accordingly. Submitting a bid is a costly process. The more uncertainty suppliers have about your requirements, the less likely they are to incur the costs of preparing a bid. Therefore the clearer you can be about your requirements, the easier it will be for potential suppliers to understand them, and the more confidence they will have when preparing and submitting bids.

32. At the earliest stage of any project, your initial business case will have an identified set of project objectives to be achieved. If these objectives can be converted into desired performance outcomes and communicated to the market at an early stage, this will allow competition between potential suppliers to focus on meeting your needs.

33. There are two broad approaches that can be adopted. For relatively straightforward “commodity-type” projects, you are more likely to be able to specify required inputs and outputs very tightly. This will encourage suppliers to compete primarily on price, as they have little else to differentiate their product or service. For more complex projects, it is more likely that output, outcome or performance specifications are used. These still need to be clearly defined before the invitation to tender or negotiate stage is reached, to encourage effective competition to meet your desired specifications.

34. Some **practical steps** you can take include:

- Defining your requirements as clearly as possible, so that suppliers can be confident that they understand your needs and how best they can meet them. This is likely to encourage them to bid
- Considering the use of bidder conferences (see box on page 12) and other methods of engaging and consulting with suppliers to help define, refine and clarify your requirements. But be careful of how far you take this, to avoid facilitating collusion by suppliers. Particular care should be taken where there are a small and stable number of credible suppliers who are likely to be bidding regularly against one another. See section on “Mitigating risks of anti-competitive behaviour” (page 16) for further information.

⁷ OGC Supplier Intelligence Service (SIS) can assist by providing information and analysis on specific key suppliers and/or supply markets. For further information, contact the OGC Service Desk on 0845 000 4999.



Bidders' Conferences

A bidders' conference can add significant value to your project, by bringing together all potential suppliers and giving you the opportunity to explain your procurement process to all of them at the same time. The conference can also: help provide further insight into what you are trying to accomplish with the project; assist in focusing suppliers on the need to give you best value; and help you refine your specification.

For suppliers with whom you have previously worked, it can be a means of demonstrating that you have alternative suppliers and thus strengthen your negotiating position. But be aware that bringing suppliers together at a bidders' conference could facilitate collusion, particularly if there is a small and stable number of credible suppliers.

Choosing your selection criteria

35. The choice of selection criteria, both their number and weighting, will determine the number and type of bidders you attract and, consequently, the intensity and effectiveness of competition in the tender process. The decision on what selection criteria to use is not only important for the current project, but also in maintaining a pool of potential credible bidders with a continuing interest in bidding for future projects. It is therefore important to ensure that selection criteria are chosen in such a way that credible bidders, including small and medium-sized enterprises (SMEs), are not deterred unnecessarily.
36. Selection criteria are important at two key stages in the procurement process:
 - Pre-qualification of bidders
 - Evaluation of tenders.
37. In both cases, you will need to think through both the quantitative and qualitative criteria, to ensure that there is effective competition and that you are achieving best value for money. Quantitative assessment criteria tend to focus on the whole-life costs of the project. These criteria interact with the qualitative assessment criteria, which relate to the asset's fitness for purpose, e.g. the suitability of the design, the attention to meeting your environmental, sustainability and access agendas, space flexibility and the adequacy of ICT (Information and Communication Technology) connectivity.

Pre-qualification criteria

38. Pre-qualification criteria can be used to filter credible and non-credible bidders, but if used in a heavy-handed way, without good knowledge of the market, can inadvertently narrow the number of suppliers.
39. To identify effective competitors, you do not have to rely solely on your own pre-qualification procedures. If firms know the tender evaluation criteria you will use before they decide to apply, then they can and will self-select. However, it is insufficient to announce that, say, you will give an 80% weight to something called "quality" and a 20% weight to price, if you do not provide clear indication of what you mean by quality and how you will measure it.
40. It is also critically important to consider how to avoid unnecessarily deterring bidders. For instance, if new police station accommodation is being procured, the choice of pre-qualification criteria stating that prior experience of building police stations is required may exclude bidders with a proven capability of building similar units outside the police sector. This may then unnecessarily restrict the choice of potential partners at the pre-qualification stage.

