

Appendix C Supplier selection methods

Direct appointment

Direct appointment is a supplier selection method in which the purchaser selects a single supplier and negotiates the contract terms, including price.

Using direct appointment

Direct appointment may only be used to select a supplier and establish a contract when:

1. the contract is a low dollar value contract (refer to section 10.9 *Direct appointment and closed contest for low dollar value contracts*), or
2. the contract is a low dollar value contract and the supplier selection process commences as a closed contest, but only one potential supplier is identified (refer to section 10.9 *Direct appointment and closed contest for low dollar value contracts*), or
3. the supplier selection process commences as an open competition, but only one potential supplier is identified (refer to section 10.8 *Competition for supply*), or
4. a monopoly supplier situation exists (refer to section 10.10 *Direct appointment of a monopoly supplier*), or
5. the requirements for direct appointment are met (refer to section 10.11 *Direct appointment where competition reduces value for money*).

Proposal evaluation procedure

When selecting a supplier using the direct appointment method, approved organisations must use the following proposal evaluation procedure.

- Step 1** Undertake market research to determine potential suppliers.
- Step 2** Identify the preferred supplier and select on the basis of the supplier's experience and skills with activities of the same or similar nature.
- Step 3** Negotiate contract terms with the preferred supplier and establish a contract that is designed to obtain the best value for money.

Steps 1 and 2 are only relevant when section 10.9 *Direct appointment and closed contest for low dollar value contracts* applies, and the estimated contract value is within the limit that allows use of the direct appointment method.

Alternative proposals

The negotiation process can accommodate any alternative proposals offered by the preferred supplier.

Negotiation

Negotiation is the basis for determining all contract terms, including price.

Lowest price conforming

Lowest price conforming is a supplier selection method in which the preferred supplier meets all the requirements set out in the RFP and offers the lowest-priced proposal, after deducting any added value premium.

Appendix C Supplier selection methods continued

Lowest price conforming continued

Using lowest price conforming

Lowest price conforming should be used where the approved organisation determines that best value for money will be obtained by having suppliers compete on price alone and the approved organisation is not prepared to pay a premium for additional quality. The preferred supplier is the supplier that offers the lowest price and meets all the minimum requirements, including quality, as set out in the RFP.

Proposal evaluation procedure

When selecting a supplier using the lowest price conforming method, approved organisations must use the proposal evaluation procedure below.

Step 1 Rank proposals in ascending order based on price.

Step 2 Evaluate all proposals (except for alternative proposals).

- Commence with the lowest-priced proposal.
- Determine that the proposal is within the RFP's scope and requirements.
- Evaluate each non-price attribute on a pass or fail basis.
- Reject (exclude from further consideration) any proposal that fails against an attribute.
- Cease evaluating proposals when the first conforming proposal is identified.

Step 3 Evaluate alternative proposals.

- Evaluate all alternative proposals (regardless of price) in accordance with the second, third and fourth bullets under step 2.
- Evaluate in accordance with the relevant rules contained in section 10.16 *Alternative proposals*.
- Determine any added value premium in accordance with section 10.17 *Added value premium*.
- Deduct any added value premium from the price of the alternative proposal.

Step 4 Identify the preferred supplier.

- The preferred supplier is the supplier that presents the proposal that is within the RFP's scope and requirements, passes on all non-price attributes and has the lowest price after deducting any added value premium.

Guidelines for proposal evaluation

Rules and guidelines on the selection and evaluation of non-price attributes are set out in section 10.14 *Non-price proposal evaluation attributes*. Section 10.15 *Price and price weight* sets out the relevant requirements for price.

The RFP must establish the criteria that may lead to a non-price attribute being evaluated as a fail and any other criteria that may lead to the rejection of a proposal.

Approved organisations may use a two-envelope system and evaluate the non-price attributes of each proposal before opening the price envelopes, if they consider that the extra time and effort required will be beneficial.

Appendix C Supplier selection methods continued

Lowest price conforming continued

Alternative proposals

Lowest price conforming can accommodate alternative proposals. Alternative proposals must be evaluated in accordance with the proposal evaluation procedure described above.

