

3. CHANGE OF CONTRACTING PRACTICES: PROPERTY UNIT

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The purpose of this report is to seek Council approval for negotiating a Facility Maintenance Management (FMM) contract with City Care for the maintenance of the Council's property portfolio.

EXECUTIVE SUMMARY

The report presents background information highlighting the obligations and high level of complexity of current contractual relationships, aimed at maintaining the Council's property assets. It also presents a summary of the evolution in management practice of maintenance contracts from a task defined environment to an outcome defined one.

Best practice is identified in the related processes of Facilities Maintenance Management (FMM) and Supply Chain Optimisation (SCO). FMM is defined as a performance based partnership between a primary provider and the Council. SCO is the supporting process of rationalising the contractual relationships necessary to provide the FMM services. The implementation of FMM by other councils (Auckland and Wellington) has resulted in cost savings in excess of 40%, for values of more than \$1M.

The recommended approach to developing the Council's capability to tender a comprehensive FMM contract is detailed, including significant constraints impinging on the process. A large portion of the scope of work is committed to City Care under existing agreements, making City Care the preferred option through which to engage the process. A staged process of supply optimisation while developing joint capability is recommended.

BACKGROUND

Administering Contracts

The Council currently has in place over 400 different formal and informal contracts with over 100 different suppliers for maintenance of property.

This large number of contracts and suppliers creates a significant workload just in administering the flow of work, payments for work done and contract renewals and re-tenders. This means that at times Council officers have difficulty in achieving key Council policy outcomes owing to the time involved in managing maintenance processes.

City Care

Last year the Council sold the building services business (which was part of the Plant and Building Services Unit) to City Care. The sale and purchase agreement sets out an expected work contract value for building services work totalling \$1.48m per annum reducing by 10% per annum with a term of 4-5 years starting from 1 July 2001. This covers building work for housing, leisure facilities and community facilities and includes building repairs, painting and refurbishment activities. City Care has a stated direction of developing its facility maintenance management capabilities.

Form of Contracts

Over the last few years there has been a substantial change in the approach taken to contracting. The traditional way of contracting for maintenance services has been to use the method based approach. This style of contract sets out in great detail the way the work is to be carried out (the method to be used) and how many activities are anticipated.

This results in a complex schedule of items where the contractor prices each item, with the sum of these totalling to the contract price. This approach requires extensive supervision of the work to ensure that the way we said the work should be done was adhered to. It also results in a lack of initiative from contractors in determining innovative options for completing tasks. This lack of initiative also means that contractors tend to stay in their capability niche as a grass mowing contractor or a footpath surfacing contractor.

This style of contracting supports a reactive approach to asset maintenance with the contracts let when there is an identified problem to fix. Currently we spend approximately 80% of our maintenance budget on reactive work. In other areas of Council contracting, we have demonstrated that moving to a proactive maintenance regime can produce significant cost savings as the need for call-outs and after hours work is reduced.

Organisations such as the Council now focus more on the end result of the work and use performance based contracts to achieve this. This approach requires the client to be quite clear about the standards to be maintained, the levels of service to be achieved and the need for flexibility in the methods employed.

The result has been to reduce the level of supervision required with a move to an audit based approach. This also simplifies the administration of the contract and provides opportunity for the contractors to gain 'competitive advantage' through development of innovative solutions. The taking of initiative by the contractors also results in them looking to expand outside their specific area of expertise as they recognise the opportunity to leverage their existing capabilities.

The next stage in this development is for contractors to recognise their potential to add significant value to their clients. This will be achieved by the contractor providing a single point of contact for all maintenance work on an asset; integrating financial, customer response and asset systems with the client; providing up to date reporting on asset condition and work being undertaken and carrying out self-audits of performance. This is called a Facility Maintenance Management approach (FMM).

Facility Maintenance Management

A recent review of the Housing Team disclosed that this team was spending a disproportionate amount of its time managing the maintenance process rather than delivering the Council's tenant support policy. The solutions that emerged from consideration of these issues were that the Council could gain benefit from addressing its supply chain (the number of contractors providing maintenance services) and from considering the form of contract it was using.

Best practice nationally and internationally supported the introduction of a Facility Maintenance Management (FMM) contract covering the total maintenance activity for the property portfolio. The key aspects of this style of contract are:

- It is performance based with the Council setting out the standards to be achieved (rather than how to do the work);
- It requires the contractor to determine the appropriate maintenance programme and solution for the asset (rather than the Council telling the contractor what to do and when to do it);
- It puts in place a lead contractor for all the work required to maintain the assets with the lead contractor employing the specialist sub-contractors (rather than the Council having a relationship with all of the contractors employed for each part of the work maintaining the asset); and
- It is a partnership between the lead contractor and the Council with information being openly shared and innovation fostered (rather than a 'them and us' contractual relationship).

