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COOPERATIVE RESEARCH
CENTRE
for
CONSTRUCTION INNOVATION

**Cost of Tendering
First Interim Report**

Program	C
Program Title	Delivery and Management of Built Assets
Project Number	2002-035-C
Project Title	Linking Best-Value Procurement Assessment to Outcome Performance Indicators
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Cost of Tendering in Construction

Introduction

This is the first interim report on the **Cost of Tendering component of the Best Value project**. This report provides some insight from 'cost of tendering' literature and discussions with CRC partners.

With the completion of this scoping project, sufficient understanding will be developed to determine the need for more detailed research. This scoping project does not intend to provide guidance for the way to change the tendering process, although a need will be demonstrated for control and reduction of cost of tendering.

Acknowledgement of Cost of Tendering as an Issue

Some key players in the construction industry find tendering to be unnecessarily costly to builders. One CEO observed "the cost of tendering is outrageous".

It will be shown that there is a widely held concern that the cost of tendering for construction projects is disproportionate to the probability of winning jobs and the rewards to those who win them. Various studies show that these costs can be between about 1% and 10% percent of the total project cost. Furthermore, the probability of winning tenders is about 20 percent. This means that the opportunity to recover the cost of tendering depends on achieving a sufficient margin on one of five tenders won. The cost to builders – and ultimately customers – appears enormous (see appendix A) and a better way of awarding projects in the construction industry would reduce total construction costs.

While work has been conducted to demonstrate that there is a cost of tendering and that it is perhaps "outrageous", there has been no effort to identify the specific costs associated with tendering or to quantify these costs. This paper is a proposal for such a study to be conducted.

The Tender Process

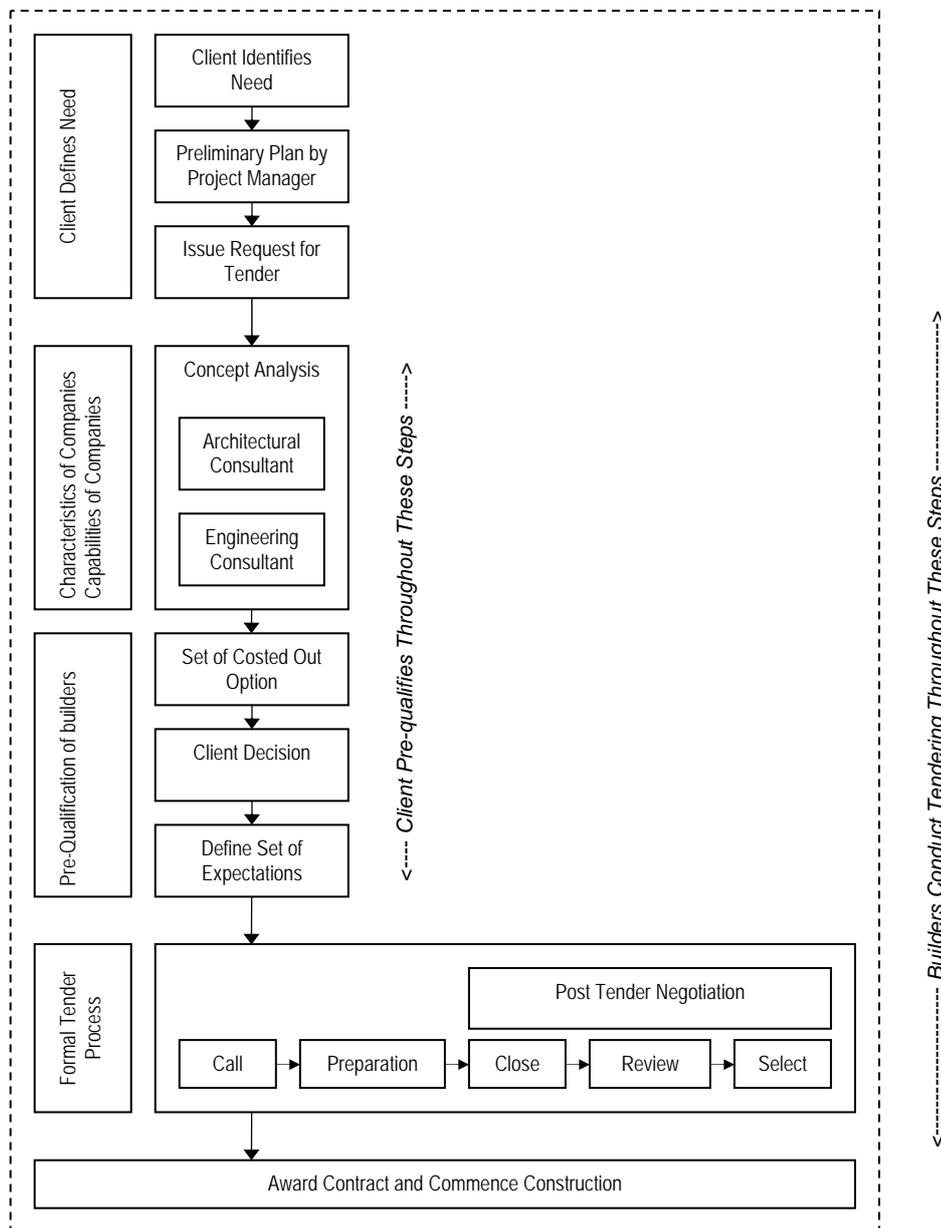
Tendering is the accepted process in the construction industry that that broadly entails:

- Search for prospective suppliers to complete planned work,
- Preparation of proposals to complete work to plan,
- Review of those plans, and
- Selection of supplier.

While it could be viewed in terms of a customer – supplier relationship as simply the selection of suppliers, this process is far more complicated. Whereas in a customer – supplier relationship products tend to be clearly specified, in the construction industry only the materials and end state are specified. There is a far greater opportunity for

construction suppliers to vary the process whereby materials are transformed into the end state. Hence, there is a large design component required for a tender to be prepared; the plan needs to be interpreted in terms of the wide range of resources required to build the end state construction. Furthermore, because of the cost of construction, it is necessary to scrutinise estimates made during the tender development process.

A Generic Tender Process – figure 1



Costs are incurred by builders throughout the tender process (Figure 1). In the initial stages, builders are faced with reviewing requests for tenders, providing marketing literature and meeting with client representatives. These marketing efforts may be duplicated for architectural or engineering consultants. With being pre-qualified by the client, builders are then obliged to engage in the tender process. It is possible to decide to not tender, but this is made in the face of threats of not being given

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opportunities to tender in the future. While builders are assured this is not the case, they remain cautious not to lose their place on lists of potential builders.

There appear to be opportunities to reduce the cost of tendering by placing more of an onus on clients during the pre-selection stage of tendering. By selecting the most appropriate builders to offer tender opportunities, the field can be narrowed considerably. Indeed, there is some attempt to pre-select, but not to a degree necessitated by changes to business practices in recent years.

Margins have reduced significantly rendering the viability of submitting tenders increasingly difficult for many builders (Barker 1998). In an effort to win business, overzealous sales-forces appear to have carelessly submitted under financed tenders that have proven impossible to deliver. Melbourne's Spencer Street Station redevelopment could be such a case. These actions by some sales forces are perhaps driven by unrealistic expectations of some clients, who believe that they can drive down the cost of construction. This sort of economic rationalism was not part of the business environment that led to the contemporary tendering process.

Tendering as occur today has not changed dramatically for several hundred years. It evolved to where it is today in an environment typified by modern sensibilities of fairness and material respect as opposed to what would be referred to as post-modern economic rationalism that subverts the conservative processes that influence how builders operate.

Some Limited Details of Cost of Tendering

While there is limited realisation that tendering has a cost, there appears to be even less understanding of the components of that cost. Wills, et al (2001) state that the cost of tendering "is widely suspected to be excessive" and have shown that the typical cost of tendering ranges between ½ - 1% of turnover, and 2-3% of bid price. While this does not appear to high, they go on to explain that the nature and degree of sub-contracting in the construction industry multiplies these values for every level of sub-contracting. Australian Defence purchasing manuals acknowledge the cost of tendering and have devoted a chapter to this subject. In this document the wastage of scarce resources that arises from inappropriate tendering is acknowledged.