41. Similarly, pre-qualification criteria requiring extensive information on the legal and financial standing of a firm may be relatively easy for a large firm to provide, but may be too burdensome and costly for small and medium size enterprises (SMEs), so creating another barrier to SMEs entering the market. Centralised schemes for registering such information, so that each firm only needs to provide it once per year, can help solve this problem. Constructionline⁸ is a national example.
42. Some **practical steps** procurers can take are:
- Ensuring that pre-qualification criteria are relevant, transparent and designed to obtain a set of effective and credible bidders. Inappropriate criteria can create barriers to entry so, for example, procurers should be flexible in their financial information requirements, and request only that which is needed for financial appraisal
 - Designing the tender in such a way that suppliers (including SMEs) that could be efficient and effective partners are not inadvertently deterred from submitting bids
 - Being aware that extensive requests for pre-qualification information can be burdensome to suppliers and raise the costs of tendering, deterring bidders, as well as often unnecessarily excluding particular types of suppliers who would be capable of delivering an effective performance.

Evaluation criteria

43. Once a set of credible bidders has been short-listed, the choice and disclosure of the criteria to be used to evaluate the subsequent bids is vital to ensure that you make the most of competition among the short-listed bidders. Clearly, value for money is the key consideration. However, this should usually be seen in the context of whole-life value, i.e. the most economically advantageous, rather than lowest cost, bid, as illustrated by the Prison Service example below.

Developing long-term capacity in the market – Her Majesty's Prison Service (HMPS)

The Prison Service has been at the forefront of PFI (Private Finance Initiative) since the mid-1990s, when it started work on HMP Altcourse (Fazakerley) and HMP Parc (Bridgend). These were the first designed, constructed, managed and financed (DCMF) private prisons in the UK. These projects presented a new challenge to the industry, as limited capacity existed to deliver such a wide brief in a specialised market (i.e. the construction and complete operational management of a prison). There were five compliant bids for each project.

The projects were awarded to two different bidders, despite one bidder offering best short-term value for money for both prisons. This was justified because of the need to develop a market for the supply of DCMF prisons and ensure that, in the long term, the Prison Service would be able to achieve value for money.

The dual award started a market base that was added to in subsequent DCMF competitions by two more contractors, giving four contractors for the nine DCMF prisons in England and Wales.

Source: www.hmprisonservice.gov.uk

⁸ www.constructionline.co.uk

44. The choice of criteria can make competition more effective, as it can provide incentives for firms to invest in earning a reputation for trust and quality of performance. However, such criteria could also limit competition, by making it more difficult for you to switch supplier and for new suppliers to enter the market. Therefore, it is also important to consider whether suppliers possess the skills necessary to meet your needs from their experience of delivery in other sectors.
45. Some **practical steps** when considering what selection criteria to use include:
- Keeping bidding costs as low as possible and minimising the administrative burden, by only asking for information that will subsequently be used in your evaluation
 - Giving a new entrant the opportunity to gain experience, e.g. by parceling contracts, so that a number of suppliers are able to invest in a reputation for trust and quality and extending the pool of future credible bidders
 - Providing information about sub-contractors and/or using bidding conferences to open up the opportunity for consortia to be formed (to reduce the costs of searching for sub-contractors when preparing the bid)
 - Allowing, or even encouraging, the performance record in other industries to count in the selection criteria for the bid
 - Communicating clearly the evaluation criteria, and relative weightings, to be used.

Incentivising, measuring and rewarding good performance

46. Suppliers are often selected for their ability to offer quality. It is therefore vitally important that, as a public procurer, you are able to measure this, so that you can ensure whole-life value for money. Monitoring and benchmarking performance is a key way in which you can use competition to achieve this:
- It helps you identify which firms are more efficient and reliable in the marketplace, thereby allowing you to select better value suppliers for future contracts
 - Monitoring the effort and achievements of suppliers in a contract helps ensure that firms are fairly rewarded, encouraging them to bid for future contracts
 - Benchmarking the costs of a supplier against those operating similar contracts can allow you to reward suppliers according to how well they perform relative to other suppliers. This gives good incentives for firms to compete by innovating to improve quality and drive down costs.
47. Another approach to help you provide incentives for firms to deliver on their promises is by rewarding firms that perform well with future work. However, there is an important trade-off to be borne in mind, in that new firms that do not have an established track record can find it difficult to compete for contracts.
48. Rewarding suppliers according to how they meet specified targets is not without its dangers. First, there is a risk that suppliers will perform so as to meet the targets set, rather than the ultimate outcomes desired by the client. Second, it is often important to reward effort as well as achievement, particularly where costs rise through no fault of the supplier.

