Cost Reimbursable

Procurement Requirements

VICTORIA State Government | Treasury and Finance

The Secretary
Department of Treasury and Finance
1 Treasury Place
Melbourne Victoria 3002
Australia
Telephone: +61 3 9651 5111
dtf.vic.gov.au

Authorised by the Victorian Government
1 Treasury Place, Melbourne, 3002

ISBN 978-1-925551-87-7
Published September 2023

If you would like to receive this publication in an accessible format, please email information@dtf.vic.gov.au

This document is also available in Word and PDF format at dtf.vic.gov.au

Contents

1. Introduction

1.1 Purpose

This document is one of a suite of publications that constitute the Department of Treasury and Finance's (DTF) whole of government Infrastructure Procurement Framework (Framework).

It sets out the Victorian Government's requirements for cost reimbursable procurement in High Value High Risk (HVHR) projects. It may also be used for cost reimbursable procurement in non-HVHR projects as appropriate.

The document is for use by Victorian Government delivery agencies, or portfolio departments where the delivery agency is separate from the department. It is also for use by other industry practitioners, government stakeholders, tenderers and advisers who wish to understand the Framework.

The document covers the procurement and delivery phases of a project. It discusses:

- the suite of cost reimbursable procurement models
- assurance, approval and governance requirements
- policy requirements and best practice
- the use of competition in cost reimbursable procurement models
- value-for-money (VfM) assessment requirements
- probity and disclosure requirements.

Chapters 1 to 3 detail key government policy requirements when undertaking cost reimbursable procurement.[1] Chapters 4 and 5 detail best practice guidance when using these procurement models.

The Treasurer may elect to nominate a project to be delivered in accordance with the requirements of this document where the project is considered to have sufficient cost reimbursable characteristics.

The document is not to be used for selecting a project's procurement method or packaging approach. Procurement and packaging options are usually assessed as part of the business case, following the Procurement Investment Lifecycle and High Value High Risk Guideline (Procurement ILG) available on DTF's Procurement ILG webpage.

Before beginning procurement, the delivery agency should consider whether any changes in circumstances have altered the rationale for selecting cost reimbursable procurement for the project or package.

[1] In these sections 'should' reflects something that is strongly recommended and under normal circumstances should be implemented.
The term 'consider' means taking the matter into account for the relevant procurement model and activity, as appropriate for that procurement.

1.2 Context

The Cost Reimbursable Procurement Requirements fit within the Framework.

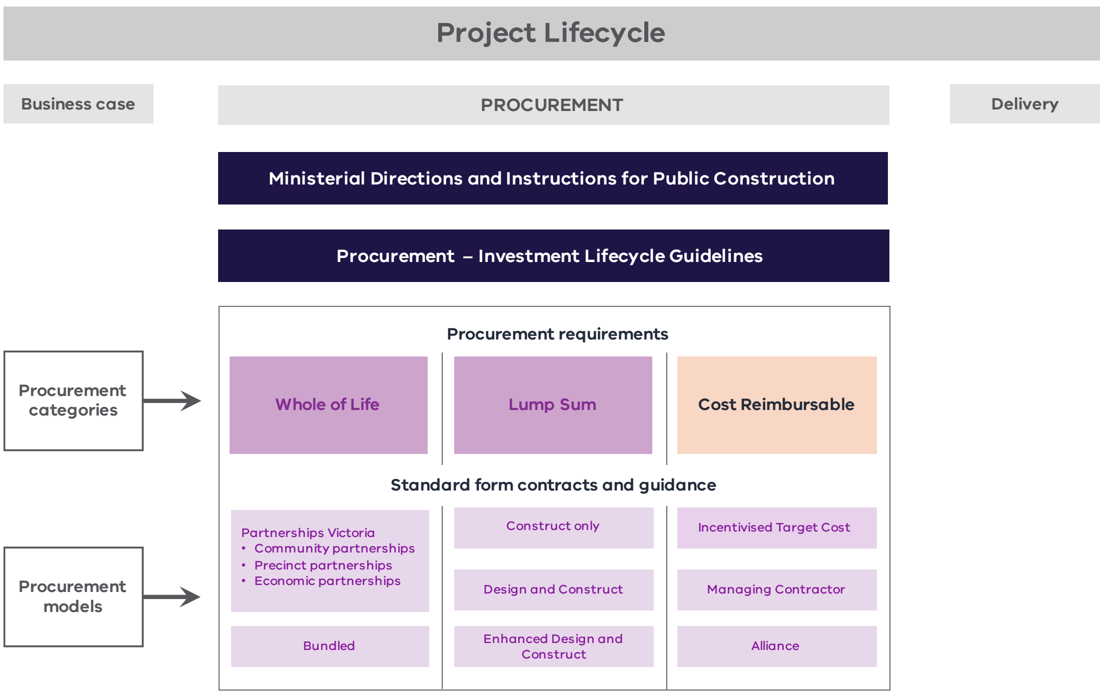
The Framework includes three categories of procurement, comprising whole of life, lump sum and cost reimbursable, with each category containing a set of approved procurement models for use on Victorian Government infrastructure projects.

It consists of the following policy, guidance and standard form contracts:

- the Ministerial Directions and Instructions for Public Construction Procurement (Ministerial Directions), established under Part 4 of the *Project Development and Construction Management Act 1994* (Vic)
- the Procurement - Investment Lifecycle Guideline, which outlines the three procurement categories and a set of approved procurement models
- a Procurement Requirements document for each of the three procurement categories
- standard form contracts and guidance for a subset of the approved procurement models.

Figure 1 provides an overview of the Framework and indicates where the Cost Reimbursable Procurement Requirements sit within it.

Figure 1 – Victorian Government Infrastructure Procurement Framework



Other Victorian Government legislation, policies and frameworks that are applicable across the project lifecycle include:

- the Standing Directions 2018 under the *Financial Management Act 1994* (Vic)
- the Investment Lifecycle Guideline (ILG) series
- the Asset Management Accountability Framework, Investment Management Standard and Bid Cost Reimbursement Policy for Major Construction Projects
- the High Value High Risk (HVHR) project assurance framework and associated Gateway Review Process.

National policies, such as the National Alliance Contracting Guidelines, may also be applicable.

Where there is a difference in the application of this document from the National Alliance Contracting Guidelines, the requirements in this document take precedence.

1.3 Cost reimbursable procurement

Cost reimbursable procurement models can optimise project outcomes for the state when used appropriately.

Key characteristics of cost reimbursable procurement models can typically include:

- payment by reimbursable cost mechanisms (in part or in full)
- payment of a fixed percentage-based margin for contractor overhead and profit
- commercial frameworks between the delivery agency and contractor to share risks and opportunities in project delivery
- incentive based payment regimes for select performance criteria
- elements of greater cost transparency and use of open-book pricing
- ambition to align the interests of all parties to achieve agreed project outcomes to varying degrees.

Cost reimbursable procurement recognises there are certain project risks that cannot be effectively priced or programmed on a fixed price or program basis, and therefore should not be fully allocated to the contractor. It also recognises that specific risks can still be effectively priced and allocated to the party best able to manage them.

Cost reimbursable procurement models promote collaboration between the participants and encourage effective and innovative solutions in project delivery. These models embed collaboration by capturing some or all of the following characteristics:

- governance arrangements that facilitate collective problem-solving and decision-making, including 'best-for-project' decision-making and issue resolution
- commercial incentives and contractual commitments between the contractor and delivery agency supporting behaviour frameworks, including for the parties to act in good faith
- early and ongoing engagement between delivery agencies and contractors throughout delivery of the project.

Cost reimbursable procurement models are sometimes referred to as collaborative contracting models.

1.4 Cost reimbursable procurement models

A range of cost reimbursable procurement models can be used to deliver infrastructure in Victoria. These models include:

- incentivised target cost (ITC)
- managing contractor (MC)
- alliance.

Details about each of these models, including contracts and accompanying guidance, are available on the Cost Reimbursable Procurement webpage.

1.4.1 Incentivised target cost

The ITC procurement model features elements from the traditional design and construct and alliance models. The ITC model allows for risks to be shared, while allocating some risk (such as time and quality risk) to the contractor as the party best able to manage these risks.

The standard ITC model typically includes a two-stage approach, including a:

- **development phase:** where shortlisted respondent(s) are engaged to perform early work including design work and developing a project proposal incorporating a target outturn cost (TOC). The TOC is the estimated cost of completing the contracted works and achieving the minimum outcomes required by delivery agencies for the project
- **delivery phase:** which proceeds on an open-book basis where the state reimburses the contractor for actual incurred costs of performing the works and a percentage for corporate overhead and profit. It also includes a cost gainshare/painshare adjustment to incentivise cost control and a performance regime to incentivise key delivery and project outcomes.

