



DERBY CITY COUNCIL

**AUDIT AND ACCOUNTS  
COMMITTEE  
12 DECEMBER 2007**

Report of Assistant Director,  
Highways and Transport

# ITEM 7

## Highways Maintenance Term Contract

### RECOMMENDATION

- 1.1 To note the report and the actions that are being taken to improve the management and delivery of the Highways Maintenance Term Contract.

### SUPPORTING INFORMATION

- 2.1 At its meeting on 27 September 2007, the Committee requested that it wished to have the opportunity to have a presentation on the new Highways Maintenance Term Contract and discuss the issues with the managers responsible for the service.
- 2.2 Appendix 2 is a report which briefs members on the issues.

**For more information contact:** Christine Durrant

**Background papers:**

None

**List of appendices:**

Appendix 1 – Implications

Appendix 2 – Update on the Highways Maintenance Term Contract for  
Audit and Accounts Committee, 12 December 2007

<b>IMPLICATIONS</b>
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**Financial**

1. As detailed in Appendix 2.

**Legal**

2. As detailed in Appendix 2.

**Personnel**

3. As detailed in Appendix 2.

**Equalities impact**

4. The delivery of the highways maintenance and transport improvement schemes provide a key contribution to the accessibility of the highway network for all users.

**Corporate objectives and priorities for change**

5. This contract contributes to the delivery of a number of the council priorities. The key priorities are; making us proud of our neighbourhoods, creating a 21<sup>st</sup> Century city centre and leading Derby towards a better environment.

**Update on the Highways Maintenance Term Contract for Audit and Accounts Committee, 12 December 2007**

**1.0 Introduction**

1.1 This report sets out to review previous highways maintenance term contracts, HMTc, and other major scheme contracts that have been procured. It sets out the pros and cons related to the different types of contracts and explains the reason for the new approach that we have developed in procuring and awarding the current contract. The contract was awarded to Alfred McAlpine Government Services Ltd and for delivery purposes is branded 'Derbyroads'.

**2.0 Background**

2.1 Since the council became a unitary authority in 1997 there has been an HMTc to ensure that the Council, as the highway authority are able to carry out its statutory duties in terms of road safety and maintenance of the highway network.

2.2 The contract has changed slightly over the years covering different elements of service delivery, but the key work areas that are in the new contract are:

- Reactive and emergency maintenance works
- Winter maintenance operations
- Planned highways maintenance and transport improvement works

2.3 Within the current contract there is an expectation that at least £4.5m worth of work will be carried out by Alfred McAlpines each year over the five year contract term. Within the terms of the contract works up to a project value of £1m can be delivered through this contract. Any schemes expected to cost over this sum would be subject to a separate procurement process.

**3.0 Review of recent highways contracts**

3.1 There have been three key contracts procured in recent years that have influenced the way in which the Council decided to procure the current HMTc. These include;

- the previous HMTc
- the Inner Ring Road Integrated Maintenance Scheme, IRRIMS
- the East Street refurbishment scheme

**Previous HMTc**

3.2 This 4 year contract, which ended on 3 August 2007, was with Morrison Highway Maintenance Ltd, MHM. It was won under competitive tender, on a traditional ICE 5<sup>th</sup> Edition Contract with a priced schedule of rates. The original contract was tendered and awarded to AWG Highway Maintenance who was subsequently taken over by Morrison.

3.3 Key problems that arose during the contract were:

- fixed schedule of rates – no efficiency incentives, rates fixed at unrealistically low level to win the contract, so contractor's major preoccupation was always about how he could reduce his costs irrespective of performance and client satisfaction.
- fixed 'schedule of rates' type contract worked against the objective of developing a partnership approach

- poor quality of work, especially on routine maintenance; in hindsight we should have used defect clauses
- poor delivery of works on time, no real ability within the contract to deal effectively with this issue, lead to poor public perception
- claims culture developed over the length of the contract due to contractor's inadequate rates leading to increasing losses,
- no single coordination point at the City Council, lead to a lack of overall awareness of contract performance

3.4 At the instigation of the Audit and Accounts Committee in September 2006 an audit was carried out on one of the schemes delivered through this contract, the Chellaston Real Time Information scheme. The key conclusions and recommendations of this audit that were made in June 2007 were:

- there needs to be a performance management approach to the new contract that can focus on the timeliness of scheme delivery
- there is a need for better monitoring of individual schemes, within the context of the wider contract, recognising the impact that poor individual scheme delivery can have on residents and transport users
- an overall contract manager should be put in place to monitor targets and take remedial action when necessary

### **Inner Ring Road Integrated Maintenance Scheme**

3.5 Funding was allocated by the Department for Transport following a major scheme bid from the council to deliver IRRIMS. The works contract was procured as a New Engineering Contract partnership contract (NEC) One of the key reasons for doing this was that, from finding out that we had secured the £10.8m worth of funding, to having to spend the money on works, there was insufficient time to complete the scheme design. Without a full scheme design to price there was no way which we could procure a fixed price or even a target price contract. The contract was awarded on a cost reimbursement basis with a fixed 'profit' element.

3.6 There was always an intention to move to a target price approach in years 2 and 3 of the contract, but the very urgent delivery timetable meant that it was extremely difficult for the designs to keep up with the works programme. Asking the contractor to develop a target price would have delayed the scheme and the agreed spend programme with the DfT.