49. Successful projects are a result of having both a good client and a good supplier: just as suppliers may fail to deliver on their contractual promises, procurers can impose additional demands and costs on their suppliers. Most often this will be done inadvertently. For example, failure to communicate adequately your requirements to your supplier, changing those requirements, or causing delays in a project can all add to the suppliers' costs. Increasing the costs of a supplier in this way can damage your reputation as a client to be trusted. This may deter some suppliers from bidding for your contracts, and those that continue to do so may submit higher bids in order to compensate for the increased risk.

50. Some **practical steps** include:

- Ensuring that you are able to measure the performance of suppliers (i.e. benchmarking), especially where they have been selected on the basis of their ability to deliver quality
- Considering whether you can commit to providing more work for existing suppliers that have performed well, while still encouraging new suppliers. If suppliers feel there is no commitment to honour good performance by providing further work, they will have much less incentive to invest for the future
- Encouraging suppliers to bid for future work by, for example: agreeing to share gains from better-than-expected performance; providing firms with a reasonable rate of return for the effort and resources they dedicate to a project and the output they produce; and engendering a culture of fairness and trust on both sides.

Managing the supply chain

51. Subcontracting and extended supply chains are prevalent in the construction sector. Prime contractors are therefore key players in managing an effective supply chain. The relationship between you and the prime contractor, and the influence you can exert on the prime contractor, will set the tone for how the rest of the supply chain is managed.
52. It is essential to “peer down the supply chain” when selecting your principal suppliers. Often, procurers concentrate on ensuring competition between bidders for main or direct contracts. However, subcontractors can create the majority of the value added in construction, and often the roles that will be “critical” for delivery of promised project attributes or outcomes are subcontracted. Therefore, the credibility of bidders highly depends upon how they, in turn, organise competition for their subcontracts. If, for instance, the prime contractor is appointed on the basis of delivering quality and value rather than lowest cost, but goes on to appoint their own subcontractors solely on a lowest price basis, your needs may not be met and value for money may not be achieved.
53. As noted in a recent National Audit Office report⁹, there is still more to be done to ensure that supply chains are fully integrated. A particular problem noted by NAO was the lack of fair payment practices for specialist suppliers, which reduces the incentive to invest in capacity or innovate and may even threaten a supplier's existence, e.g. if they are not paid for a long time.

⁹ NAO (2005), “Improving Public Services through better construction”, London: Her Majesty's Stationery Office (HMSO).



54. Practical steps include:

- Finding out how the prime contractor selects its sub-contractors
- Helping suppliers (especially SMEs), where possible, overcome regulatory barriers and administrative burdens to encourage more effective competition throughout the supply chain. The Ministry of Defence (MoD) provides an example of this.

Project Bank Account – MoD Defence Estates

The Ministry of Defence (MoD) was concerned that sub-contractors were often dissuaded from bidding for work because of late payments made to them by Prime Contractors (PC). To address this issue, Defence Estates, in collaboration with Bucknall Austin – the project directors who innovated and developed the approach – set up a Project Bank Account (PBA) in trust for the whole supply chain, with payments from it authorised by the client and the PC. The payment system was based on alliance principles, whereby the MoD and PC pay all members of the supply team (including the PC) out of a single bank account, which they jointly run.

Interim applications for payment were put together by the supply chain and interim payment certified by Defence Estates; the allocation of payment was based on principles agreed by all of those involved in the supply chain. The client and prime contractors then certified the payment schedule. After clearance with the MoD's Finance Department, a signed payment breakdown analysis was forwarded to the bank, which then simultaneously made payments from this account to all contractors involved in the supply chain. Defence Estates also had the ability to audit the bank account.

Although this was a more expensive payment mechanism to administer, it was successful in ensuring that sub-contractors were fairly rewarded for their work, by ensuring timely payment of all parties in the supply chain. This efficiency was particularly significant at the lower end of the supply chain, where delays in payment can result in financial charges and interest payments to sub-contractors. It also ensured that the “30-day rule” for payments was achieved.

The certainty of payment and clear demonstration of the MoD working with innovative suppliers encouraged more suppliers with a lower turnover (SMEs) to bid for work.

Source: Ministry of Defence (MoD)

Mitigating the risks of anti-competitive behaviour

- 55.** We have focused in this guide on how to make the most of competition. It is also important to recognise, however, that suppliers can engage in anti-competitive behaviour – there is sometimes a fine line between collaboration and collusion. Anti-competitive behaviour can take many forms. These range from formal market sharing agreements to bid rotation (where firms agree to take it in turns to submit a realistic bid), bid suppression (where one or more firms agree not to bid, or to withdraw their bids) and the submission of cover prices (bids set deliberately too high to win, or with unacceptable conditions). The damage to procurers caused by anti-competitive behaviour can be significant, and felt not only in higher prices, but in poorer quality, a restricted choice of partners and a lack of innovation.

