Network Outcomes Contract Governance & Management Group Clarification	
Reference Number:	NOCC No. 24
Subject Title:	Rehabilitation Base Preservation Quantities Reconciliation Process
Issue Date:	26 September 2017
Clarification Purpose	Clarification is provided to ensure the NOC is being interpreted consistently. The clarification does not remove or supersede the Network Outcomes Contract documentation.

SUBJECT

The Contract contains a mechanism to reconcile the funded and completed rehabilitation works against the Contractors Tendered cumulative Base Renewal Preservation Quantities (BRPQ). This mechanism seeks either:

- A reduction in the Routine Sealed Pavement Maintenance lump sum where the Principal funds additional rehabilitation works over and above the Contractors Tendered Annual Cumulative BRPQ and has been SM018 justified, or
- Pavement maintenance risk will pass over to the Principal if the Principal is unable to, or chooses not to fund SM018 justified pavement rehabilitation renewal projects where this results in the Contractor being prevented from implementing the renewal investment levels as set out in the Contractor's tendered BRPQ.

Two questions have arisen:

1. The Contractor is able to show that while more renewals have been done on the network their forward projection of future pavement repairs exceeds their tendered assumptions and therefore challenges the philosophy that an increase in rehabilitation works will correspond with a decrease in routine sealed pavement maintenance.

2. Can the Agency confirm the approach for the BRPQ reconciliation process and its application in the Network Outcomes Contract?

BACKGROUND

The Contract has been developed such that the Principal desires the Contractor to adopt a stewardship role over the State Highway network and has nominated renewal investment levels for the Contract period. The BRPQ were based on Principal's assessment at the time of tender for the Contract of what would be required to adequately preserve the network's asset over the Contract period and beyond. The BRPQ investment must then be balanced by an appropriate routine maintenance strategy, which in turn is used to deliver relevant maintenance activities against the Routine Sealed Pavement Maintenance lump sum agreed in the Contact. As part of the Contractor's Maintenance Management Plan (MMP), the Contractor is required to distribute these BRPQ over the contract period through its baseline plans. This must then be balanced by the Contractor's own maintenance strategy as articulated in the MMP.

At the Time of Tender

During the tender phase, it was necessary for the Contractor to carry out detailed Network assessment and modelling to formulate their overall maintenance strategy, and corresponding lump sum requirements based on the Principals BRPQ investment level.

Reconciliation Approach

There are numerous references to how the baseline plan annual reconciliation process works, which defines when/where/how/who in terms of risk changes. These are repeated throughout the NOC MS whenever the renewal topic is raised; i.e.

- MS 2.5.4 Changes to Annual Renewal Investment Levels
- 6.1.2 Pavement Rehabilitation
- Appendix 2.4, Process Maps, includes the Management of Annual Rehabilitation Quantity process map.
- Variation benchmark questionnaire

In essence to best serve the best needs of national Network prioritisation, and to take account of the funding capabilities of the Principal, the Base Renewal Preservation Quantities may still vary from the quantities nominated within the contract. If this occurs, the Baseline Plans will become a reference point during **each year** of the Contract Period, to quantify the impacts of any interference with the previously developed investment levels.

INTENT

The Baseline plan is there for the protection of all parties (The Client, the Supplier, the Network).

The intent was, NZTA are obliged to fund every rehabilitation project that is 'justified', up to a maximum level of the baseline plan accumulated quantity, each year, as protection for the Supplier.

This also means that NZTA have the right to decline funding more than the accumulated baseline quantity, in any year, without incurring a risk change claim from the Supplier, protection for the Client.

The intent was that NZTA would not simply default to 'Only funding up to the baseline plan quantities, but fund what was best for network (justified), even if over the baseline plan and NZTA could afford to financially, for protection for the Network.

It should be made clear that if NZTA fund a renewal, it is only because it is submitted by the Supplier and justified.