Customers who impose the tendering process would be expected to realise that tendering costs are absorbed into overheads, but one wonders whether or not they realise that they are also paying for costs of failed tenders. It can be supposed from Wills et al (2001) that success rate for large contractors can be expected to be around 10% to 20%. This means that at best one in five won jobs pay the tender costs for five. By comparing this with the cost of tendering for an individual project, and assuming that project values are all equal, about 15% of each project income covers expenses made to tender for the work. This does not appear to cover advertisement, customer relations, public relations and other marketing expenses large constructions firms must expend.

Arndt (1999) notes that the increasing adoption of complex delivery methods such as Build Own Operate Transfer (BOOT) requires clear processes for assessing tenders, awarding contracts and managing the delivery of projects. He acknowledges the “significant costs that arise from involving the private sector in the delivery of infrastructure” being composed of documentation, lawyers and financiers.

Sidwell and Kennedy (2000) observed that the cost of preparing detailed tenders limits the competition for many projects. Wills et al (2001) refer to the “sheer expense of complying with tender procedures.” It is common for those in the construction industry to explain that only the larger firms are able to engage in the tender process. Reeves (2001), on behalf of the Canberra Business Council made a submission to the Inquiry into IT Outsourcing Senate Finance and Public Administration Committee, noted “improvements were needed in ... the cost of tendering”. While his comments refer to information technology (IT) and not construction, his interest is in large infrastructure type projects and in that sense IT and construction are similar.

Hings (1993) Expresses the cost of tendering in terms of his experience leading a national firm of construction cost consultants and quantity surveyors.

Sample Size

The sample size has been raised as an issue by one of the CRC industry partners.

At the beginning of the CRC cost of tendering project, it was proposed to study a large sample of builders. **The decision to broaden the range of participants has been suspended until the outcome of this scoping project.**

Some individual managers of CRC industry partners raised the objection that the CRC industry partners who will provide data are so different that there would be little to compare in a sensible way. They suggested the shortsightedness of **an approach that does not recognise the challenge of comparing the disparate characteristics of builders who operate in atypical ways and who perform unlike work. There is a concern that conclusions might be limited** to providing only an understanding of **superficial** value to all CRC partners. Based on this reaction, it is proposed that a more detailed analysis be undertaken, which does broaden the number of builders who contribute cost of tendering data.

Conclusion

The cost of tendering is **considered by some to be a burden** imposed on an industry that is increasingly suffering from ever tightening margins. **While** the tender process has not evolved in several hundred years, **the construction industry has faced significant changes** in the past 30 years. **It appears that builders may have been disenfranchised as a result; perhaps it is now appropriate to realign the tendering process to reflect recent changes.** How these changes must be designed cannot be

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specified at this time. Further study is required to understand the costs and their impact on builders, clients and the wider public.

This scoping project will continue and a report will be prepared. It is anticipated that a proposal will detail further study of specific costs by reviewing the costs of tendering incurred to a wide range of builders.

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Appendix A
Survey of Costs of Tendering Estimates

Issue	Cost	Location	Source
Tendering costs arising from privatising bus services	24m	Ireland	Competitive tendering could cost Bus Eireann €24m Irish Examiner, 20 May 2004 http://www.breakingnews.ie

Appendix B
Organisations that Acknowledge the Cost of Tendering Is Hight

Organisation	Cost	Location	Source
Department of Health		Ireland	Competitive tendering could cost Bus Eireann €24m Irish Examiner, 20 May 2004 http://www.breakingnews.ie

Appendix C
Organisations that Acknowledge it is appropriate to pay the Cost of Tendering on receiving the tender

Organisation	Cost	Location	Source
NSW Health		NSW Australia	https://tenders.nsw.gov.au/health/shared/help.cfm?p_page=index&p_pagetitle=HOME

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