56. The following box outlines the relevant UK competition law.

Competition legislation and illegal cartels

The Competition Act 1998 and Part 6 of the Enterprise Act 2002 have been enacted to tackle cartels and anti-competitive agreements. Where cartels operate, costs escalate, there is less choice and economic growth is stifled.

If a company has any agreements with its competitors to fix prices, to share a market by setting geographical territories or allocating customers, or to conspire together over contracts by bid rigging (collusive tendering), it is likely to be judged to be operating an illegal cartel.

Typically, those involved in a bid rigging cartel work together to decide who will win a contract. Firms may “pay off” those who agree not to tender a bid. They may also provide “cover bids” to allow a competitor to be sure of winning a contract in exchange for a similar favour when future contracts are awarded. It has been confirmed by the Competition Appeal Tribunal that bid rigging is illegal – see *Apex Asphalt and Paving Co Limited v OFT* (www.catribunal.org.uk).

The OFT can impose fines of up to 10% of turnover and individuals can be prosecuted and imprisoned for up to five years for bid rigging and other forms of anti-competitive behaviour.

57. The OFT has fined a number of construction companies for anti-competitive behaviour. An example of a recent cartel case is set out below.

Roofing works cartel – South Tyneside Council

In the summer of 2002, South Tyneside Council placed an advertisement in local newspapers in relation to works at two primary schools. The works included some roofing and consisted of single storey accommodation extensions to both schools, the provision of two new multipurpose halls, alterations to the existing building and some external works. The total value of the package was approximately £1.1 million. Main contractors were invited to apply for this work, and were provided with a list of roofing sub-contractors to invite to tender for the roofing element of the contract.

The OFT subsequently found evidence that two of the roofing subcontractors, Hodgson and Dufell, had engaged in price fixing. Dufell had decided that it did not want to win these contracts, but that it did not want to exclude itself from receiving future enquiries. It therefore did not want to take the time to calculate and submit a competitive tender; nor was it prepared to inform the main contractors involved that it was too busy to prepare a tender. Dufell decided to submit a false bid for the works and, to this end, requested pricing information from Hodgson. Hodgson provided Dufell with this pricing information by fax on 1 October 2002 and Dufell used Hodgson's tender figures to prepare and submit a false and inflated bid for the works.

The OFT concluded that the two parties had engaged in an agreement and/or concerted practice with the object of fixing tender prices, in breach of the Competition Act 1998. Fines of approximately £75,000 were imposed on both of the parties.

Source: www.of.gov.uk

58. As in many areas of business, prevention is better than cure, and there are a number of **practical steps** that you can take to reduce the risks of anti-competitive behaviour:

- Think of using non-collusion clauses and/or certificates of independent bids (self-certification by the supplier that they have not colluded with others, containing warnings exposing those who make false declarations to legal action: OFT can provide recommended text – see Annex A for details) and request the disclosure of subcontractors
- Ensure sufficient credible bidders and regularly review evaluation criteria through careful design of the procurement process itself
- Avoid obligatory bids as a condition of staying on approved lists, but seek objective justification for any failure to bid
- Look for suspicious bidding patterns using the checklist below.

Suspicious bidding patterns – ten things to look out for

- 01.** Bids received at the same time or containing similar or unusual wording.
- 02.** Identical prices.
- 03.** Bids containing less detail than expected.
- 04.** The likely bidder failing to submit a bid.
- 05.** The lowest bidder not taking the contract.
- 06.** Bids that drop on the entry of a new or infrequent bidder.
- 07.** The successful bidder later subcontracting work to a supplier that submitted a higher bid.
- 08.** Expected discounts suddenly vanishing or other last minute changes.
- 09.** Suspiciously high bids without logical cost differences (e.g. delivery distances).
- 10.** A bidder betraying discussions with others or with knowledge of previous bids.

- Know your cost environment and benchmark bids against other procurers (but be aware they might also be victims)
- Keep good notes of all discussions with potential bidders and systematically scrutinise them for suspicious patterns, e.g. geographical prevalence of certain suppliers' areas or the apparent rotation of contracts between suppliers.

