

BITUMEN COST ADJUSTMENT SERIES CHANGE

General Circular No° 19/04

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Circulated by	Tara Macmillan, Senior Manager Procurement
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PURPOSE

This general circular advises a change to how Waka Kotahi NZ Transport Agency is calculating monthly values for the bitumen cost adjustment series. The bitumen cost adjustment series is used with the bitumen volume based method of contract price adjustment, which is described in the [instructions for infrastructure contract price adjustment](#).

Approved organisation 'purchasers' and their suppliers who have contracts affected by this change do not need to take any specific action in response, providing they are using the [Adjuster](#) to calculate the cumulative cost fluctuation adjustment figure to the end of each month, and are following the advice in section 7. in the above [instructions](#) when preparing contract progress payment claims.

PLEASE NOTE - discussions with Civil Contractors NZ (CCNZ) and bitumen suppliers, on how to fairly introduce this change, are ongoing. An interim value for the bitumen cost adjustment series was published on the Transport Agency website for the month of November early in the month and added to the [Adjuster](#). However, that value has subsequently been changed. It has been increased from the first published figure to a final figure of 0.6438 \$/litre.

Established Transport Agency practice has been to publish the [bitumen cost adjustment series](#) value for any given month, and add it to the Adjuster, on or about the third working day of the month. This practice of publishing the value for a given month early in the month will cease for the time being. Until further notice the value for any given month may not be published until later in the month.

EFFECTIVE DATE OF THESE CHANGES

The first value for the bitumen cost adjustment series, calculated using the new approach, will be for November 2019 and will determine bitumen cost adjustment payments for work completed during November. Referring to the note above - the final value for November will be added to the [Adjuster](#) by 2 December at the latest.

WHY A CHANGE IS NECESSARY

The Platts Singapore high sulphur fuel oil (HSFO 180) price has been used by the Transport Agency for more than 15 years as a surrogate for the price of bitumen. The HSFO 180 price has been an input to the Bitumen cost adjustment series since the bitumen volume-based method of contract price adjustment was introduced in 2013. Prior to that the HSFO 180 price was used to calculate a bitumen price index.

International marine regulation changes to be introduced in January 2020 mean that the close relationship between the price of HSFO 180 and that of bitumen that has been the case to date may not hold in the future. There is a high likelihood that there will be a divergence in the two prices. The price of HSFO 180 has been quite volatile in recent months, suggesting that this divergence might have already started.

The Transport Agency has been aware of the risk that movements in the price of HSFO 180 will cease to be an appropriate proxy for movements in the price of Bitumen for some time. It has been working with contractors, through CCNZ and New Zealand bitumen suppliers to find a replacement for HSFO. We have engaged with local authorities through the REG Procurement Working Group. We have sought specialist advice from PwC New Zealand (PwC).

As we have worked to find a replacement for HSFO 180 we have been mindful of the principle that risks should be managed by those in the best position to do so. We have also been conscious of the need to maintain the conditions necessary to enable others to import bitumen, given the structure of the bitumen supply market in New Zealand and that there is one only local manufacturer (Z Energy) who also supplies the majority of the bitumen used on New Zealand roads.

Key to the ability to import has been the fact that HSFO 180 is a traded commodity and it has been possible for importers to obtain hedging instruments that have enabled them to manage their exposure to changes in bitumen prices between when they pay for the bitumen they import it and when they on-sell it or use it.

Advice received from PwC suggests that Dubai crude is an appropriate replacement for HSFO 180 in the Adjuster. The Transport Agency has consulted with various parties on the use of Dubai crude and, following feedback, has decided to adopt Dubai crude as the proxy for bitumen in the Adjuster. Therefore, the November and subsequent bitumen cost adjustment series values will be calculated using the Dubai Crude price published by the World Bank. Dubai Crude is able to be hedged.

The situation we now face is not ideal. Z Energy has decided to base its bitumen price on the bitumen price published by Argus Singapore. The Transport Agency considered using the Argus price as the HSFO 180 replacement, but the Argus price cannot be hedged. Many CCNZ members would have preferred that the HSFO 180 price be replaced by the Argus price. They point to what they see as a heightened risk that Z Energy pricing and the Transport Agency's bitumen cost adjustment series will not follow one another.

THIS CHANGE MAY BE A SHORT-TERM CHANGE

Using the price of Dubai Crude, in place of HSFO 180, as the basis for calculating the bitumen cost adjustment series will continue until further notice but it may not be a permanent change. A better basis for the series may be able to be found. The Transport Agency has agreed to keep talking to industry stakeholders (contractors and bitumen suppliers) about the best and fairest basis for the series.

FURTHER UPDATES

This general circular has been emailed to all who are registered as [Procurement Manual](#) users. Further updates on how the bitumen cost adjustment series is being calculated and managed will similarly be sent to registered manual users. To register use this link to add your name and email address to the list of users.

ENQUIRIES

All enquiries relating to this circular should be directed to procurement@nzta.govt.nz.

Nga mihi,



Tara Macmillan

Senior Manager Procurement