1.4.2 Managing contractor

The MC procurement model traditionally involves the delivery agency engaging a contractor who is responsible for all aspects of project delivery, including:

- managing the coordination and completion of design and construction documentation
- tendering and awarding trade packages
- managing the work of the subcontractors and other activities on site through to completion and handover.

The MC procurement model typically comprises two stages, including the:

- **development phase (Stage 1):** which involves the contractor progressing design, preparing construction documentation, identifying and commencing early works and submitting an offer to the State for construction of the works. The offer typically includes a schedule with completion dates and a Guaranteed Construction Sum (GCS), being the estimated cost of delivering the works
- **delivery phase (Stage 2):** where subject to acceptance of the GCS and program by the State, the contractor proceeds to construct and commission the works, with an agreed date for practical completion. The contractor manages design and construction risks, including the schedule.

The contractor typically carries out subcontracting in close consultation with the delivery agency. The delivery agency keeps authority to approve or reject tenderers. This level of consultation enables the delivery agency to maintain reasonable control over the design process and construction, where appropriate.

The contractor is reimbursed for actual costs on an open-book basis plus fixed fees or percentage margin for preliminaries, overheads and profit. It may also receive additional incentivised payments through contract mechanisms that reward performance or achievement of specific key result areas (KRAs), for example cost savings.

If the contractor fails to meet the agreed completion date(s) liquidated damages may apply.

1.4.3 Alliance

Under the alliance procurement model, an alliance is formed between the delivery agency and non-owner participants, comprising the contractor, designer and other contracted parties, to design and construct a project.

The alliance participants work together in good faith and as an integrated team to deal with key project matters on a 'best-for-project' basis. The parties share risk, responsibilities and rewards in delivering the project.

A TOC and proposal for delivery is developed as part of procurement for the project. A contractor is then selected for delivery of the project.

Contractors are commercially incentivised under cost gainshare/painshare adjustment, where costs below and above the TOC are shared between the parties using a pre-agreed percentage split. Performance regimes are also used to incentivise the contractor to meet certain behaviours and obligations.

The delivery agency reimburses the non-owner participants on an open-book basis, including agreed corporate overheads and profit (COP) margins. Typically, the State pays the total cost of the project delivery. Only COP margins are at risk for contractors. The delivery agency takes 100 per cent of cost overrun risk beyond that point.

Legal rights to litigate against breach of contract, mistakes and negligence can be limited under an alliance. The model relies on a 'no blame, no disputes' philosophy.

Chapter 5 provides further detail in the commercial framework for each model.

2. Governance, approvals and assurance

This chapter outlines governance, probity and the integrated approval and assurance requirements.

2.1 Governance roles

Governance is defined as the system by which a project is controlled and operated and the mechanisms by which accountability is upheld.[2]

Strong governance is integral to successful project delivery. Cost reimbursable governance systems are characterised by high levels of transparency and shared accountability to optimise project delivery and meet agreed project outcomes.

2.1.1 Ministerial oversight

Each project requires ministerial oversight. The relevant portfolio ministers or ministers are responsible to the Government and the public for actions taken under their authority for delivering, managing and implementing the project.

[2] Delivery agencies should also refer to the Procurement ILG which provides general guidance on governance for the procurement phase of a project and the ILG governance technical supplement.

2.1.2 Delivery agency

Delivery agencies are responsible for the project and securing the agreed outcomes and outputs. Delivery agencies should obtain the required government approvals detailed in this document, establish governance systems and a project team, manage key stakeholders and deliver the project in line with government policies and objectives.

Delivery agencies are also responsible for project appointments and may consult with DTF on key appointments.

2.1.3 Department of Treasury and Finance

The Treasurer has whole of government responsibility for sound financial management. DTF supports this role through:

- developing and implementing infrastructure policy frameworks and standard deeds
- supporting selection and delivery of projects, including providing independent advice to the Government on significant issues and facilitating key project approvals
- undertaking assurance to monitor the progress and performance of projects and readiness to advance at key project milestones.

2.1.4 Office of Projects Victoria

The Office of Projects Victoria (OPV) provides project advice to the Government, with a focus on technical aspects of project development and delivery. It undertakes specific assurance reviews, and provides advice and resources to delivery agencies to support project outcomes and address specific project needs. It also develops systemic project delivery improvements targeting more productive infrastructure delivery.

2.2 Governance plan

A governance plan should be approved by the Government as part of the business case. It needs to be updated before procurement commences and reviewed at conclusion of the procurement phase ahead of project delivery.[3]

[3] The governance plan typically forms part of the procurement plan, completed after business case approval. Delivery agencies should refer to the Procurement ILG for guidance on the purpose and content of the procurement plan.

Delivery agencies should consult DTF when developing governance plans, incorporating DTF's participation across all levels of the governance system. DTF should be provided with the opportunity to participate on the following or equivalent bodies:

- **steering committee:** the governing and decision-making body with overall responsibility for delivery. The steering committee is not a consultative or noting forum. It should endorse key procurement recommendations including milestones before key government approvals
- **working groups:** undertaking project development activities including tender documentation, VfM framework, commercial framework, contractual risk positions and documentation, principal's benchmark (the State's independent estimate of completing the contracted works), TOC and other benchmarking activities
- **procurement and evaluation panels:** undertaking key negotiations, including participation in executive evaluation panels and relevant evaluation working groups.

OPV will also participate in project governance as required and agreed in the Project Assurance Plan (PAP) (see section 2.3.1).

2.2.1 Contents of governance plan

Governance structures identified in the governance plan depend on the procurement model being used.[4] While integrated governance and joint decision-making can drive project outcomes, governance structures should balance delegating and sharing decisions within the project with maintaining overall state accountability for the project delivery and outcomes.

There are key areas for which the State should keep ultimate decision-making power during the procurement and delivery of projects, including:

- variations to scope or design, cost and project timelines, including adjustments to the TOC. These include approval of adjustment events that are predefined circumstances in project delivery where adjustments are made to the TOC, scope, performance regime and the dates for completion
- variations to risk positions and allocations from approved project deeds and previously agreed positions
- development of the principal's benchmark (if applicable)
- development of the gainshare/painshare and performance regime
- approval of payments to the contractor, including payments under the gainshare/painshare and performance regimes

[4] Delivery agencies should consult existing alliancing and ITC guidance when considering how to structure optimal governance arrangements for the procurement and delivery of the project, including participation and interaction with contractors.

- assessment of key performance indicators (KPIs)
- management and approval for drawdowns on state project contingency
- independent reviews and assessment, including those led by the delivery agency, OPV and central agencies
- VfM assessments.

Delivery agencies should ensure a balanced relationship with the contracted parties. This requires an appropriately skilled and resourced team supporting the project. The delivery agency will access advice (internal or external) independent of the contractor to inform its decisions, and to ensure it remains a capable, informed and active client. Project outcomes may be compromised if there is an over-reliance of the delivery agency on the advice and expertise of the contracted parties.

Where expertise is not available internally, delivery agencies may engage external advisers, such as commercial, risk, insurance and legal advisers, at various phases of the project. However, delivery agencies should consider the appropriate balance of using external advisers and building longer term internal expertise.

2.3 Investment assurance and key approvals

Table 1 details the key approvals and assurance requirements at each stage of cost reimbursable procurement, noting that project-specific arrangements for projects may be agreed in a PAP. Some of the approvals below can be sought concurrently.

Table 1 – Integrated approvals and assurance at each stage of the investment lifecycle

Stage	Government approval	Indicative assurance
Business case: Investment decision and procurement model	The Government approves the business case, including the preferred procurement model.[5]	Gate 1 – Concept and feasibility Gate 2 – Business case HVHR deliverability assessment Technical review advice (if directed by the Treasurer and Premier)
Procurement: Procurement preparation and development	The Treasurer approves: • the PAP • changes to the procurement model • the tender engagement strategy[6] [7]	

[5] Approval of the procurement model is required where it is not yet approved by government, or where it has changed from what was previously approved by government at the business case stage.
[6] The tender engagement strategy details the method of engaging a contractor to perform the works (including the type, form and stages of tendering). It forms part of the procurement plan as detailed in the Procurement ILG. It will consider the use of single versus competitive TOCs and level of price competition in procurement.
[7] If the tender engagement strategy is approved as part of the business case, additional approval is only required where it has changed from what was previously approved by government.