A key aspect of putting in place a FMM contract is the process of improving the relationships with sub-contractors; this is referred to as Supply Chain Optimisation (SCO).

Supply Chain Optimisation

Improving our supply chain is a continual focus for the Council. The area of property maintenance provides an opportunity to simplify contractual relationships and reduce contract administration effort as well as producing cost savings from the better packaging of work.

The traditional procurement of FMM services has involved a chain of independent supplier organisations. Typically, each link in that supply chain has been an 'arm's-length' pact. Buyers shopped for price (lowest cost provider) and (sometimes) performance in the open market.

Driven by competition, supply chains in every industry are moving toward integration. The demands on individual organisations have become too vast to allow them to continue operating in isolation. For a company to deliver maximum value to its customers, it must receive maximum value from its suppliers. A contract or any amount of bargaining power cannot create these benefits. Benefits can only be gained in an environment of co-operation and mutual commitment.

By definition, a strategic alliance is a relationship between organisations in which they co-operate to produce more value (or at a lower cost) than is possible in a market transaction. To create that value, they must agree on what 'the value' is, use each other to achieve it, and then share the benefits. Without a shared objective, meaningful co-operation is not feasible. If they do not share the benefits, they cannot expect the commitments required for co-operation. For alliances between customers and suppliers, an elaborate web of joint tasks is created and these are governed by a set of agreed principles.

The greatest benefits of customer-supplier alliances come from continuous improvement over the long term. Such improvement calls for ongoing alignment of organisation priorities and resources, which requires top-to-bottom connection at all relevant policy and operating levels. If decisions on matters like capacity and technology development are made separately, partner firms may evolve away from meeting each other's needs. Further, to create the most value, a supplier must adapt its organisation for each customer interface, reflecting the need for resources, structure, and practices that are unique for each situation.

FMM alliances work better when an organisation reduces the number of suppliers to a select few. This creates scale economies, gives each remaining supplier a better chance to win more of the customer's business, and facilitates closer working relationships.

Moving towards a **single supplier strategy** introduces both cost and performance effectiveness opportunities. Single supplier sourcing promotes greater commitment to forming an alliance and this fosters best practice initiatives and innovative developments that assist the asset user. By giving a single supplier more reliable and greater volumes of work the supplier can discount cost by volume yet protect the supplier's cost structure. This methodology works particularly well where similar skill sets (i.e. within engineering services or cleaning services) can be utilised during single site visits.

FMM single supply strategies have been successfully applied to Local Authority FMM contracts (as well as to private sector organisations such as Telecom NZ, Carter Holt Harvey and NZ Post) by the Auckland City Council and the Wellington City Council. Case study examples follow:

Wellington City Council – aggregated and rationalised all FMM services (engineering, cleaning, grounds and gardens, et al) in to one lump sum comprehensive performance based service contract. Five year term. Savings in excess of \$1.1M per annum (45% saving).

Auckland City Council – Staged, aggregated FMM supply chain exercise. Lifts and escalators completed with one supplier providing all Council lifts and escalator maintenance, with a 55% cost saving per annum.

Council Approach to FMM – The Property Portfolio

Supply Chain Optimisation

The first step in optimising our supply chain will see us rationalise the major engineering service contracts, which are currently awarded to several firms under a variety of arrangements. Each class of engineering service will be awarded to a single supplier (unless there are joint ventures), with a comprehensive performance based contract. This will result in the following contract structures. Future contract values are unknown at this time, but are expected to represent savings over the aggregate present value:

Category	Before 1		After	
	Contracts/Suppliers	\$ p.a.	Contracts	~\$ p.a.
Lifts and Escalators	33 / 2	~\$100,000	1	TBC
Fire, Safety & HVAC	347 / 31	~\$350,000	1	TBC

A limited number of suppliers have the capability to fulfil these contracts. The contracting process for each of these categories is as follows:

1. Draw up a performance based contract for each class of service.
2. Where more than five (5) firms are known to be engaged in fulfilling a particular service, invite expressions of interest (EOI) from the market.
3. When applicable, select from the EOI process the five that best meet the attributes of the performance based contract.
4. Invite proposals (tender) from the short list of suppliers.
5. Award the contracts on the basis of fitness to perform and price.

A similar performance based service agreement will be drawn up to cover other work currently awarded to City Care and a number of smaller contractors for grounds & gardens and building refurbishment work. This agreement would also incorporate provisions for managing sub-contractors and providing customer response management for issues forwarded by the Council for resolution. This will result in the following contract structure.