Negotiation

The approved organisation may negotiate with the preferred supplier, providing any negotiations are carried out in accordance with the RFP's requirements. See section 10.12 *RFP contents and conformity* and section 10.18 *Use of negotiation in a supplier selection process*.

Purchaser nominated price

Purchaser nominated price is a supplier selection method where the approved organisation fixes the price to be paid and advises this through the RFP. Proposals must meet the requirements of the RFP and are evaluated on the basis of quality only.

Using purchaser nominated price

Purchaser nominated price should be used where the approved organisation requires outputs that are difficult to specify but it has determined a price that it is prepared to pay for those outputs and described the desired outcome (in the RFP). Best value for money is then obtained by selecting the supplier that provides the best proposal for the price set out in the RFP.

The best proposal will be determined on the basis of the non-price attributes of the supplier and any differences that the competing suppliers offer in terms of quality or quantity of output.

This method is typically used for such activities as strategy studies, feasibility studies, transportation studies and investigations.

Proposal evaluation procedure

When selecting a supplier using the purchaser nominated price method, approved organisations must use the following proposal evaluation procedure.

Step 1 Evaluate proposals.

- Determine that the proposal is within the RFP's scope and requirements.
- Grade each non-price attribute for each proposal from zero to 100.
- Reject (exclude from further consideration) any proposal that fails against an attribute.
- Multiply the weight (specified in the RFP) by the grade for each non-price attribute and divide by 100. The result is the index for each non-price attribute.
- Add all the indices for each proposal. The result is the weighted sum of the non-price attribute grades.

Step 2 Identify the preferred supplier.

- The preferred supplier is the supplier that presents the proposal that is within the RFP's scope and requirements, passes on all non-price attributes and has the highest weighted sum of the non-price attribute grades.

Appendix C Supplier selection methods continued

Purchaser nominated price continued

Guidelines for proposal evaluation

Rules and guidelines on the selection, weighting and evaluation of non-price attributes are set out in section 10.14 *Non-price proposal evaluation attributes*.

The RFP must establish the criteria that may lead to a non-price attribute being evaluated as a fail and any other criteria that may lead to the rejection of a proposal.

The purchaser nominated price method is not recommended for physical works or public transport services contracts, as, with these contracts, both the outputs required to deliver the desired outcome and the outcome itself are usually well understood. Wherever more than one willing and able supplier exists, a competition that includes price competition will generally be appropriate.

The purchaser nominated price method is also not recommended for routine professional services engagements. As stated above, it may be suited to strategy studies, feasibility studies, transportation studies and investigations where the desired outcome is known but the required outputs are not as well understood. Depending on whether price competition is appropriate, either the quality based or price quality methods will normally be used to find the preferred professional services supplier.

Alternative proposals

When the purchaser nominated price method is used, all proposals are in effect alternative proposals. However, their evaluation will be based on grading the non-price attributes described in the RFP alone, and the requirements and permissions set out in section 10.16 *Alternative proposals* and section 10.17 *Added value premium* will not apply.

Negotiation

The approved organisation may negotiate with the preferred supplier, providing any negotiations are carried out in accordance with the RFP's requirements. See section 10.12 *RFP contents and conformity* and section 10.18 *Use of negotiation in a supplier selection process*.

Any negotiations that led to a decision to let a contract for a price other than the price nominated in the RFP would destroy the integrity of this method and would be determined by the NZTA as being inconsistent with the RFP. See section 10.12 *RFP contents and conformity*.

Price quality

Price quality is a supplier selection method where the quality attributes of suppliers whose proposals meet the RFP's requirements are graded, and the preferred supplier is selected by balancing price and quality through the use of a formula.

Using price quality

Price quality should be used where the approved organisation determines that best value for money will be obtained by having suppliers compete on both price and quality and selecting the supplier that offers the best combination of the two.

The process an approved organisation goes through to decide how much more to pay for additional quality is clearly shown.