3.7 However this subsequently left a number of difficult issues for the Council;

- lack of certainty over costs and under-estimates of final outturn figures
- although the contractor should have been providing forecast cost estimates these were never produced on a timely basis and the contract did not allow us to do anything about this
- funding from the Council capital programme having to be approved in retrospect

3.8 This is certainly not the type of payment mechanism that we would want to enter into again. However this would not be possible now for two key reasons. First, there have been changes in the way in which the DfT award major scheme funding as they will only formally sign off funding when a target price has been submitted by a contractor. Secondly, internally there is an acceptance that we cannot bid for funding without having completed significant design work to produce robust cost estimates, including detailed risk assessment analysis.

### **East Street Refurbishment Works**

3.9 These works, at a cost of around £2m, were carried out to replace and improve the paving and street furniture in East Street and Exchange Street. The works were actually carried out

by the same contractor that carried out the IRRIMS contract, using the same NEC partnership contract and using cost reimbursement as the payment mechanism.

3.10 This project was completed within time and budget. The key reasons for this are;

- a much less complicated scheme than IRRIMS
- the risks that could have come to fruition did not all arise
- DCC Sections that have all provided significant input into the scheme due to its high priority; DCC resource intensive during construction stage
- negotiations with STATS went well that enabled their works to be carried out whilst not effecting programme; this is not usually the case
- ground conditions were favourable in Phase 4.

#### **4.0 Procurement of the new HMTC**

4.1 Having learnt a number of lessons from these previous contracts the key elements that we wanted to look for in the new HMTC were:

- partnership approach embedded in contract, non-confrontational
- improved strategic and operational management, individual contract managers for Council and Contractor
- deliver improved service; quality and value for money
- sharing risks appropriately
- flexible scope of contract; encouraging efficiencies
- performance management linked to payment mechanism
- open book/transparency of costs
- fair payments reduces claims culture

4.2 The procurement of the contract took over a year and guidance has been sought along the way from the Head of Procurement and internal audit.

#### **Partnership Agreement and management**

4.3 The contract does come within the NEC suite of partnership contracts. It is based upon having a Partnership Agreement and the contract managed through a Partnership Board, with equal representation from the City Council and Alfred McAlpine. The Partnership has been branded as 'Derbyroads' to try to get away from the traditional client - contractor relationship, which can become more about confrontation and blaming, rather than resolution and shared responsibility. We all need to see this as a partnership not an 'us and them' situation. The Partnership Agreement has within it a vision and values that Derbyroads will strive to achieve:

**Vision:** A strategic partnership with a single identity, structure and shared business processes, delivering innovative, sustainable and valued services.

**Values:** Collaboration, Customer focussed, Innovation, Honesty, Enjoyment

4.4 Part of the partnership approach will be to develop regular dialogue with the Planning and Transportation Cabinet Member, the Planning and Transport Commission and the Audit and Accounts Committee and other Members as they feel appropriate, to address key issues and concerns as they arise.

4.5 A key difference in management approach is the decision to put in place an overall Contract Manager from the Council who can provide the key coordination point for the Council clients to focus any of their concerns and similarly be a key point of contact for the Contractor.

## Payment Mechanisms

- 4.6 A key element of the management of the contract is reflected in the payment mechanism and the link to key performance indicators against which the contractor is measured, and to which payment is linked.
- 4.7 The basis of works payments are either:
- **Cost reimbursement:** for small elements where it is not appropriate to develop a schedule of rates; neither the City Council or Alfred McAlpine are keen on this mechanism as it can be administratively time consuming
  - **Schedule of rates:** the majority of reactive work is still carried out under this pricing structure as it does give the City Council a clear way of estimating and measuring scheme costs that is clearly understood; developed based on realistic costs
  - **Target price:** for schemes over £40,000, with a pain-gain approach; this is only worth doing for larger schemes as essentially it is measured in a cost reimbursement way reviewing the actual payments that are made for labour, plant and materials.
- 4.8 On top of these costs which are calculated for each job an operational overhead figure of 13.8% is applied. This is largely to cover the cost of office-based supervisory and administrative staff based in the depot at Stores Road. This was a figure that was agreed as part of the procurement process.
- 4.9 The performance element of the payment mechanism relates to what is termed the 'Base Fee', which is a further 6% applied on top of all of the works and operational costs comprising 4% management overhead and 2% profit. This base fee is adjusted by plus or minus 2% depending on the Contractor's performance scores against a range of performance indicators. The areas covered by the performance indicators include:
- Timeliness of works
    - Emergency call out
    - Winter maintenance – response and completion
    - Capital and reactive works start and completion times
  - Quality of works
    - Inspections of schemes and reactive works
  - Safe working
    - No reportable incidents, property or utility damage
- 4.10 On annual works that are of the order of £4.5m, the management overhead and profit element within the contract is worth between £180,000 and £360,000, depending on the contractor's performance. The lower figure represents a scenario where the McAlpine only recovers their overhead but makes no profit, the upper figure a scenario that rewards them with double the base profit figure. Therefore any performance improvements that the contractor makes can have a significant affect on their profit and vice versa. McAlpine have made it clear that any contract that returns zero or low profit would be very damaging to their company.
- 4.11 Obviously if works that are inspected are of unacceptable quality then they would be re-done at the contractors expense, as well as being reflected in poor performance of the indicators and hence reducing the base fee.

## 5.0 Conclusion

- 5.1 Having had some very difficult contracts to manage in the past we believe that we have procured a flexible, yet robust, contract that will allow us to improve service delivery to the public, improve the highway asset and continually support innovation and efficiency. The five year contract is extendable by three years, with the agreement of both parties, and if this contract length can be achieved it will reduce the very considerable costs that recent procurement processes have required.