If you suspect that you may have been a victim of a cartel, contact the OFT. In order to take action, the OFT needs reasonable suspicion. The OFT has a range of powers at its disposal, including entering premises with a search warrant and searching for documents, and forensic examination of computers. The OFT has a "first past the post" Leniency Programme, which can provide participants in a cartel with total or partial immunity from fines in return for the provision of information which genuinely assists an investigation. You may also be able to seek compensation, via the courts, for losses incurred as a result of cartels. The OFT can be contacted via its cartels hotline, on 020 7211 8888 – all calls are treated in strict confidence. All guidance materials are downloadable from the OFT website (www.of.gov.uk), under Cartels.

Conclusion

- 59.** In this guide we have outlined some practical steps you can take to make the most of competition, as well as pitfalls to avoid.
- 60.** Below are some key questions you should ask yourself and your teams when thinking about the impact of your procurement on competition in the market.

How can we...

- Ensure that there are sufficient credible bids through early engagement with suppliers?
- Make the most of EU procurement arrangements to attract the bidders we want, e.g. through using Prior Information Notices (PINs)?
- Assess the costs, benefits and risks, and make the appropriate choices, when aggregating contracts?
- Work strategically with other public sector procurers, from sharing knowledge through to undertaking joint procurements?
- Define our requirements clearly enough by engaging with the market?
- Choose our selection criteria in a way to optimise the number of credible bids and reduce unintended barriers to entry?
- Put in place mechanisms to ensure suppliers deliver on their promises, by designing appropriate incentives, measures and rewards for good performance?
- Influence the prime contractor to put in place effective arrangements to ensure sufficient “competitive tension” in the supply chain?
- Be more aware of, and mitigate, the risks of anti-competitive behaviour?

- 61.** It is important to remember, however, that competition is not an end in itself, but rather one of the important means by which you can realise the full benefits from effective construction procurement – more reliable, better quality assets with improved track records for operation and maintenance.
- 62.** If you require further advice, refer to Annex A for further information and contacts.



Annex A – Contacts and further sources of information

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More information and further advice on many of the issues covered in this guide can be found in the following publications.

Making sure you have enough credible suppliers

Organisation	Title
Constructing Excellence www.constructingexcellence.org.uk	■ All Construction Key Performance Indicators Pack ■ A Guide to Standard forms of Construction Contract outlining Key Characteristics and Components ■ Rethinking Construction in local government: ten key issues and how to address them
Office of Government Commerce (OGC) www.ogc.gov.uk	■ The Successful Delivery Toolkit ■ Achieving Excellence in Construction guides and publications ■ OGC guidance on using SMEs ■ OGC Supplier Assessment Guidance

Capitalising on EU procurement arrangements

Organisation	Title
Office of Government Commerce (OGC) www.ogc.gov.uk	■ Procurement Policy and application of EU Rules OGC has an important role representing the UK on procurement matters to the European Commission, other EU partners and to the World Trade Organisation and its members, and also in helping departments to apply the rules in the UK.
The European Commission http://www.europa.eu	■ European Commission public procurement website
Tenders Electronic Daily (TED) http://ted.europa.eu	■ Tenders Electronic Daily (TED) The EU database of procurement contracts advertised in the Official Journal.
SIMAP Project¹⁰ http://simap.eu.int	■ SIMAP SIMAP provides background information, links and automatic exchange tools to public purchasers and businesses interested in embracing public procurement opportunities in Europe.

¹⁰ SIMAP stands for "Système d'Information pour les Marchés Publics" (Information system for public procurement).

Aggregating contracts

Organisation	Title
Office of Government Commerce (OGC) www.ogc.gov.uk	Aggregation: is bigger always better? The OGC has also published "Guidelines on factors that can be considered when trying to reduce the risks of over-dependence on a supplier". This is located under the Kelly Programme section of the website.

Working strategically with other public sector procurers

Organisation	Title
Partnerships UK (PUK) www.partnershipsuk.org.uk	■ Partnerships UK projects database
Office of Government Commerce (OGC) www.ogc.gov.uk	■ Supplier Intelligence Service (SIS) OGC's Supplier Intelligence Service (SIS) provides information and analysis on specific key suppliers and/or supply markets. The SIS team gather information from a wide range of sources, including press reports, various commercial databases, direct contact with suppliers, and unique data on suppliers' business with government.