Stage	Government approval	Indicative assurance
Procurement: Procurement and contract award	The Government **or** the Treasurer and responsible minister approves: • alliancing and ITC: – release of the expression of interest (EOI) – selection of shortlisted tenderers and release of the request for proposal (RFP) together with an updated cost estimate[8] or Principal's Benchmark (whichever is appropriate) – selection of preferred tenderer for the TOC development phase, together with an updated cost estimate[9] or updated Principal's Benchmark (whichever is appropriate) – contract execution – material variations of scope, and cost and timing changes related to or impacting package or project commencement or completion.	Gate 3 – Readiness for market Gate 4 – Tender decision HVHR assessment before releasing the RFP and at the time of contract award as required in the PAP Quarterly asset and investment report (QAIR) Major projects performance reporting (MPPR)
	• managing contractor: – release of the tender documentation – the principal's benchmark or an updated cost estimate (also known as the total construction cost) before the GCS is developed – contract execution – acceptance of the GCS offer and progression to Stage 2 (delivery) – material variations of scope, and cost and timing changes related to or impacting package or project commencement or completion.	

[8] Including breakdown and key risk assumptions
[9] Including breakdown and key risk assumptions

Stage	Government approval	Indicative assurance
Delivery	The Government **or** the Treasurer and responsible minister approves: • material variations of scope and cost and timing (impacting package or project completion dates) from what was previously approved by the Government • material contract variations • release of the project summary.	Gate 5 – Readiness for service Gate 6 – Benefits realisation Project Assurance Review QAIR and MPPR Technical review advice for major scope changes requiring additional budget (if directed by the Treasurer and Premier)

2.3.1 Role of the Project Assurance Plan

The key approvals and assurance for a project are documented in the PAP, which is prepared by DTF, in consultation with OPV and the delivery agency.[10] The PAP is approved by the Treasurer in the procurement preparation and development phase. It will be informed by discussions of senior representatives from DTF and the delivery agency. The PAP provides flexibility to tailor approval points and assurance requirements for projects and packages, considering project complexity and other circumstances. These approvals and assurance requirements may also be tailored to meet the requirements and phases of different cost reimbursable procurement models.

The PAP will include:

- the role of DTF, OPV and advisers in project evaluation and working groups
- designated assurance processes and independent reviews, including review of the principal's benchmark or an updated cost estimate (as required)
- adviser signoffs required
- key government approval points.

The approach to approvals and other key procurement documentation may be different for program approaches, such as where approval of pre-agreed standard form documents can occur in lieu of seeking individual approvals for certain documents. These changes should be agreed with DTF and captured in the program's PAP.

[10] The PAP template can be accessed at www.dtf.vic.gov.au

2.3.2 DTF review

DTF will review key documentation before the delivery agency seeks relevant government or Treasurer approvals, including:

- the tender engagement strategy (where applicable)
- tender documentation, evaluation plans and evaluation outcomes
- the principal's benchmark or an updated cost estimate, TOC or GCS (as applicable)
- the project contract and risk allocation
- the commercial framework
- approach to bid costs reimbursement
- supporting documents for material contract variations.

DTF or its representatives should be consulted in the development of the principal's benchmark and in developing the TOC. In some instances, DTF may elect to separately review the principal's benchmark for specific projects.

Separately, consistent with the HVHR framework, DTF may appoint independent estimators to review the project cost estimates in the business case and procurement stages.

2.4 Probity and disclosure

Delivery agencies are accountable for the use of public funds, the consequences flowing from their use and successful project delivery.

Elements of cost reimbursable procurement, including collective responsibility, joint governance processes and payment of risk and reward, highlight the importance of probity in dealings with the market.

All procurement activity should meet high standards of behaviour and action. Procurement must be transparent, fair and ethical. Procurement teams should operate with integrity, impartiality and accountability.

A probity plan should be in place for all projects.

The probity plan should be approved by the project steering committee or equivalent governance body. A probity report detailing compliance with the probity plan should be provided for consideration by the Government as part of seeking approval for contract execution.[11]

[11] Please refer to the Procurement ILG for a more general discussion of probity requirements.

2.4.1 Project disclosure

All cost reimbursable projects are subject to contract publishing requirements. Contracts over $10 million should be published on the Victorian Government Tenders website within 60 days of the contract being executed. The contract is to be published in full, with limited exceptions from disclosure, guided by the criteria in the *Freedom of Information Act 1982* (Cth).

A project summary for each cost reimbursable contract over $1 billion should be released within 60 days of contract execution on the relevant delivery agency or departmental website.

The project summary will cover:

- project objectives, scope, procurement process and the parties involved
- financial outcome, including the value of the project and cost to the Government
- commercial risk allocation of the project based on the contract.

Content for each project summary will be determined according to each project's circumstances and characteristics. Appendix 1 outlines proposed content for the project summary.

The Treasurer and responsible portfolio minister should approve the project summary.

Delivery agencies should update project summaries if any significant changes are made to the contract after release, with changes to be approved by the responsible minister.

2.5 Standard form contracts

Delivery agencies should use the standard form contracts in delivering HVHR projects when available. Any derogation from the standard form contract should be approved by the relevant steering committee or the equivalent governance body.

Standard form contracts for the ITC model are available on DTF's Cost Reimbursable Procurement Category webpage[12].

[12] DTF and or government has agreed alternative contract forms for use on projects, which are not intended to be impacted by this document.

3. VfM requirements

This chapter outlines the requirements for achieving and reporting VfM for cost reimbursable procurement models.

3.1 VfM under cost reimbursable models

Cost reimbursable procurement models feature a different approach to sharing risks and a collective approach to decision-making that should be carefully considered when assessing and delivering VfM for these projects.

VfM is an assessment that weighs the cost of procuring assets against the value and outcomes the assets provide. It balances costs against a range of outcomes, including the:

- suitability and quality of infrastructure
- financial benefits
- project's risk exposure
- timeliness of outcomes
- projected social, environmental and industry outcomes.[13]

Delivery agencies will assess VfM when selecting the successful contractor.

Under cost reimbursable models, there may be changes in risk allocation, time, cost and scope in finalising the TOC or GCS. There is also flexibility to make scope, cost and timeline adjustments to address specific events during the delivery of the project. Delivery agencies should manage these changes carefully, having regard to the impact of these changes and adjustments on VfM.

VfM drivers, as detailed in this document, include:

- clearly communicating the State's requirements to tenderers
- ensuring the capability and capacity of the delivery agency's resources can manage the project without being overly reliant on contractors
- ensuring the tender process and TOC development process are carried out on a competitive basis (noting there are exceptions where this may not be pursued)
- minimising variations to the risk allocations outlined under the respective cost reimbursable contracting models
- establishing and maintaining a VfM or benchmarking strategy suited to the procurement, including use of a principal's benchmark
- carefully managing any changes in scope, timeframes and cost during project delivery to maintain or enhance VfM outcomes, including auditing requirements to ensure that costs incurred are reasonable
- reporting and reconciling achievement of VfM at key project stages.

[13] Please refer to the Procurement ILG for a more general discussion of VfM in the context of procurement.

3.1.1 Optimising the tender engagement strategy

The tender engagement strategy details the method of engaging a contractor to perform the works (including the form, type and stages of tendering). It will document the use of single versus competitive TOCs and level of price competition[14].

Alliance and ITC models include the development of a TOC. Where a competitive TOC development process is not the preferred approach, the delivery agency should clearly outline why a single TOC approach or other non-price alternatives are proposed when seeking approval for the tender engagement strategy.

Under a single TOC approach the TOC is developed with a preferred single tenderer/contractor. The State then reviews the offer, including the TOC, with the delivery phase awarded to the tenderer/contractor if this is accepted. If an acceptable TOC is not achieved, or is unlikely to be achieved, engagement may occur with another tenderer/contractor to separately develop a TOC.

A dual TOC involves two teams each developing a TOC in parallel. Selection of the successful contractor for delivery of the project occurs after the TOC has been fully developed and finalised by the competing teams, informing the final evaluation process.

Delivery agencies may consider measures to encourage participation and mitigate costs incurred by industry where appropriate, for example through reimbursement of bid costs when assessing market appetite for the project and the tender engagement strategy.

3.2 Assessing and driving VfM during procurement

3.2.1 Development and use of the principal's benchmark

A principal's benchmark is a key tool for the delivery agency to ensure VfM throughout the procurement process. It is required for all projects, unless an alternative approach is agreed with DTF and approved by the Treasurer.

Delivery agencies should seek approval for the principal's benchmark or an updated cost estimate in accordance with Table 1.

Any changes to the principal's benchmark or updated cost estimate from the approved version should be explained as part of the process to seek government approval for the contractor to construct the project (delivery phase).

In some instances, DTF may elect to separately review the principal's benchmark or updated cost estimate for specific projects.

[14] Please refer to the Procurement ILG for a more general discussion of the tender engagement strategy, which forms part the Procurement Plan.

The principal's benchmark for the ITC and alliancing models should include the same scope, risk assumptions and cost breakdown structure as detailed in the TOC, to enable an effective comparison for VfM purposes. The structure of the updated cost estimate should also include these components.

