

Subject	Bitumen volume based contract price adjustment for cost fluctuation
Circulation	All Territorial Local Authorities Auckland Transport Department of Conservation Local Government New Zealand Highway and Network Operations (NZ Transport Agency) Association of Consulting Engineers NZ (ACENZ) NZ Contractors Federation Inc. Roading New Zealand
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This general circular was first issued in November 2012 and included the instructions for using bitumen volume based contract price adjustment. This version does not include the instructions. For the current version of the instructions go to the NZ Transport Agency's website:

<http://www.nzta.govt.nz/resources/procurement-manual/procurement-tools.html>

Refer to the 6th bullet under the heading 'Infrastructure'.

Purpose

The purpose of this general circular is to:

1. introduce a new method of contract price adjustment for cost fluctuation, able to be used on all reseals contracts and other contracts which include the supply of bitumen
2. remind road controlling authorities (RCAs) that it is the NZ Transport Agency's expectation that contracts will include a rational and fair way to manage bitumen cost fluctuation risk
3. advise RCAs that the Transport Agency's *Revised reseal* index (introduced in 2001) will cease to be published once existing contracts that use this index have ended; and
4. advise that the Transport Agency expects that no contracts let after 1 February 2013 will use the *Revised reseal* index.

Introduction

The Transport Agency publishes cost indexes to be used to adjust contract prices for cost fluctuation. These indexes include several which are used on infrastructure contracts including the *Revised reseal* index introduced in 2001¹.

The bitumen volume based contract price adjustment for cost fluctuation methodology, being introduced through this general circular, replaces the *Revised reseal* (2001) index method from 1 February 2013. The Transport Agency will continue to publish the *Revised reseal* (2001) index for as long as is necessary to accommodate existing contracts

This new Bitumen volume based contract price adjustment method is a significant departure from the current method. It uses an index to calculate the compensation for fluctuations in the cost of inputs excluding bitumen but in addition it uses the change in a bitumen cost adjustment dollar series, applied to the volume of bitumen supplied in a month, to adjust contract price for bitumen cost fluctuation.

The need for change

On a number of occasions in recent years, when the price of bitumen has changed rapidly, the *Transport Agency revised reseal* (2001) index has evidently not tracked these changes well. Many contractors now lack confidence in this index. This new method of contract price adjustment uses a significantly different approach. It not only uses a new bitumen cost adjustment dollar series, which is expected to better track changes in the cost of bitumen, but also, and most importantly, it uses the volume of bitumen supplied in a month.

These changes are expected to restore contractor's confidence that bitumen cost fluctuation risk will be managed fairly. In the medium term purchasers can expect to obtain better value for money through better management of this risk.

New tools on the Transport Agency website

There are three new Procurement manual infrastructure tools on the Transport Agency website - <http://www.nzta.govt.nz/resources/procurement-manual/procurement-tools.html>:

1. *Bitumen volume based contract price adjustment for cost fluctuation* - a document which describes the method and includes model contract provisions
2. *Latest index values for 2012 infrastructure cost indexes* - the indexes published through this spreadsheet include indexes for 'costs excluding bitumen' and are intended to be used with the bitumen volume based contract price adjustment method. Index values will be updated quarterly
3. *Latest values for the NZ Transport Agency bitumen cost adjustment series* - this spreadsheet table of cost adjustment series values will be updated monthly.

¹ To avoid confusion it is referred to in this general circular as the *Revised reseal* (2001) index.

A web based tool to perform the bitumen volume based contract price adjustment calculations is being developed. It will also be placed on the Transport Agency's website.

Transport Agency policy requirements

The *Bitumen volume based contract price adjustment for cost fluctuation* document sets out how the Transport Agency will calculate both the *NZ Transport Agency reseals index (costs excluding bitumen)* and the *NZ Transport Agency bitumen cost adjustment series*, and how purchasers are expected to use them.

The Transport Agency's policies on contract price adjustment for cost fluctuation under infrastructure contracts are set out in the Transport Agency's *Procurement manual* section 6.6. It states that "With best practice risk management, risks that cannot be managed by suppliers, such as inflation, should not be passed to suppliers. An approved organisation that does not apply cost fluctuation adjustment to its contracts (and passes cost fluctuation risk on to the supplier) may pay more as a result."

The manual goes on to say that using a Transport Agency published cost fluctuation adjustment mechanism is "the most practical way to manage inflation risk long-term and help approved organisations obtain value for money."

The Transport Agency does not require approved organisations to make provision for contract price adjustment for cost fluctuation in infrastructure contracts. However, the Transport Agency strongly advises all approved organisations to ensure that cost fluctuation risk in those contracts which include bitumen supply is managed in a rational way that is fair to all.

Building the new method

A cross sector group developed the bitumen volume based contract price adjustment methodology. It comprised representatives of the purchasers, both the Transport Agency and local authorities - through local Government NZ (LGNZ), suppliers - through Roothing NZ who also represented the NZ Contractors' Federation and the Association of Consulting Engineers NZ (ACENZ).

Enquiries

For further information on this general circular, please contact Bernard Cuttance at the Transport Agency Auckland Office on 09 969 9856 or by email bernie.cuttance@nzta.govt.nz.

Attachments

There are no attachments to this general circular.



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