Defining your requirements clearly

Organisation	Title
4Ps www.4ps.gov.uk	■ Guidance to Local Authorities in putting together their Outline Business Case
Office of Government Commerce (OGC) www.ogc.gov.uk	■ A Map of the PFI process ■ Successful Delivery Toolkit Guidance on preparing a business case

Choosing your selection criteria

Organisation	Title
Office of Government Commerce (OGC) www.ogc.gov.uk	■ Examples of standard Pre-Qualification Questionnaires

Incentivising, measuring and rewarding good performance

Organisation	Title
Construction Industry Research and Information Association (CIRIA) www.ciria.org	■ Construction contract incentive schemes – lessons from experience (C554), D Richmond-Coggan, 2001 This publication summarises the findings from a survey of 20 construction projects, which used incentivised contracts. Clients, contractors and consultants from the private and public sector were interviewed and the detailed case studies form part of the report.
Electronic Service Delivery toolkit (ESD) www.esd-toolkit.org	■ The ESD toolkit provides national and local statistics for benchmarking and improvement. It has established itself as a useful tool in helping authorities manage and measure the “e-enablement” of their services. It manages four types of data: ■ Local Authority data, specific and closed within protected, individual workspaces ■ Data that Local Authorities have identified as eligible for sharing and also aggregate analyses of data undertaken by <i>esd-toolkit</i> or other groups that pass results back to the <i>esd-toolkit</i> ■ Discussion forum content and views expressed ■ Personal user information.

Managing the supply chain

Organisation	Title
Department for Communities and Local Government (DCLG) www.communities.gov.uk	■ DCLG guidance on strategic partnering ■ The Strategic Partnering Taskforce Final Report This brings together the Taskforce's principal findings and puts forward its recommendations on what can be done to make partnerships a realistic procurement option for local authorities of all sizes. ■ Small Business Concordat: Good Practice Guide This Good Practice Guide supports the Small Business (SME) Friendly Concordat (Statement of Principles), which has been prepared for Local Authorities in support of the National Procurement Strategy for Local Government. The Guide provides examples of good practice and explains how Local Authorities can frame and deliver their procurement strategies in accordance with the principles of the Concordat.
Small Business Service (SBS) www.sbs.gov.uk	■ Small supplier... better value? This is a new, updated edition of the OGC and SBS booklet, "Smaller Supplier Better Value". It aims to raise awareness of the value for money that small firms can offer, to explore the issues that can make it difficult for them to win public sector business, and to set out some ideas about how public sector procurers can help to lower barriers.
Perform21 www.perform21.com	■ Perform21 is a new initiative offering a comprehensive package of information, advice and guidance to Local Authorities to assist them in the application of a partnered approach to procurement, implementation and management of construction and related projects in order to achieve Best Value through Best Practice. Perform21 has been developed by Knowles Management, an industry leader in the field, in partnership with the Federation of Property Societies (FPS) and with the assistance of eight Pilot Authorities.

Mitigating the risks of anti-competitive behaviour

Organisation	Title
Office of Fair Trading (OFT) www.oft.gov.uk	■ Cartels Hotline The OFT can be contacted via its cartels hotline, on 020 7211 8888 – all calls are treated in strict confidence. More information is available from the website. ■ Roofing cartel For more details of the roofing works cartel in South Tyneside, visit the OFT website.
Organisation for Economic Co-operation and Development (OECD) www.oecd.org	In 1998 the OECD initiated an anti-cartel programme with the adoption of the Council Recommendation Concerning Effective Action against Hard Core Cartels.

General

Organisation	Title
Improvement and Development Agency (IdeA) www.idea.gov.uk	■ IdeA procurement services The IdeA Knowledge procurement resource, provide a range of guidance, good practice and other information on all aspects of procurement. This includes a series of briefing papers on a range of procurement topics, case studies, as well as the latest government guidance on procurement. It also highlights the valuable lessons learnt from the IdeA's procurement-based work within local authorities.
National Audit Office (NAO) www.nao.org.uk	■ Improving Public Services through better Constructions The 2005 NAO report assesses the progress that departments and their agencies have made in improving their construction delivery performance, by examining data on 142 construction projects delivered between April 2003 and December 2004, as well as the impact of relevant OGC initiatives.

Annex B – List of contributors

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- Hampshire County Council
- Highways Agency
- Home Office / Her Majesty's Prison Service
- Local Government Task Force
- Manchester City Council
- Ministry of Defence – Defence Estates
- North West Centre of Excellence
- Office of the Deputy Prime Minister
- Building Schools for the Future (BSF), Partnerships for Schools (PFS)
- Partnerships UK
- Procure 21 / NHS Estates
- Reading University
- Royal Institute of British Architects
- SERCO
- South West Centre of Excellence
- St Helens Council
- TPS consulting

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