Appendix C Supplier selection methods continued

Price quality continued

Proposal evaluation procedure

When selecting a supplier using the price quality method, approved organisations must use the following proposal evaluation procedure.

Separation of non-price and price information

- Proposals must be submitted in two separate envelopes. Envelope 1 must contain all proposal information, other than the price. Envelope 2 must contain the price information.
- Approved organisations must complete steps 1-5 before opening envelope 2.

Step 1 Grade the non-price attributes.

- Open envelope 1.
- Determine that the proposal is within the RFP's scope and requirements.
- Grade each non-price attribute for each proposal from zero to 100.
- Reject (exclude from further consideration) any proposal that fails against an attribute.

Step 2 Calculate the weighted sum margin.

- Multiply the weight (specified in the RFP) by the grade for each non-price attribute and divide by 100. The result is the index for each non-price attribute.
- Add all the indices for each proposal. The result is the weighted sum of the non-price attribute grades.
- Deduct the lowest weighted sum from each proposal's weighted sum. The result is the weighted sum margin for each proposal.

Step 3 Calculate the supplier quality premium.

- Calculate the supplier quality premium for each proposal using the following formula:

Supplier quality premium = estimate * (weighted sum margin / price weight)

- The estimate used in the formula must exclude any amount fixed by the approved organisation, such as any provisional sums contained within the schedule of quantities.

Step 4 Confirm the supplier quality premium.

- Review the supplier quality premium calculated for each proposal.
- Confirm that the supplier quality premium for each proposal represents the amount more that the approved organisation is prepared to pay for a higher-quality supplier.
- Replace any supplier quality premium with an acceptable figure if the review shows that any supplier quality premium does not represent the extra amount that the approved organisation is prepared to pay.
- Confirm the new figure with those responsible for determining the preferred supplier.

Appendix C Supplier selection methods continued

Price quality continued

Step 5 Calculate the added value premium.

- Calculate the supplier quality premium for alternative proposals by following steps 1-4 above.
- Calculate the added value premium for each alternative proposal by following the method set out in section 10.17 *Added value premium*.

Complete steps 1-5 before opening envelope 2.

Step 6 Identify the preferred supplier.

- Open envelope 2.
- Deduct each proposal's supplier quality premium and each alternative proposal's added value premium from the price.

The preferred supplier is the supplier that presents the proposal that is within the RFP's scope and requirements, passes on all non-price attributes and has the lowest price less supplier quality premium and less any added value premium.

Guidelines for proposal evaluation

Rules and guidelines on the selection, weighting and evaluation of non-price attributes are set out in section 10.14 *Non-price proposal evaluation attributes*. Section 10.15 *Price and price weight* sets out the relevant requirements for price and price weight.

The RFP must establish the criteria that may lead to a non-price attribute being evaluated as a fail and any other criteria that may lead to the rejection of a proposal.

Testing the price quality method

Before using the price quality method, an approved organisation must fully understand how the method works. The choices made will influence the proposal evaluation outcome because of their impact on the supplier quality premium values – the amount more that the purchaser is prepared to pay for a higher-quality proposal. Supplier quality premiums are influenced by:

- the price estimate
- chosen non-price attributes
- how the non-price attributes are graded (the spread of grades)
- weights given to the non-price attributes
- weight given to price.

All impact on the supplier quality premiums, but the most significant impact typically arises from the weight given to price.

The *Attribute weight setting tool* is available to help set the weights for the price and non-price attributes. The *Price quality evaluation tool* will also assist with this testing.

Grading the non-price attributes for alternative and non-alternative proposals

Grade the non-price attributes of all proposals, including alternative proposals. Alternative proposals should not be evaluated until step 5.

Appendix C Supplier selection methods continued

Price quality continued

This separation will help ensure that the evaluation of the supplier (the main focus of the non-price attribute evaluation) is separated from the evaluation of differences in the output offered under an alternative proposal (usually the main focus of the alternative proposal evaluation). The distinctions between the two – the supplier and the output offered – are then more easily drawn. See section 10.17 *Added value premium*.