Delivery agencies should provide a comparison of the TOC or GCS with the final principal's benchmark or updated cost estimate as part of the VfM assessment. Delivery agencies should also detail how VfM has been achieved for a project where project cost exceeds the final principal's benchmark or updated cost estimate when seeking government approvals. This analysis will include a breakdown of the reasons why the project cost has exceeded the final principal's benchmark or updated cost estimate.

OPV is developing a central platform of benchmark infrastructure costs across all HVHR projects which can inform development of the principal's benchmark.

Points to consider when developing the principal's benchmark

- Include all elements of the TOC/GCS to allow for a proper comparison. It can also be used to check the cost and underlying assumptions developed as part of the TOC/GCS.
- It enables the delivery agency to understand the key pricing assumptions and risk assumptions that are driving differentials in pricing between the tenderer's proposal relative to the benchmark. The delivery agency will determine whether these variances and pricing differentials are considered fair and reasonable.
- Delivery agencies should reconcile the costs and quantities of all elements within the TOC (e.g. designer costs, construction methods, indirect costs and contingencies) to the principal's benchmark at the component level. Delivery agencies may carry out a line-by-line analysis of a tenderer's cost build-up, which may provide useful insights that can be used during final contract negotiations.

3.2.2 Independent estimator review

At different stages of procurement and delivery, independent estimators can:

- assess the reasonableness of the project cost, contingency, risk estimates and timeframes at the business case stage
- inform and assess the reasonableness of the principal's benchmark
- assess the reasonableness of bid elements and TOC/GCS development, including assumptions
- provide other benchmarking data to assist evaluation and verification of project costs during project evaluation and delivery.

Delivery agencies should carry out independent cost reviews of the TOC/GCS for projects exceeding $500 million where the development of a TOC/GCS pricing is carried out by only one tenderer/contractor.[15] An independent estimator using cost assessment and benchmark data from similar government projects to evaluate the TOC/GCS will ensure a fair and reasonable estimate of the outturn cost.

DTF may separately engage an independent cost estimator to conduct its HVHR assurance processes.

3.2.3 Financial audit

Delivery agencies may engage a suitably qualified financial auditor to conduct detailed investigations of the financial and costing records of the contracting parties as part of the procurement process. This will provide a level of comfort that the contracting parties have sufficient financial capacity and capability to engage in a transaction with the State. The audit assesses the financial health and liquidity of the contracting entities and any associated parent companies that are providing security as part of the contracting arrangement.

---

[15] The GCS is typically developed by only one contractor under MC arrangements.

3.3 Managing VfM during project delivery

Delivery agencies should have strategies in place to monitor and manage changes to VfM throughout the project. Variations, changes in scope or unexpected events can impact the final VfM outcomes of the project.

Delivery agencies may arrange periodic independent audits of the progress and performance of the works carried out. This can confirm that contracted parties are delivering the project in accordance with the terms of the contract. An independent auditor can also confirm that the direct costs, COP and other payments are in accordance with the contract and that the contracting parties' internal systems and procedures remain rigorous and robust.

3.3.1 Material variations and key considerations for VfM

The Government will consider material variations to the scope, time and cost of a project during delivery. DTF can confirm the level of approval required and the key issues that need to be addressed to obtain that approval.

Identified acts, events and circumstances that may result in adjusting the TOC/GCS are known as adjustment events (or GCS amendments or both). These are defined in the Victorian public sector standard form contracts and discussed in Chapter 5. Genuine innovation by the contracted parties that generates cost savings during delivery would not constitute an adjustment event. However, delivery agencies should be aware of situations where project scope is reduced by contracted parties to address cost overruns as this can materially impact the project's VfM outcomes.

The TOC/GCS may typically be adjusted where the delivery agency has directed a change that amounts to a:

- significant material change, amendment or alteration to the scope of works
- fundamental changes to the requirements of work.

These types of adjustment events are referred to as scope variations. What constitutes a scope variation under the contract should be agreed during the selection phase of the procurement.

Independent cost estimators and external advice may be required to provide robust benchmarks and independent validation of adjustment events.

The KRA/KPIs for the project should only change when a predefined and agreed adjustment event has occurred.

3.3.2 Reporting and reconciling VfM over the life of the project

Delivery agencies should prepare a project completion report for the Government, including VfM outcomes, upon contract completion. The completion report will be developed and verified independently of the contractor to ensure an impartial and objective assessment of project performance.

The completion report should include:

- a full reconciliation of total delivery agency budget with the actual total project cost to the Government (this should include a breakdown of provisions outside the TOC, such as owner's costs and contingencies)
- a reconciliation of the TOC against the expected actual project cost (AOC) (for alliances and ITC contracts)
- an assessment of the risks that eventuated on the project in comparison to expectations at project tendering
- a summary of contractual changes during delivery (since execution)
- a summary of the contractor's performance, including against KRAs and payments made to the contractor
- quality, innovations and other improvements identified and implemented during the project by the contractor, including the benefits delivered from those innovations (with verification)
- a summary of scope changes and their effect on capital expenditure and operational expenditure, including a reconciliation between project scope contracted for and what was delivered
- an assessment of whether the agreed legal and commercial terms and conditions in the contract executed has provided for a best-in-market actual outcome
- a summary of lessons learned, including aspects that could have been improved, with recommendations for how performance can be improved in the future.

Delivery agencies should also provide progressive reconciliations of changes to project budget, cost, scope and timeframes from what was approved by the Government in the business case at key project decision points where appropriate. These changes will be captured in one report, updated for changes at each approval point from what was previously approved by the Government, including the reasons for any proposed changes.

4. Procurement for cost reimbursable models

This chapter outlines the procurement stages and key considerations for delivery agencies in planning and managing procurement for cost reimbursable procurement models.

4.1 Procurement stages

Cost reimbursable procurements will typically have the following stages:[16]

Table 2 – Stages of procurement

<table>
<tr><th>Stage</th><th>Managing contractor</th><th>ITC</th><th>Alliance</th></tr>
<tr><td>Procurement preparation and development</td><td colspan="3">Consult market, finalise tender engagement strategy, establish governance, assemble resources and develop tender documentation and commercial framework.</td></tr>
<tr><td>Procurement</td><td>Procurement of managing contractor
Conduct tender to select managing contractor.
Project development
The managing contractor:
• develops the project design and construction documentation
• tenders for subcontractor packages
• prepares the GCS offer for consideration by the delivery agency.</td><td colspan="2">EOI
Identify tenderers with appropriate capability and compliance with government requirements to shortlist tenderers for the RFP stage.[17]
RFP or development phase
Shortlisted tenderer(s) design and develop the project collaboratively with the delivery agency, including finalising the risk allocation and developing the TOC.[18]</td></tr>
<tr><td>Contract award</td><td colspan="3">Final agreements are negotiated and executed.</td></tr>
</table>

[16] Delivery agencies should also refer to the Procurement ILG, which provides general guidance on the procurement phases and key requirements for conducting procurement for a project.
[17] The EOI can be preceded by a 'registration of interest' to identify potential tenderers.
[18] The delivery agency may engage with preferred tenderer(s) to negotiate the ITC Development Agreement that will guide the TOC process, including the development of a technical proposal.

4.1.1 Program approaches

Cost reimbursable procurement models can also be used in program approaches. This refers to contracting arrangements for the delivery of multiple discrete projects over a typically longer time horizon.

Contractors are typically engaged on a panel through an open market process. Under this arrangement, contractors sign a panel participation agreement to lock in key commercial terms and conditions. Contractors then bid for work, which is delivered through the selected procurement model (e.g. alliance contracting).

Further information on program approaches is available in Chapter 5 and the Procurement ILG, available on DTF's Procurement ILG webpage.

4.2 Key considerations for successful procurement and project delivery

Delivery agencies will consider specific issues when preparing for procurement using a cost reimbursable model.[19]

4.2.1 Clearly communicating project objectives, desired outcomes and the procurement process

Cost reimbursable models typically require a high level of collaboration between the participants throughout procurement and delivery of the project. Making decisions that are best for the project requires a joint understanding of the project objectives and requirements of the State.

Delivery agencies should be able to clearly communicate the proposed procurement process. This ensures the State's requirements are understood by both delivery agencies and tenderers or participants, including:

- the process for assessing the tenderers, including the selection criteria to be used in evaluation and the relative importance of the criteria
- clear project objectives
- key project issues, risks, stakeholders and interfaces
- key commercial arrangements, including any reimbursement of bid costs, risk allocation for key design- and construction-related risks, payment arrangements, performance regime, indemnities, insurance requirements and limitation of liabilities.

[19] Delivery agencies should also refer to the Procurement ILG, which provides general guidance on the procurement phases and key requirements for conducting procurement for a project.