If NZTA fund more than the Suppliers accumulated baseline plan, then NZTA are entitled to money back from the suppliers lump sum (either pro-rata or a one off credit), protection for the Client and the Network.

PROCESS

It is still necessary for the Contractor to carry out detailed modelling, programme optimisation and prioritisation on an **annual basis**. The Contractor will then need to make a case to the Principal, in order to be able to apply the base renewal preservation quantities. This is in accordance with the annual plan process, The Annual Plan Instructions Manual (SM018), and the Principal's nominated prioritisation process.

Annual Plan Instructions state that the renewals Do Minimum scenario means the minimum level of routine and reactive maintenance necessary to maintain compliance with Contract OPM's.

To take account of the funding capabilities of the Principal, the Base Renewal Preservation Quantities may still vary from the quantities nominated within the contract. If this occurs, the **Baseline Plans will become a reference point during each year of the Contract Period**, to quantify the impacts of any interference with the previously developed investment levels.

Process Map 2.5.4/6.1.2 shows the annual cycle for the management of the Rehabilitation Quantity.

The following Table sets out a simplified process for assessing the impacts of the base preservation quantities.

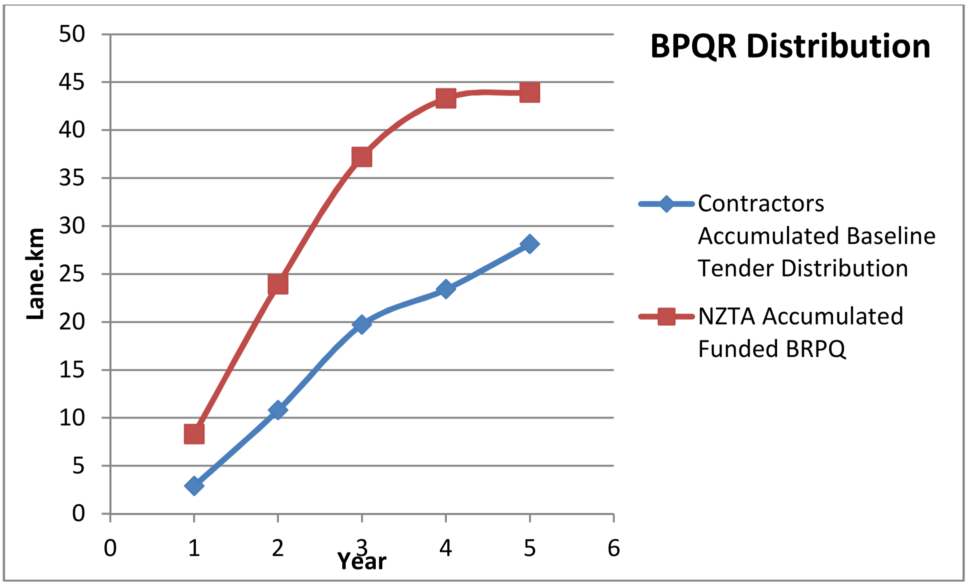
Time Line	**Principal**	**Contractor**
At time of Tender	Sets the BPQR's	Articulates their Base Renewal Preservation Quantity distribution strategy (by lane length) over the Contract Period
Annual Plan Process		On an annual basis, the Contractor makes a case to the Principal, in order to be able to apply the base renewal preservation quantities. In accordance with the annual plan process.
	Assess the validity of the proposal (that is the sites are NPV justified) and whether the accumulated funded plan varies from the quantities nominated within the contractors Tender. Note: the Principal need only fund up to the justified quantities per year (based on the justified cumulative BRPQ) if this is below the Contractors nominated distribution	For sites which are promoted but the Principal has rejected the NPV justification, the Do Minimum maintenance risk sits with the supplier within their lump sum