Information and guidelines on how to grade non-price attributes are in section 10.14 *Non-price proposal evaluation attributes*.

The estimate used in the supplier quality premium formula

The estimate used in the supplier quality premium formula must be included in the RFP to ensure that the process is transparent.

As noted in step 3 above, any amount fixed by the approved organisation must be excluded from the estimate. These amounts are usually a provisional sum, a prime cost sum or a contingency sum.

Any provisional, prime or contingency sum priced by a supplier when preparing a proposal and not fixed by the approved organisation must be included in the estimate. The estimate is for the part of the output that the supplier is required to price.

Confirming the supplier quality premium

The review of each proposal's supplier quality premium (step 4) is intended to confirm that no supplier quality premium is too high or too low. If the review concludes that one or more supplier quality premium values should be adjusted, then the conclusion and its reasons must be recorded.

The NZTA expects that use of the permission (in step 4) to adjust one or more of the supplier quality premium values will only be rarely used and its use will be limited to those exceptional occasions when the proposal evaluation process reveals something that could not have been anticipated by a capable purchaser. Before using this permission, the purchaser should consider seeking specific legal advice.

Approved organisations should be mindful of the heightened possibility of a hostile response from proposal submitters if they choose to use this permission in a way that could not have been foreseen by those submitting proposals.

Supplier quality premium values must not be adjusted for an arbitrary or irrelevant reason. Adjustment will in most instances be viewed by suppliers as an admission by the purchaser that some aspect of the procurement procedure design was wrong. For example, when a decision is made to adjust all values by a fixed percentage, this will be seen as an admission that the chosen price weight was wrong.

Approved organisations should state in the RFP that the supplier quality premium values calculated by the price quality method formula at step 3 may be adjusted in certain circumstances. Where the approved organisation can identify the circumstances under which such an adjustment may occur, then, in the interests of transparency, it should outline those circumstances in the RFP.

Disclosing the results of the evaluation process

Approved organisations should advise each proposal submitter of the value of their supplier quality premium, and how it differed from the preferred supplier's supplier quality premium.

Appendix C Supplier selection methods continued

Price quality continued

Alternative proposals

Price quality can accommodate alternative proposals. Alternative proposals must be evaluated in accordance with the proposal evaluation procedure described above.

When using price quality for professional services, true alternative proposals are unlikely to be received. In most cases, professional services proposals are in effect all alternatives. This issue is further discussed in section 10.16 *Alternative proposals*.

Negotiation

The approved organisation may negotiate with the preferred supplier, providing any negotiations are carried out in accordance with the RFP's requirements. See section 10.12 *RFP contents and conformity* and section 10.18 *Use of negotiation in a supplier selection process*.

Quality based

Quality based is a supplier selection method where the quality attributes of suppliers whose proposals meet the requirements of the RFP are graded and the preferred supplier is selected solely on that basis. A price is then negotiated with the preferred supplier, based on their price proposal.

Using quality based

Where the scope of the outputs (works or services) cannot be fully described, competition on price may not help to obtain best value for money. The quality based method should be used where the approved organisation determines that best value for money will be obtained by selecting the supplier on the basis of supplier quality alone. There is no competition on price.

The quality based method is an advanced component where the output being purchased is anything other than professional services. As an advanced component, an approved organisation must have the NZTA's prior written approval under s 25 of the LTMA for its use.

Proposal evaluation procedure

When selecting a supplier using the quality based method, approved organisations must use the following proposal evaluation procedure.

Separation of non-price and price information

- Proposals must be submitted in two separate envelopes. Envelope 1 must contain all proposal information, other than the price. Envelope 2 must contain the price information.
- Approved organisations must complete steps 1-3 before opening envelope 2.

Step 1

Grade the non-price attributes.

- Open envelope 1.
- Determine that the proposal is within the RFP's scope and requirements.
- Grade each non-price attribute for each proposal from zero to 100.
- Reject (exclude from further consideration) any proposal that fails against an attribute.