4.2.2 Ensuring delivery agency resourcing and expertise

A delivery agency should have the resources, skills and processes in place to fully support implementation of cost reimbursable procurement models.

Moving from a traditional project owner and contractor relationship to an active delivery partnership requires appropriate leadership, skills, experience and behaviours that support a collaborative approach.

Delivery agencies that are active and informed clients, with accountability for key decisions that impact project outcomes, is integral to the success of cost reimbursable procurement models. These models:

- can be resource intensive, requiring delivery agencies to potentially establish two teams during the procurement phase
- require delivery agencies to understand project risks and their potential impacts, participate in decision-making about shared risks, and support and monitor controls and mitigations
- require delivery agencies to understand the scope and design of the project in sufficient detail to interrogate costs through the open-book processes.

The skills and capabilities required of delivery agencies will vary with the procurement model used. The degree of capability, capacity and experience required of the delivery agency will increase as the scale and complexity of the project and degree of risk-sharing increases.

4.2.3 Incentivising the right behaviours for collaboration

Delivery agencies and contractors should commit to and facilitate collaborative, cooperative behaviours early in the procurement process. Collaboration in cost reimbursable models will begin during the procurement or development phase (e.g. in the development of the TOC or GCS) rather at than the formal initiation of the project.

The commercial framework, including the contractor's risk exposure, payment of risk and reward and other elements, remains a key driver of contractor behaviour during delivery.

The most effective approach to embedding collaborative behaviours under a cost reimbursable model is to develop principles embedded into all contracts, including the development agreement (if applicable). This could include a charter or a contractual behavioural framework, to better align the objectives of the delivery agency and the contractor so that all decisions are made for the benefit of the project.

Behavioural principles for cost reimbursable models include:

- maintaining a culture of cooperation to achieve objectives
- ensuring safety
- resolving differences early
- addressing risks and issues efficiently
- striving for VfM
- committing to transparency
- sharing learnings
- developing capacity.

These principles should be agreed on and established early in the process.

Collaboration will also be reflected in both the governance model for the contract and in the staffing of key leadership positions.

Delivery agencies may request tenderers to detail their proposed governance structures and how this will facilitate collective problem-solving and decision-making. Delivery agencies may also consider how ongoing collaboration will be monitored and measured, as well as mechanisms for feedback to be shared between parties on a structured basis. This could include the use of metrics for leadership participation, dispute resolution, collaborative culture, continuous improvement and joint management of risks and opportunities.

4.2.4 Committing to organisational culture

The organisational culture of the delivery agency and contractor is fundamental to gaining the benefit of cost reimbursable procurement.

The delivery agency may consider whether it has or could develop the right organisational structures to support the project, including:

- effective and flexible processes to manage change over the course of a contract
- a culture that supports the development of trusted partnerships, including managing differences between parties
- processes that support knowledge-sharing and coordination with project partners as required.

Delivery agencies may identify opportunities to use interactive or collaborative procurement processes within appropriate probity frameworks. When the contract is awarded, they could identify opportunities for cultural alignment activities.

4.2.5 Understanding the market

Delivery agencies should have a strong understanding of the market, including contractors' appetite for bidding and taking specific risks on projects. This ensures the tender approach and contracts are designed in a way that engages market interest and optimises competition to provide better VfM outcomes.

Engaging early with the market can help inform key procurement process decisions and enable delivery agencies to better understand the risks of the project. This includes risks that cannot be appropriately priced and managed by contractors and how contracting arrangements can help mitigate and manage these risks.

Delivery agencies can develop their understanding of the market for a given project or program through early and ongoing market consultation.

4.2.6 Using subcontractors and suballiances

Delivery agencies should consider the risks related to subcontractors for the specific project and how these risks may need to be mitigated.

The State should require visibility of all key subcontracts for the purpose of understanding:

- the identity of the subcontractor
- the scope being subcontracted
- the limits on liability that apply
- what costs are being passed through to the subcontractor
- what risks and costs are being retained by the State.

Tenderers should provide evidence for and detail of their proposed subcontracting and procurement strategy. This includes explaining how their strategy will achieve the best VfM for the project.

Delivery agencies should consider selecting subcontractors on a competitive basis and ensuring the procurement process is transparent.

For the MC model, this will include the degree of works being self-performed by the head contractor and considering limits to or conditions for self-performance of construction work.

Suballiances, where an alliance uses tier-two suppliers as subcontractors under an alliance arrangement, can change the balance of risks for the project and increase cost and risk exposure for the State. DTF can advise on the use of these arrangements.

4.2.7 Determining bid costs

Delivery agencies will consider reimbursing bid costs of unsuccessful tenderers (or unsuccessful alliance participants as part of a dual TOC process) for cost reimbursable procurement models.

Delivery agencies should refer to DTF's Bid Cost Reimbursement Policy for Major Construction Projects in determining the level of bid costs for a project. Delivery agencies will develop transparent parameters and verification processes for assessing reasonable bid costs. These requirements will be clearly communicated to the tenderers before commencing any procurement process. This includes:

- definition of what costs are covered and excluded
- the stage that bid costs will be reimbursed
- the method for calculation (percentage of total costs covered, and external versus internal costs)
- minimum tender submission requirements that need to be met for costs to be paid.

Paying bid costs under cost reimbursable procurement models is intended to encourage greater industry participation in the tender process. The level of additional costs to the Government will be considered against the greater VfM that can be achieved for a project through better resourced teams and improved competition.

5. Commercial framework(s) and risk allocation for cost reimbursable procurement models

This chapter describes the range of commercial mechanisms used in cost reimbursable procurement models. It also outlines best practice considerations for delivery agencies and differences in the approach to risk for cost reimbursable procurement models.

5.1 The cost reimbursable commercial framework

The commercial framework should align the interests of the State and contractors to achieve agreed project outcomes.

The following elements underpin cost reimbursable procurement models and will be supported by the commercial framework:

- The delivery agency and contractor will work collaboratively early in the procurement process to maximise the opportunity for innovative and efficient project delivery.
- Some risks are shared and jointly managed by the delivery agency and contracted parties.
- The reward of outstanding performance and the penalty for poor performance are typically shared between the delivery agency and the contractors.
- There is a commitment between contract parties to work cooperatively and encourage problem-solving as challenges and issues arise.

The application and calibration of these commercial components will depend on the cost reimbursable procurement model used and specific project characteristics.

Table 3 – Key commercial components of the cost reimbursable procurement models

Commercial framework component	Managing contractor	ITC	Alliance
Risk management and contractor liability			
Elements of shared risk and limited liability	✓	✓	✓
Incentivising, measuring and rewarding performance			
Payment arrangements (fee structure)	✓	✓	✓
Use of TOC	✗	✓	✓
Use of GCS	✓	✗	✗
Risk and reward framework	✓	✓	✓
KPIs	✓	✓	✓
Managing scope and project timing in construction			
Contingency management	✓	✓	✓
Adjustment events	✓	✓	✓
Promoting cooperation and early identification of risk			
Early risk identification and issue resolution	✓	✓	✓
Program of works			
Suitable for programs of work	✓	✓	✓

✓ included ✗ not included

5.1.1 Shared risk and contractor liability

Cost reimbursable procurement models involve high levels of risk-sharing between the State and contractors, and greater limits on liability for the contractor than other procurement models.

Shared risk denotes a broad range of arrangements where the contractor and state share the day-to-day operational obligations to manage the risk (risk management) or the financial consequences of the risk materialising (cost assignment). Risks may not be shared in equal proportions between the State and the contractor.

Overall, the contractor's exposure to the financial consequences of risks materialising may be limited under cost reimbursable models:

- There can be lower liability caps for contractors, with the State typically taking financial responsibility for cost overruns when the liability caps for projects are reached.
- There are timeframes for when responsibility for risks may revert to the State, for example when the period to address defects has expired.
- Risks that form part of a TOC are subject to caps through the gainshare/painshare regime.

Delivery agencies should be conscious of the differences in risk allocation and cost assignment across the different cost reimbursable procurement models:

- Risks are shared under an alliance procurement model, with the contractor's potential painshare value (percentage of cost overruns carried by the contractor) capped to the contractor's contribution to overheads and its profit margin. The contractor will not be liable for any further losses (except in limited circumstances, such as wilful default).
- While many risks are shared under an ITC procurement model, some specific risks can be allocated to the contractor. For example, the breach of timing obligations under the ITC model may expose the contractor to liquidated damages.
- While some risks are shared under an MC procurement model, some specific risks can be allocated to the contractor, particularly in Stage 2 of the procurement process. The liability of the contractor will typically be capped at total construction cost, although this may vary on a project-by-project basis.