Time Line	Principal	Contractor
On release of Funded Plan	Prioritise sites where funded plan varies from the justified quantities nominated.	
Site Prioritisation	Priority should be based on NPV justification, road class, and as detailed within the Contractor's MMP	
Annual Field Inspection	In August of each year a joint inspection (if required) is completed to confirm the year 1 holding costs to be transferred. Note, this should be the same or very similar to the NPV do minimum year 1 holding costs.	
Annual Financial Impact for under funding	Principal arranges payment to the Contractor for the agreed Do Minimum holding cost completed works	Contractor completes agreed holding treatments
Annual Financial Impact for over funding	Principal receives an invoice credit note from the Contractor	
End of Contract Reward	The Principal will assess key elements of the Contract delivery to determine the appropriateness of a reward	

EXAMPLES

Example 1: Where the NZTA has over funded from the start of Contract and the sites are all considered NPV justified

Date	2014/15	2015/16	2016/17	2017/18	2018/19
Contractors Cumulative Baseline Tender Distribution (Lane.km)	2.9	10.8	19.7	23.4	28.1
NZTA Cumulative Funded BRPQ (Lane.km)	8.3	23.9	37.2	43.3	43.9
Annual Difference Funded (Lane.km)	5.4	13.1	17.5	19.9	15.8



The Impact from this example:

Year 1, Contractor gives a credit note to NZTA for 5.4 lane.km year 1 holding costs on lowest priority sites

Year 2, Contractor gives a credit note to NZTA for 13.1 lane.km year 1 holding costs on lowest priority sites

Year 3, Contractor gives a credit note to NZTA for 17.5 lane.km year 1 holding costs on lowest priority sites

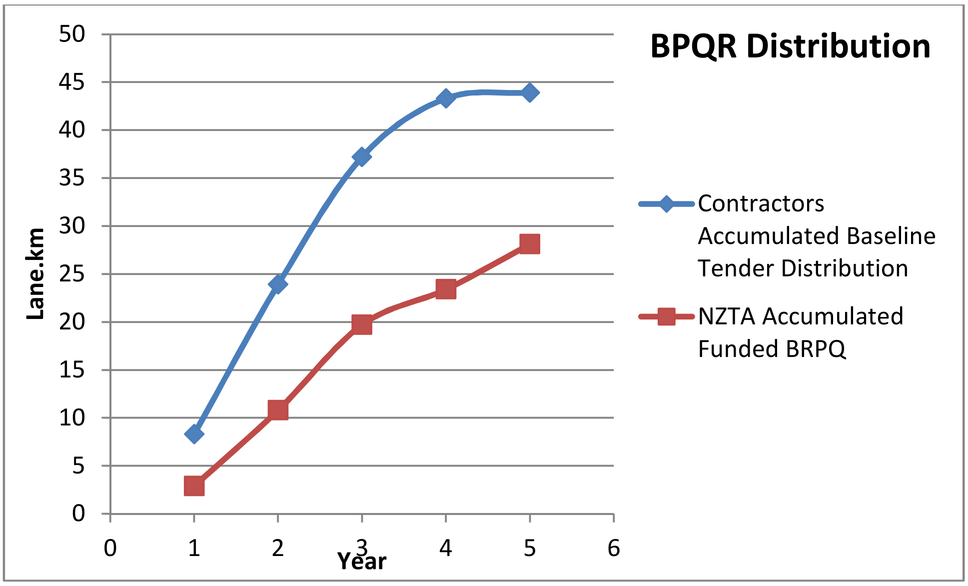
Year 4, Contractor gives a credit note to NZTA for 6.1 lane.km year 1 holding costs on lowest priority sites (refer points of note 3 below)

Year 5, Contractor gives a credit note to NZTA for 0.6 lane.km year 1 holding costs on lowest priority sites (refer points of note 3 below)

Overall, the Agency has funded an additional 15.8 lane.km to that specified in the tendered program. The Contractor has returned year 1 holding costs on 42.7 lane.km for the 5 year term.