Category	Before 1		After	
	Contracts/Suppliers	\$ p.a.	Contracts	~\$ p.a.
Grounds & Gardens	/ 9	~\$200,000	1 City Care	TBC
Building Maintenance	/ 115+	~\$1,900,000		
Contract & Customer Management	0	0		

Given that City Care provides a significant part (50%+) of these services under existing long term arrangements, including the sale and purchase agreement, a different contracting process is needed. The process needs to allow for the fact that other contractors provide specialist services, such as electrical and plumbing response based maintenance, for which City Care currently has limited capability. The following process accommodates this:

1. Draw up a performance based contract.
2. Invite City Care to price this contract.
3. City Care to negotiate with a range of sub-contractors for the specialist work they do not currently provide (plumbing and electrical).
4. Award the contract to City Care on the basis of a negotiated price including the value of the sub-contract work.

It is proposed that all these performance based contracts be awarded for a five year term, this period being considered the shortest length viable in this type of arrangement. An initial five year term also allows for the development of the Council's and City Care's capabilities in managing and running FMM style contracts, as well as the full rationalisation of existing contracts which still have time to run. At the end of the contract term, it is the intention that the engineering services (lifts, HVAC, Fire Service) will be incorporated into the full FMM contract.

It is proposed to negotiate a contract with City Care Ltd (who will negotiate or tender with subcontractors) with a current approximate yearly additional value of \$1M. Section 247E of the Local Government Act requires that where the Council is contemplating entering into any contract for the supply of services that is likely to involve the Council in expenditure that the Council considers significant, the Council shall consider whether or not the matter shall be put to tender. Where the Council decides not to put out to tender such a contract, the Council must record the reasons for its decision in writing.

It is considered this contract should not be tendered for the following reasons:

1. Existing contractual obligations preclude entering into a comprehensive FMM agreement with any supplier other than City Care, to which a substantial part of the work is already committed.
2. Developing a thorough understanding of FMM requirements through a staged approach will ultimately enhance the ability of the Council to successfully tender a full and comprehensive FMM contract at a later date.

3. It would not be good management practice to defer introduction of this maintenance process (FMM) until the sale & purchase arrangements expire, given the benefits it can deliver:
- Housing staff will be freed to enhance levels of service to housing tenants in accordance with the tenant support policy.
 - Reduced overhead and administration cost involved in maintaining over 200 suppliers.
 - Development of City Care's FMM capability will result in it becoming the only Christchurch based and owned provider for this type of service, enabling it to compete for other external work.
 - The Christchurch City Council will ultimately benefit from the development of City Care's FMM capability through dividends accruing from its commercial contract.

FMM Contract

The process of putting a full FMM contract in place is expected to take 12-18 months. This timeframe recognizes that there is a considerable amount of process to be put in place by both City Care and the Council to successfully manage such a complex contract.

The sale and purchase agreement for the transfer of building services provides a substantial framework on which to build the FMM contract with City Care. The proposed contract will however extend beyond the sale and purchase agreement in terms of the range of activities covered, the yearly value of work and the length of contract. This will require a separate report to the Council seeking approval of the negotiated contract, most likely in the April/May 2002 round of meetings.

In broad terms the process for putting a full FMM contract in place, and the pathway to either publicly tendering or re-negotiating is:

Stage 1 – Put contracts for lifts, fire and safety and HVAC in place – March/April 2002 (EOI/RFP tender process).

Stage 2 – Negotiate contract with City Care for the supply of gardens and buildings maintenance and overall contract and customer management – April 2002.

Stage 3 – Pass the task management responsibility for lifts, fire and safety and HVAC to City Care under the FMM contract – mid 2003.

Stage 4 – Public re-tender/re-negotiation of the full FMM contract – April 2007.

CONCLUSION

Nationally as well as internationally, Facilities Maintenance Management (FMM) has been recognised by public and private organisations as the key to effective maintenance of property assets. As a large owner of property assets, the Christchurch City Council is well positioned to reap significant financial rewards from introducing this management process. Introduction of FMM has yielded savings in excess of 30% in both Auckland and Wellington.

The implementation strategy included in this report presents a staged approach that will yield maximum benefits to the community.

- Recommendation:**
1. That the concept of FMM and its implementation be approved.
 2. That City Care Ltd be nominated as the FMM provider of choice for the purposes of negotiating an FMM agreement based on the provisions of the existing sale and purchase agreement, with the draft FMM agreement to be subject to final ratification by the Council, via a further report to the Property and Major Projects Committee.
 3. That, for the purposes of section 247E of the Local Government Act 1974, it be recorded that the Council has decided to negotiate a contract with City Care Ltd rather than calling tenders for the contract, for the reasons set out in this report.

Chairman's

Recommendation: That the above recommendation be adopted.