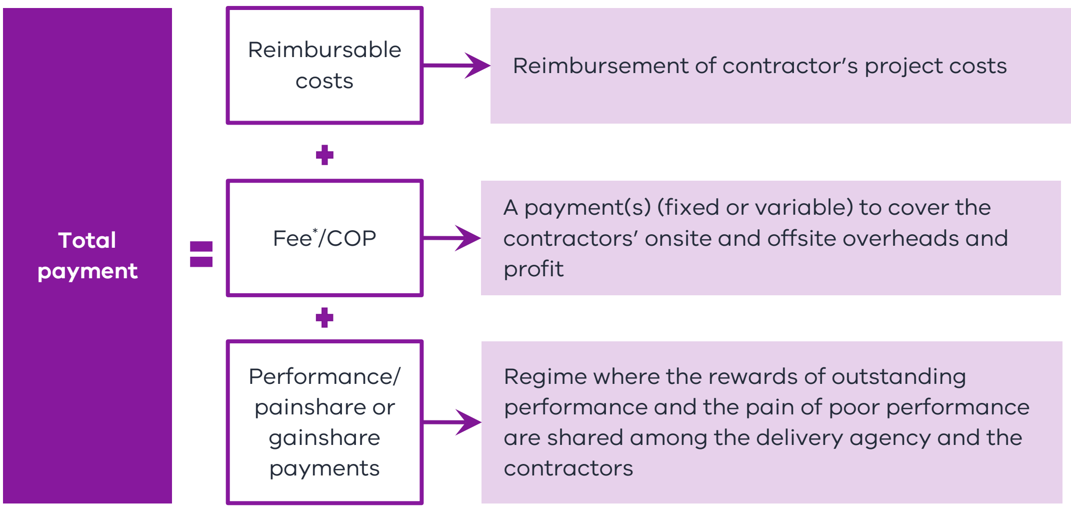
A high-level summary of typical risk allocations for the three cost reimbursable procurement models and detailed definitions of individual risks are provided in Appendix 2.

Delivery agencies can refer to Appendix 3 for a high-level summary of general liability caps and indemnities provided under cost reimbursable procurement models.

5.1.2 Payment arrangements (fee structure)

The payment structure for cost reimbursable procurement models is typically structured across three components, as shown in Figure 2.

Figure 2 – Payment structure



* Fees for the MC models may include construction and, potentially, design management fee (fixed price fee ($)); preliminaries and onsite overheads (fixed % or $); and offsite overheads and profit (fixed %).

Points to consider for reimbursable costs and setting fees

Reimbursable costs typically include:

- **design costs:** all costs related to detailed design and investigations
- **preliminaries costs**: mobilisation and demobilisation, and contractors' management, insurance and supervision costs
- **construction costs**: all direct construction-related activities costs
- **management costs**: management and offsite overhead costs and insurances.

Contractors should only be reimbursed for costs actually and reasonably incurred. The delivery agency should commit contractors to an open-book arrangement where reimbursable costs are subject to broad audit and due diligence requirements.

The delivery agency should agree with contractors what reimbursable costs (in particular wages and plant equipment hire costs) are considered costs or corporate overhead as this delineation may not always be obvious.

The delivery agency should tailor what it considers a reimbursable cost with respect to the risk and reward regime. For example, costs incurred that were solely attributed to contractor negligence would not be considered reimbursable.

The contract should make clear the approach to (and any conditions on) reimbursing subcontractor costs and include a clear auditing process.

For construction works, the fixed fee is usually pegged to a pre-agreed percentage of the construction portion of the TOC and ensures the contractor cannot earn greater fee revenue by incurring more direct costs.

For design works, the fee is often calculated on a variable basis, by applying a pre-agreed percentage to the actual direct costs incurred. This approach avoids the situation where the contractor does not want to take on additional scope post TOC development because it will not receive additional fee revenue.

The State continues to pay a percentage of reimbursable costs regardless of whether the contractors' painshare cap has been reached or is about to be reached. Delivery agencies should consider mechanisms to incentivise contractors to manage the level of reimbursable costs paid by the State in these circumstances, including the use of cure plans.[20]

[20] A cure plan is an agreed plan for the contractor to improve performance.

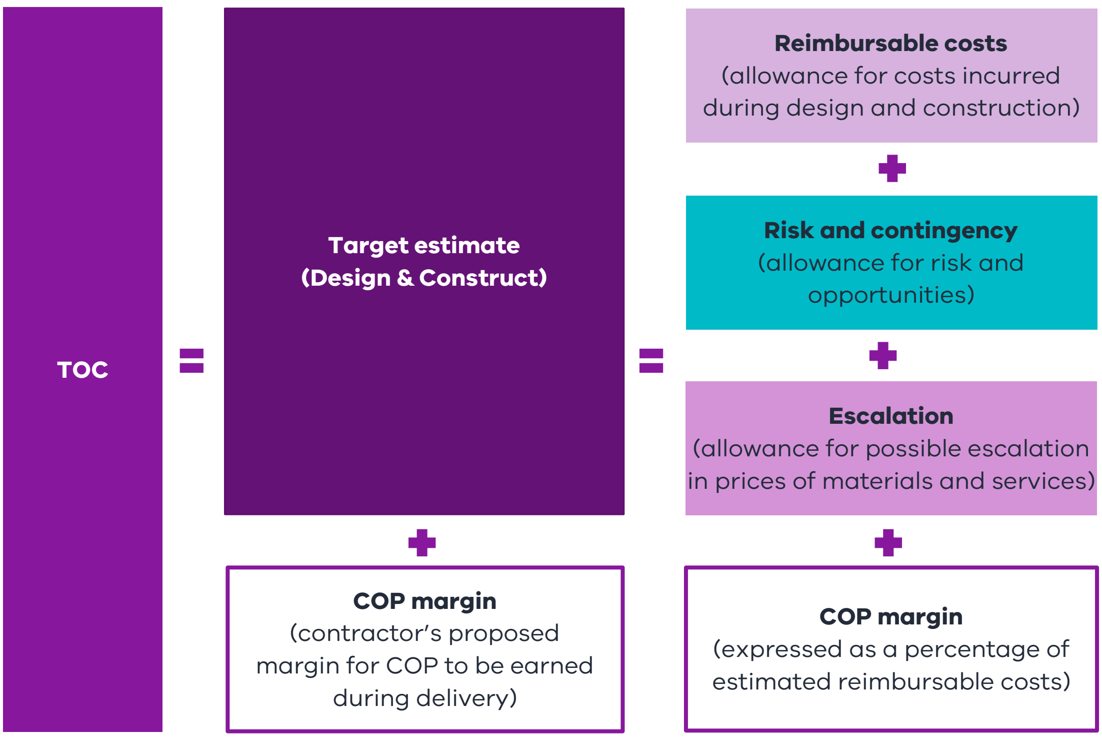
5.1.3 Use and development of a TOC

The TOC represents the estimated cost of completing the contracted works and achieving the minimum project outcomes. It does not equate to the delivery agency's capital works budget as this also includes costs that sit outside the contract, such as project contingencies.

The TOC is used in alliance and ITC procurement models. It is a key element in assessing VfM and determining performance and gainshare/painshare amounts, including where:

- the TOC is compared with the principal's benchmark, which has been developed to provide a point of cost comparison for the delivery agency during the evaluation process and to assess VfM
- the AOC is measured against the TOC for the purposes of assessing cost gainshare/painshare amounts.

Figure 3 – Components of the TOC



Delivery agencies should ensure that the TOC is developed by the contractor on a transparent, collaborative and open-book basis. The delivery agency should have a robust understanding of the TOC estimate and its underlying assumptions to effectively evaluate and negotiate the TOC with a contractor.

There is a risk that the TOC will not represent the cost to complete the works, is set too high or will reduce VfM where there is a different level of information between the delivery agency and the contractor.

Points to consider when developing the TOC

- Delivery agencies should understand the nature of the project risks and their potential cost consequences in developing the TOC. This is particularly crucial where the delivery agency uses a single TOC process in its selection approach.
- Delivery agencies should deploy a robust set of price-estimating procedures and ensure the information it is validating is the same set of information used by the tenderer during the TOC development process. An independent estimator should be used to interrogate cost items within the TOC.
- The contractor should share the methodology, assumptions and calculations used to determine the components for the TOC.
- Corporate overhead, a component of the TOC, should only support the reasonable recovery of non-project-specific overheads (e.g. general head office management costs).

5.1.4 Use of a Guaranteed Construction Sum

The GCS is used in the MC cost reimbursable procurement model. It represents the contractor's estimate for completing the construction works. The GCS is a key element in assessing VfM and determining performance payments under the MC model.

Under the MC model, the GCS is finalised and agreed as part of the State's decision to progress to the delivery phase of the project (Stage 2), involving construction of the asset.

