



## Strategic sourcing decision for large regional water company

### the challenge

A regional water company had a goal of reducing their costs and engaged MHC to assess whether outsourcing their Maintenance function would provide tangible cost benefits.

The main challenge was to assess four short-listed respondents (plus an internal, 'insourced bid') from a Request For Tender (RFT) and select one that would meet a wide range of predefined qualitative and quantitative criteria from the client.

The process was made precipitously difficult by the variability of responses and operational models proposed without extensive precedence (i.e. there was risk in the bid's ability to achieve performance targets for the price). This required MHC to devise a new methodology to objectively and rigorously select the best option for the client over the next 4.5 years.

### what Marchment Hill did

Working closely with our client, our assessment of the RFT responses was two-pronged: i) qualitative assessment; ii) quantitative assessment.

#### Qualitative Assessment

Our subject matter experts at MHC and senior members of our client team assessed each of the tenders against a range of predefined non-financial criteria. Firstly, individuals scored each of the tender responses in isolation. Additionally, a group review of outlying scores addressed the issue of inconsistency and error.

N	Criteria	Sub-Criteria	XXX	XXX2	XXX3	XXX4
2.1	Delivery Model	Governance arrangements	3.8	4.3	3.1	4.0
2.2	Delivery Model	Management systems (SGE)	3.5	4.0	3.3	4.8
2.3	Delivery Model	Management of subcontractors	3.0	3.3	2.5	4.0
2.4	Delivery Model	Process & Systems alignment	2.0	4.4	3.1	3.2
2.5	Delivery Model	Amendments to contract agreement	1.3	3.0	1.0	1.8
3.3	Operating Competency	CVs of key personnel	2.1	2.8	2.5	3.9
3.4	Operating Competency	Reference check		4.0	4.0	4.0
3.5	Operating Competency	Quality of subcontractors	3.5	3.2	3.1	3.3
4.1	People Management	HSE Performance	4.0	4.0	5.0	5.0
4.2	People Management	Retention of existing workforce (%)	3.0	4.0	3.0	1.0
5.1	Customer Service	Ability to achieve performance targets	2.0	3.8	1.8	3.5
5.2	Customer Service	Customer service policies & procedures	3.8	3.1	3.1	4.1
6.1	Ease of Implementation	Effectiveness of mobilisation / transition plan	3.3	4.0	4.0	3.9
6.3	Ease of Implementation	Ability to maintain service during transition period	3.0	3.5	3.3	2.9

Figure 1 - Table of Averaged Data (Non-financial)

#### Quantitative Assessment

Whilst financial elements like total bid price, labour rates, management overheads and activity costs were a straightforward comparison, devising a risk-adjusted price required a nuanced approach. We were very conscious about ensuring the bid prices

put forth by tenderers was both attractive yet realistic. This was critical since cost overruns would ultimately be a cost partly shared by our client, making unrealistically low bids unattractive. To overcome this obstacle, MHC mapped out the operational risks against each bidder, as well as the client. A sample of these categories is captured in figure 2, below.

Risk Area	Risk Example	Risk Level				
		Insignificant	Low	Medium	High	Very High
<b>Inefficient Labour Capacity</b>	Service Provider is able to cover the maintenance volumes with the number of resources listed and meet all service levels	Resource numbers are higher than Water Plan, very unlikely to miss Service Levels or GMP target	Resource numbers are similar to XXXX new baseline, very unlikely to miss Service Levels or GMP target	Resource numbers are 5 to 10% lower than XXXX, meeting Service Levels and/or GMP target will require efficiency gains	Resource numbers are 10 to 20% lower than XXXX, meeting Service Levels and/or GMP target will require large efficiency gains	Resource numbers are 20% or more lower than XXXX, Service Levels are likely to be compromised and GMP target is unlikely to be met, without reduction in planned
<b>Lack of I.T. Integration</b>	Service Provider has the capability to perform optimal scheduling through GPS capability and able to monitor the activity costs through timesheets and provide the relevant information	N/A	Service Provider will provide Timesheet and GPS capability and require minimal integration between systems	Service Provider will provide Timesheet and GPS capability and require complex integration with ERP systems	Service Provider expects XXXX to provide timesheet and GPS capability ready for start of contract and require complex integration with ERP systems	N/A
<b>Unlikely to reduce GMP Years 5 - 9</b>	No mechanism (or penalties) to ensure GMP reduces over the 3 years of the contract	N/A	Contract Framework has a method to define activity costs and has year on year	Management governance and supporting systems to control GMP costs	Service Provider has ability to negotiate contract after Year 4	N/A
<b>Aging Workforce impacting performance</b>	Cost of workforce higher and productivity lower due to older workforce	N/A	Service Provider has several contracts enabling them to draw upon a	Service Provider highly reliant on XXXX staff and has to recruit to supplement staff	N/A	N/A
<b>Unable to negotiate optimal EDA</b>	Ability to negotiate an EBA that keeps the labour costs down whilst increasing productivity	N/A	Service Provider has negotiated multiple EBA which ensure XXXX labour and productivity rates	Service Provider is reliant on XXXX to negotiate the EBA	N/A	N/A
<b>Non Compliance to Contractual Framework</b>	Service Provider complies with the Contract Framework	Minor wording changes that does not affect the structure of the Contract Framework	Multiple wording changes that does not affect the overall structure of the Contract Framework	Service Provider would like the GMP to be volume based to reduce the risk of the volumes cause a major cost issue	Service Provider would like to change the statement penalties and have the ability to renegotiate the contract after the	N/A

Figure 2 - Risk criteria

Each bid's risk (including the insource bid) was assessed by MHC experts and senior members of the client team as being Very High, High, Medium, Low or Insignificant. Their final risk score was taken as their maximum risk in any category. Their final overall score for risk-adjusted price was moderated by their bid price, as shown in Figure 3, below.

Risk Adjusted GMP	Rating				
Risk Value	1	2	3	4	5
<b>Risk</b>	Very High	High	Medium	Medium	Low
<b>Price Risk</b>	Any Price	Any Price	Similar to Water Plan (within 5% cost)	Lower than Water Plan	Lower than Water Plan

Figure 3 - Risk Scoring Table

All bids ended up receiving a final score and this was presented to the client in the form of a business case report which also took exogenous considerations into account, for example: the strategic benefits of outsourcing vs. insourcing.

the benefit

Whilst the outcome of the top two bids, one being the 'insource bid', was quite close, our analysts ultimately recommended the client outsource their Maintenance activities. Our sensitivity analysis indicated that the client could expect between 7.5 - 9.5% cost reductions below the water plan over the course of the 4.5 year period.

Interestingly, the recommended bidder was the second cheapest option. Our risk assessment of the cheapest bid determined it to be unfeasible and highly unlikely that they would be able to deliver the full range of works and maintain service levels for the price and resources indicated. This objectivity was well received by the client who had full confidence in our analyses and is currently in the process of adopting our outsourcing recommendation.