Appendix C Supplier selection methods continued

Quality based continued

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- Step 2** Calculate the weighted sum.
- Multiply the weight (specified in the RFP) by the grade for each non-price attribute and divide by 100. The result is the index for each non-price attribute.
 - Add all the indices for each proposal. The result is the weighted sum of the non-price attribute grades.
- Step 3** Identify the preferred supplier.
- The preferred supplier is the supplier that has the highest weighted sum of the non-price attribute grades.
- Step 4** Negotiate with the preferred supplier.
- Open the preferred supplier's envelope 2 and enter into price negotiations.
 - Negotiation must be conducted in accordance with the RFP and any contract let must be within the scope of the RFP.
 - If agreement cannot be reached with the preferred supplier, that proposal must be rejected. The supplier that has the next highest weighted sum of the non-price attribute grades is then the preferred supplier – begin step 4 again with the new preferred supplier.
 - When a contract is awarded, the unopened envelope 2 from each supplier that did not take part in the final negotiation process must be returned.

Guidelines for proposal evaluation

Rules and guidelines on the selection, weighting and evaluation of non-price attributes are set out in section 10.14 *Non-price proposal evaluation attributes*.

The RFP must establish the criteria that may lead to a non-price attribute being evaluated as a fail and any other criteria that may lead to rejection of a proposal.

Because price is not a factor in the selection of the preferred supplier (it is negotiated), purchasers are able to adopt a wider variety of price structures than with other methods.

Establishing the scope of the required output(s) and the price

Under this method, price is typically negotiated with the preferred supplier before a contract is let. This method can also be used to establish a price mechanism, rather than a price.

Prior to determining a price, it is necessary to establish an agreed scope of output. This must be communicated to all suppliers before the suppliers responding to the RFP present their price proposals (envelope 2). If the agreed scope of the outputs is not communicated there is a risk that the purchaser and suppliers will form different views of what is required.

The suppliers may view the scope as being more expansive than can be purchased for the price envisaged by the purchaser. The purchaser may respond by negotiating a lower price with the preferred supplier, and reduce the scope and quality of the outputs in the process. Use of the quality based method in this way is unlikely to deliver best value for money.

Appendix C Supplier selection methods continued

Quality based continued

To address this issue, each RFP must include a statement of the expected scope of the required outputs and estimated price. Suppliers responding to the RFP should be encouraged to comment on the accuracy of the scope and price statement prior to the closing date for RFP submission so that refinements can be made if necessary.

It is recommended that approved organisations consider using a staged approach to supplier selection with this method. The purchaser would then establish a short list of at least three suppliers and then enter into a formal dialogue with those suppliers (individually or collectively or both) to refine the scope and price statement before the price proposals (envelope 2) are submitted.

The price agreed with the preferred supplier could be a lump sum if the output can be adequately defined and identified risks can be managed. Alternatively, the price may be based on a schedule of intermediate outputs, or on input rates and agreed quantities.

Price negotiation

The negotiation process should not result in a large change in the quality or scope of the outputs, or in the proposed price.

Using the method to establish a price mechanism

This method can be used to select a preferred supplier and negotiate a contract that includes a mechanism to establish the price, rather than the price itself.

For example, under an alliance (a shared risk delivery model) a price mechanism rather than a price is agreed at the time the contract is let. A supplier panel or a framework contract is often established on a similar basis.

Seeking assurance that the price is reasonable

When there is competition on price, the purchaser will have some assurance that the price is a reasonable market price. The purchaser should use other means to obtain that assurance when using the quality based method.

A well prepared expected scope of the outputs and estimated price statement, along with benchmarking against similar engagements will increase the approved organisation's confidence that the price is reasonable. Open book accounting can also be used to achieve price confidence when this method is used to establish a price mechanism (rather than a price).

Alternative proposals

Alternative proposals cannot be accommodated with the quality based method. All proposals are in effect alternative proposals.

Negotiation

Negotiation plays a major role in obtaining value for money under the quality based method. Approved organisations using this method need to be clear about their requirements and know what a reasonable price should be so that they can negotiate on an informed basis. Approved organisations should also consider whole-of-life costs for the activity when negotiating on price.