5.1.5 The risk and reward framework

The risk and reward framework identifies payments to the contractor based on performance. Delivery agencies should consider how to align the risk and reward framework with the objectives of the project, to ensure that it is driving the right behaviours and outcomes.

Depending on the model, the framework may include two key components:

- gainshare/painshare adjustments
- a performance pool to incentivise non-financial behaviours.

5.1.5.1 Gainshare/Painshare

Gainshare/painshare adjustments are typically used for alliance and ITC cost reimbursable procurement models. If the AOC is less than the TOC, a gainshare amount will be payable by the delivery agency to the contractor. If the AOC is greater than the TOC, a painshare amount may be payable by the contractor to the delivery agency. The objective of these payments is to share the increase or decrease in project value driven by project outcomes between the delivery agency and contractor.

Under an MC cost reimbursable procurement model there may be payments to incentivise management of costs that include an entitlement to a share of cost savings on completion. The share of savings is usually capped to disincentivise the contractor from inflating the GCS.

5.1.5.2 Performance payment

Delivery agencies can consider a separate payment for performance against a range of KRAs.

A performance pool will be available to the contractor based on the following principles:

- Positive performance is incentivised with payments from the performance pool.
- Poor performance reduces the contractor's ability to receive a performance reward for the applicable KRA.

Under an ITC contract, the performance pool is typically sized at equivalent to 3 per cent of the TOC under a competitive process and at 1.5 per cent of the TOC under a single TOC process. An additional 1.5 per cent of the TOC is available to be added to the performance pool under a single TOC process if the TOC is set at 5 per cent below the principal's benchmark.

5.1.6 KRAs and KPIs

KRAs and KPIs are used to assess contractor performance and the applicability of a performance payment.

KRAs reflect the outcomes that the delivery agency seeks to achieve for a project and are often limited to about six or fewer. The role of the KRAs is to link project performance to priority outcomes identified for the State (e.g. time, cost, quality, sustainability, safety, community satisfaction, operational efficiency, whole-of-life costs and local industry participation).

KPIs are the criteria by which the accomplishment of KRAs is assessed. For example, the achievement of the delivery agency's quality KRA could be assessed by a KPI that assesses the number of defects observed throughout the contract term.

Delivery agencies will develop KPI regimes when using cost reimbursable procurement models tied to the headline KRAs set for the project. KPIs will vary according to individual project outcomes.

Points to consider when developing KRAs and KPIs

- Cost KPIs measure a contractor's performance against costs incurred during the design and construct phase of a project, including materials, labour, corporate overhead and margin. When using the alliancing procurement model, the contractor's performance against cost would be measured by comparing the AOC against the TOC and determining the gainshare/painshare amounts for the project.
- Non-cost KPIs can take the form of either a lead indicator (or predictive measurement) or lag indicator (or output measurement).
- KPIs should be robust and demanding but also reasonable. KPIs will be calibrated to ensure any gainshare/painshare amounts are set at values to drive the desired behaviours.
- Poor performance against a single KPI should not eliminate a contractor's entire fee or margin. Otherwise, the contractor may have limited financial motivation to achieve the delivery agency's other project objectives.

5.1.7 Contingency management

The delivery agency and contractors should adequately provision for risk and contingency both as part of the TOC and separate to it.

Table 4 – Risk and contingency

Party	Type of risk and contingency
Contractor	Allowance to cover risks and opportunities in project implementation. Included in the TOC for alliance and ITC models and GCS for MC models. Allowances for risks around omissions and negligence by the contractor should not be included in the TOC/GCS.
Delivery agency	Allowance for risks held by the State outside of the TOC or GCS.
State	Allowance for general project contingency. DTF may hold these contingencies centrally, where the Government will approve its use by the delivery agency.

Delivery agencies should ensure the contingency included in the TOC is sized to optimise project outcomes. If contingencies are not optimal then this will impact gainshare/painshare adjustments to the contractor and potentially compromise performance incentives for the contractor. It may allow the contractor to receive greater rewards given the costs savings are usually shared with the State.

Delivery agencies should develop a clear understanding and estimate of retained risks given the greater level of risk-sharing under these models.

5.1.8 Adjustment events

Under an ITC or alliance model, parties may mutually agree to revise the TOC, performance regime and the dates for project completion as external events and circumstances arise that were unforeseen in the development phase. These events are detailed in the agreed adjustment events schedule. Examples of adjustment events are a breach by the delivery agency, a force majeure event and scope variation.

Delivery agencies should seek to ensure the types of adjustment events are justified. Contractors are incentivised to secure adjustment events to remove the cost of certain risks materialising from the TOC as these costs can reduce the contractor's ability to secure gainshare.

These considerations can also apply for any adjustments to the GCS under the MC model.

5.1.9 Issue resolution

Delivery agencies should carefully define their approach to issue resolution. This will be centred around cooperative performance with contracting parties that aims to meet project objectives.

Alliance contracts generally include a 'no disputes' mechanism and therefore do not include a formal dispute resolution procedure. The 'no disputes' mechanism aims to avoid the adversarial or 'claims-based' culture of traditional contracting when poorly managed. This mechanism encourages participants to find solutions to problems, rather than to seek to blame others.

Key tools and governance structures for issue resolution will form part of the commercial framework. These may include:

- a charter or a contractual behavioural framework (as detailed in Chapter 4). This includes agreed behavioural principles to drive decision-making processes and issue resolution
- an issue resolution team, inclusive of both the delivery agency and contracting parties. This provides parties with an opportunity to agree to a bespoke process before a more formal resolution process
- a deadlock breaking mechanism in the contract. Under this process, deadlocks that cannot be resolved unanimously by the project governance are referred to an independent third party, such as a dispute resolution board.

5.1.10 Commercial frameworks for program approaches

The features of cost reimbursable procurement models can also be applied to *programs* of projects.

A programs approach can establish commercial frameworks that incentivise continual improvement and delivery of outcomes over longer periods of time as discrete projects are delivered. This approach captures efficiencies from long-term relationships with contractors, and facilitates innovation and integration between contractors and advisers.

If a delivery agency seeks to renew or extend a program, they should consider returning to the market to ensure that they are maximising competition and VfM. They should also provide for continuous improvement in terms of cost and non-cost KPIs as the program develops. This may include increasing required outcomes year-on-year over the contract term.

The delivery agency requires a strong understanding of the contractor’s cost build-ups and a robust principal’s benchmark to evaluate VfM in any given project.

Appendix A – Project summary template for cost reimbursable procurement

Purpose

This template will be used by delivery agencies for publishing project summaries on the relevant department or agency website.

Policy requirement

The Cost Reimbursable Procurement Requirements states:

- a project summary for each cost reimbursable contract over $1 billion should be released within 60 days of contract execution
- content for each project summary will be determined according to each project's circumstances and characteristics
- the Treasurer and responsible portfolio minister should approve the project summary.

Project summary form and content

This template sets out the required form and content of the project summary. Content will change as new areas of public interest emerge.

It is recommended the project summary be completed while the project advisers are still available to provide input to the document (e.g. financials, risk allocation table).

The estimated length of a project summary is up to 15 pages.

The following outline includes the template headings and proposed content for the project summary, which may differ depending on project circumstances.

Cover

The cover is to include:

- project name
- date
- Victorian Government logo.

The inside cover should include publication and copyright references.

Introduction/foreword

This explains the purpose of the project summary, the structure of the document and a brief explanation of the procurement policy framework. This section should reference links to any other published material such a project website, published contract or other material. It should also include a disclaimer such as:

> This summary should not be relied on to completely describe the rights and obligations in respect of the project, which are governed by the project contract and associated documents. The project contract and associated documents are available online at www.tenders.vic.gov.au

Part one: Project overview

Project outcomes

- Outline the project objectives, the State's need for the project and the high-level benefits expected.
- Describe the infrastructure to be provided by the private provider.

Project costs

- Detail the contracted cost of the project.
- Detail any state financial contributions to the project.
- Detail any non-financial state contributions to the project (e.g. land).

Tender process

- Detail the procurement model used to deliver the project.
- Outline the tender process for the selection of the contractor. This could reference the delivery agencies project delivery governance structure (consider including a governance diagram).
- Complete a table of key procurement milestones, as shown in Table 5 (modified as appropriate for the individual procurement).
- Detail the probity framework adopted during procurement.
- Outline any stakeholder engagement processes completed during procurement.

Table 5 – Project procurement – key dates

Procurement process	Date
Expression of interest phase	
Invitation for expressions of interest issued	
Expressions of interests submitted	
Shortlist of respondents to proceed announced	
Request for proposal phase	
Request for proposals issued	
Request for proposals received	
Negotiation and completion phase	
Preferred bidder announced	
Contract close	

Tender process outcomes

- Outline the tender outcome, including the name of the successful tenderer and key components of the successful offer.
- Detail the commitments for government policy requirements.

