

# Is tendering really the way to go?

Competitive tendering is a common practice, but research suggests that it may not only hinder efficiency, it may also encourage some questionable actions.



**COMPETITIVE TENDERING** is entrenched in New Zealanders' psyche as the way to procure construction, but who is best served by this approach? Research over the last 4 years suggests that the answer could be no one.

The PhD research through the University of Canterbury sought opinions about the competitive tendering process from those actively involved in the construction industry, including main contractors, subcontractors, consultants, architects and clients.

## **Why clients like tenders**

The findings show that clients choose competitive tendering as they believe it will identify and secure the optimum price for their build.

However, focusing on cost can attract unintended consequences, not only detracting from the quality of the finished product but also increasing the final build price. For those carrying out the construction, the margins achieved on completion also often fall short of those anticipated at the tendering stage.

## **When competition causes inefficiencies**

A look at the actions of those involved at the pre- and post-tender stage in the procurement process explains the link between competition and inefficiency.

Traditionally, the average commercial project may see between three and five main contractors asked to submit a bid. Main contractors then request pricing from their own subcontractors. Historical relationships between main contractors and subcontractors often mean they have those they would prefer to work with.

## **Lack of trust plays out**

In other instances, there can be a lack of trust between parties. This lack of trust that, balanced against a desire to work alongside preferred contractors, drives what can be seen as undesirable tender practices.

Subcontractors were found to protect themselves by holding on to a prepared tender for as long as possible, submitting to the

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main contractor just prior to the close of tenders. Even then, many submissions are invariably strewn with tags.

From the perspective of some subcontractors, this minimises the time available for a main contractor to shop around or reveal their price to a favourite subcontractor, who may subsequently undercut them.

It also limits the time a main contractor has to thoroughly evaluate the compliance of a tender, especially one of a more technical nature.

Some reading this may refute that practices such as price shopping exist in New Zealand, confident that assurances of confidentiality are robust. Regrettably, however, others found this to be a familiar sequence of events.

#### **Tags may foster pricing advantage**

Tags can be included within tender submissions for legitimate reasons, such as when a discrepancy may exist between a drawing and specifications. They may also occur as the result of a strategic business decision to disguise an artificially low tender and foster an early pricing advantage.

For example, a subcontractor will offer pre-arranged discounts on their bids to preferred main contractors as a way of improving the possibility of both parties securing a contract. This type of arrangement is ordinarily intentionally discreet.

#### **Worries about payment**

There can be several reasons why a subcontractor would offer selective pricing advantages. The most obvious is that some main contractors are poor or late payers, so a subcontractor will be prepared to give away some margin on the basis that aiding a particular main contractor will improve their own cash flow. Main contractors that do not withhold retention payments from subcontractors commonly go to the head of the preferential main contractors list.

The notion of price discrimination also persists because many main contractors and subcontractors appreciate the tangible benefits of the efficiencies that can be achieved from ongoing working relationships. Subcontractors, in particular, are aware that good project management drives efficiencies across a project.

A degree of manoeuvring during the tendering process is understandable as companies attempt to align with organisations that offer the greatest efficiencies, equating with a positive impact on the bottom line.

#### **Post-tender manoeuvres**

This drive to improve profitability showed up frequently during this research, especially during the post-tender negotiation stage,

once a contract has been awarded to a main contractor and prior to letting to subcontractors.

Although it is frequently a requirement that main contractors include trade summaries, this does not always eventuate. Sometimes, it is an oversight, but at other times, summaries may be intentionally withheld, enabling the opportunity for further negotiation.

Post-tender negotiations between main contractors and subcontractors are understandable and acceptable in most instances. What upsets many subcontractors is when a main contractor who has won a contract partially on the basis of the subcontractor's bid, then goes on to retrospectively financially squeeze the subcontractor by seeking discounts and reductions.

Subcontractors often work on meagre margins and may relent under pressure rather than lose a potential contract. The trickle-down effect is that the subcontractor then pressures their own supply chain or seeks to minimise their own costs by substituting materials with cheaper alternatives.

#### **Advantages of negotiating**

With the enormous demand for construction in Christchurch, we are witnessing a transition away from competitively tendered projects to more negotiated contracts.

However, negotiated contracts usually only extend to include the main contractor, and up to 95% of the value of most construction projects rests with subcontractors, who continue to be recruited by competitive tender.

This means we are inadvertently diminishing many of the advantages that negotiating may bring to procurement by ignoring where most of the costs and opportunities for savings and efficiencies are.

#### **Competition model has flaws**

There are other forms of procurement that the industry here and overseas is reluctant to widely adopt, continuing to remain committed to competition as a mechanism to achieve value.

Arguably, this is a flawed model, encouraging behaviours during both the pre- and post-tender stage that many in the construction industry consider to be unethical and that may inadvertently have ongoing repercussions impacting the quality of the built environment and the productivity and efficiency of the industry. ◀

**Note** Mark Hinton was a BRANZ scholarship recipient. The opinions expressed in this article are those of the author and do not necessarily reflect those of BRANZ.