Example 2: Where the NZTA has under funded from the start of Contract and all the Contractors sites are considered NPV justified

Date	2014/15	2015/16	2016/17	2017/18	2018/19
Contractors Cumulative Baseline Tender Distribution (Lane.km)	8.3	23.9	37.2	43.3	43.9
NZTA Cumulative Funded BRPQ (Lane.km)	2.9	10.8	19.7	23.4	28.1
Annual Difference Funded (Lane.km)	-5.4	-13.1	-17.5	-19.9	-15.8



The Impact from this example:

Year 1, NZTA arranges payment to the Contractor for 5.4 lane.km holding costs on lowest priority sites

Year 2, NZTA arranges payment to the Contractor for 13.1 lane.km holding costs on lowest priority sites

Year 3, NZTA arranges payment to the Contractor for 17.5 lane.km holding costs on lowest priority sites

Year 4, NZTA arranges payment to the Contractor for 19.9 lane.km holding costs on lowest priority sites

Year 5, NZTA arranges payment to the Contractor for 15.8 lane.km holding costs on lowest priority sites

Overall, the NZTA has not funded 15.8 lane.km to that specified in the tendered program. As a consequence of not funding justified sites up to the Contractors tendered program the NZTA has paid for holding costs on 71.7 lane.km for the 5 year term, which is the summation of each of the annual differences where the Agency has underfunded.

POINTS OF NOTE

1. Assessment of BPQR and the associated impact

The Contract documents are clear that reconciliation of the BPQR is undertaken annually to assess the ongoing impact on either the Contractor or Agency.

2. Impact on quantum of pavement repairs

The mechanism has as its basis that an increase in rehabilitation works will correspond with a decrease in routine sealed pavement maintenance. The Contractor was required to at the time of tendering to carry out detailed Network assessment and modelling to formulate their overall maintenance strategy, and corresponding lump sum requirements, this was the Contractors risk.

If as a consequence the Agency had only funded up to the Contractors BPQR tendered distribution and the Contractor realised a higher quantity of pavement repairs the risk would sit squarely on the Contractor and within their lump sum.

Given an example where the Agency has chosen to fund in excess of the Contractors BPQR tendered distribution and the Contractor still realises a higher quantity of pavement repairs the risk still sits squarely on the Contractor and within their lump sum. However, under this scenario the Contractors risk has been offset by the Agency funding additional justified sites above the tendered BPQR.

3. Holding Costs

The Annual Plan instructions are clear that the Do Minimum scenario for rehabilitation and Resurfacing activities means the minimum level of routine and reactive maintenance necessary to maintain compliance with Contract OPM's and as such year 1 holding costs of the Do Minimum should be reflective of the infield costs. Differences between the infield costs and NPV calculated costs for the Do Minimum in Year 1 bring into question the validity of the NPV submitted to justify a treatment.

Under Example 1 the Agency cannot seek year 1 holding costs in excess of sites to be funded even though the quantum far exceeds the tendered distribution. This is because year 1 holding costs can only be applied to next years funded sites, the Agency cannot seek holding costs beyond year 1 for sites which have already been completed.

Under Example 2 the Contractor is able to seek annual holding costs on all sites which were NPV justified but not funded for year 1 and beyond until such time that the justified site is treated.

4. Aligning sites to cumulative lane.km length

The process for reconciliation is defined by cumulative lane.km. It is very unlikely that where adjustment to the BRPQ occurs they will directly equate to one or more individual sites. To address this difference prioritisation must be completed first. Starting with the lowest priority site first, the site length needs to be compared to quantum of difference based on that years reference point. A percentage is then developed which is used to calculate the quantum costs paid to either the Supplier of the Principal.

If for example the Principal funded an extra 1 lane.km and the lowest priority site was only 0.6 lane.km in length and the second lowest priority site was 0.7 lane.km in length then the Principal would seek a credit for 100% of the year 1 holding costs on the lowest priority site and 43% of the year 1 holding costs on the second lowest priority site.