Contract milestones

- Outline the milestone dates for delivery of the project. Table 6 provides an indicative summary.

Table 6 – Key date summary

Contract component	Due date
Contract commencement	dd month yyyy
Construction commencement	dd month yyyy
Construction completion	On or before dd month yyyy
Contract expiry date	dd month yyyy

Project governance

- Detail the key governance bodies during delivery of the project.

Project advisers

- Outline the external advisers engaged for procurement of the project. Table 7 provides an indicative summary.

Table 7 – Project advisers

Role	Adviser
Financial and commercial adviser	[insert]
Legal adviser	[insert]
Probity adviser	[insert]
[insert additional project advisers as applicable]	[insert]

Part two: Key project features

Parties to the contract

- Outline the key parties to the contract.

Contractual relationships

- Outline the key contractual relationships of the project.

Risk allocation

- Outline the risk allocation under the project contract. The risk allocation matrix, completed during the project procurement phase, will provide a basis for this analysis.
- Outline any departures from the standard project deeds for specific procurement models. These may be project specific departures or negotiated outcomes.

General obligations of the contractor

- Outline the major obligations of the private party under the project contract.

General obligations of the State

- Outline the major obligations of the State under the project contract.

Performance measures and payments

- Detail the process for the State making payments under the contract, including the key performance measures and how the private provider will be accountable for cost and non-cost performance.

Key contact details and further references

- Detail contact details and further references for the project.

Appendix B – Risk definitions and allocations

Key risk categories to be considered under cost reimbursable contracting are detailed below.

Land acquisition risks: risks of increased project costs or delay arising from:

- property value fluctuations, land quality issues and heritage and native land title claims
- the acquisition for extra land by the contractor (over and beyond what is made available by the procuring agency).

Site planning and approval risks: risks of increased project costs or delay arising from planning approvals (including approvals arising from a variation or adjustment event) and compliance with planning approvals.

Site contamination risks: risks of increased project costs or delay arising from the management and removal of site contamination to meet legislative and approval requirements.

Claims for native title and Aboriginal heritage: risks of increased project costs or delay arising from heritage claims and native title claims.

Construction risks: risks of increased project costs or delay arising from:

- operational risks arising from the contractor not delivering on the project scope or delivery requirements, defects or non-compliance with contractual obligations. procuring agency-initiated variations.

Site risks: risks of increased project costs or delay arising from:

- inaccurate geotechnical data
- changes in geological conditions on site compared with baselines assumptions
- utility services, due to nature, scope, location or condition of utilities differing materially to what could have been foreseen. Utilities may include water, sewerage, electricity, gas and telecommunications.

Construction risks: operational risks arising from the contractor not delivering on the project scope or delivery requirements, defects or non-compliance with contractual obligations leading.

Design risks: risks of increased project costs or delay arising from:

- the design development process not being completed on time or to budget
- the design not meeting the project scope and delivery requirements or is not fit-for-purpose
- variations initiated by the procuring agency.

Defects: risk that defects are identified following completion of construction.

Time: risk that construction cannot be completed on time (subject to adjustment events (time))

Force majeure events: risk of delay or additional costs or both caused by force majeure events that prevent construction milestones being met.

Principal initiated variations: risk of delay or additional costs or both by the principal electing to make a variation to the works.

Site-specific industrial action: risk of delays or additional costs or both due to site-specific industrial action.

Statewide industrial action: risk of delays or additional costs or both due to statewide industrial action.

Change in law or policy risks: risk of increased project costs or delay arising from:

- a failure to comply with regulatory obligations in the form of civil/criminal charges, financial penalties and compensation or asset confiscation
- regulatory or legislative change that may lead to additional time or cost to comply with new regulations that may apply to project activities.

Pandemic risk: risk of increased project costs or delay arising from:

- future pandemic restrictions and associated site closures to due to restrictions
- capability and capacity constraints arising from future pandemics, due to staff and skills shortages.

Tax: risks of increased project costs or delay arising from:

- tax payable with respect to contractor activities, including customs duties and tariffs on imported materials
- changes in taxation legislation or other policy affecting the returns on investments.

Price escalation and supply chain: risk of:

- increased project costs arising from significant price escalation of key inputs
- project delays arising from delays in delivery of key inputs or equipment.

Fit-for-purpose: risk of additional costs to the State or reduced VfM due to the final project not being fit-for-purpose.

Quality: risk of increased project costs or reduction in VfM due to delivery of the project failing to meet the expected quality standards.

Financial sustainability of the contractor(s): risk that the project will not be completed or that there will be additional costs to the Government due to a contractor being unable to complete the project due to financial difficulties.

Table 5 provides an overview of risk allocation and cost assignment across these risk categories. This table should only be used as a guide, is illustrative only and allocations will vary depending on the specific project. Please refer to standard form contracts and guidance for each procurement model when considering risk allocations and cost assignments for projects.

Table 8 – Overview of indicative risk allocations and cost assignment across reimbursable cost procurement models

Risk	Managing contractor		ITC		Alliance	
	Risk allocation	Cost assignment	Risk allocation	Cost assignment	Risk allocation	Cost assignment
Land acquisition risks	[agency/state]	[agency/state]	[agency/state]	[shared]	[shared]	[shared]
Site planning approval risks	[shared]	[shared]	[contractor]	[shared]	[shared]	[shared]
Contamination risks*	[contractor]	[agency/state]	Varies	Varies	[shared]	[shared]
Claims for native title and Aboriginal heritage	[agency/state]	[agency/state]	[agency/state]	[agency/state]	[shared]	[shared]
Construction risks	[contractor]	[contractor]	[contractor]	[shared]	[shared]	[shared]
Design risks	[contractor]	[agency/state]	[shared]	[shared]	[shared]	[shared]
Defects	[contractor]	[contractor]	[contractor]	[contractor] [shared]	[shared]	[shared]
Time	[contractor]	[contractor]	[contractor]	[contractor]	[shared]	[shared]
Force majeure events	[shared]	[shared]	[shared]	[shared]	[shared]	[shared]
Principal initiated variations	[agency/state]	[agency/state]	[agency/state]	[agency/state]	[shared]	[shared]
Site-specific industrial action	[contractor]	[contractor]	[agency/state]	[contractor]	[shared]	[shared]
Statewide industrial action	[agency/state]	[agency/state]	[contractor]	[agency/state]	[shared]	[shared]
Change in law or policy**	Varies	Varies	[agency/state]	[agency/state]	[shared]	[shared]
Pandemic risk	[agency/state] [shared]	[shared]	[agency/state] [shared]	[agency/state] [shared]	[shared]	[shared]
Tax	[contractor]	[contractor]	[contractor]	[shared]	[shared]	[shared]
Price escalation	[contractor]	[contractor]	[contractor]	[shared]	[shared]	[shared]

Risk allocation = which party (or parties) has responsibility for the day-to-day operational management of the risk, including management of key controls and mitigating actions.

Cost assignment = which party (or parties) bears the financial responsibility if the risk materialises.

[contractor] = accountability held by the contractor.

[shared] = accountability shared between the delivery agency/state and the contractor.

[agency/state] = accountability held by the delivery agency/state.

'Varies' indicates that the allocation and assignment differs significantly with individual risks in this category.

* Certain contamination risks (e.g. where asbestos is found on site) may be shared for individual projects or may be the responsibility of the principal.

** May depend on whether the change is mandatory or not.

Appendix C – General liability caps and indemnities

Table 9 – Liabilities across procurement models

Risk	Managing contractor	ITC	Alliance
Liability	Aggregate liability of the MC may be capped in the order of the total construction cost. This may vary for different projects.	Contractor's liability is capped at 50% of the contract sum, subject to standard exclusions.	Includes a 'no blame, no disputes' clause. Painshare is typically capped at loss of profit and contribution to overheads.
Indemnities	Typically, the MC to indemnify the principal for damage to persons and property other than the work under the contract.	Contractors are to provide indemnities for property damage and personal injury or death in connection with any act or omission of the contractor. The contractor's liability to indemnify will be reduced (other than to the extent the contractor is entitled to recover under any of the insurances) to the extent that the liability is caused or contributed by: • any breach of the ITC Development Deed by the delivery agency • any fraudulent, reckless, unlawful or malicious act or omission of the delivery agency or any its associates • the contractor's compliance with a direction of the delivery agency • a failure of the delivery agency or its associates to mitigate the extent or consequences of the liability.	Alliance agreements include a 'no blame, no disputes' clause that precludes liability arising between alliance participants (except for wilful default). Subsequently, professional indemnity risks require special consideration and should be covered by project-specific 'first-party' professional indemnity insurance.