



DISPUTE



Snap shot

Context

A government client awarded a contract for remote off-shore logistics, emergency and medical services, facilities contraction and maintenance, catering, and cleaning services. The contract was worth more than \$100 million per annum, had been in place for three years, and had a six-month renewable term. Client staff were dissatisfied and viewed the contract as over-priced.

Objective

Resolve disputes with contractor without invoking formal dispute clauses.

Kiah approach

Strategy, negotiation and management of legal and consulting support.

OPPORTUNITY FROM ADVERSITY—
A 30 PER CENT COST SAVING

A government client was three years into a competitively awarded contract for remote, offshore, logistics including:

- ▶ rotary wing support
- ▶ emergency and general medical services
- ▶ facilities construction and maintenance
- ▶ catering
- ▶ cleaning services.

Worth more than \$100 million per annum, the contract provided services essential to the client's outcome. The services could be required for as long as a decade, however, the future was unpredictable, and no commitment over 12 months could be made. The existing contract had a six-month renewable term.

There was dissatisfaction amongst client staff who viewed the contract as over-priced. This resulted in reinterpretation of the contract, and part payment and non-payment of invoices to the value of several million dollars a month. Senior executives only discovered the problem when anticipated expenditure profiles were not met.

Client dissatisfaction was compounded when an external audit uncovered invoicing errors going back several years.

Further, the auditor's findings were based on an incorrect—albeit reasonable—interpretation of the contract. This added to the confused client-contractor interaction resulting in continuous operational tension and a deterioration in working relationships and service quality.

While the formal dispute clauses of the contract had not been invoked, the disagreement had escalated and was being dealt with at the highest levels of both client and contractor organisations.

Kiah was invited to assist in resolving the dispute through strategy, negotiation and management of legal and consulting support.

An initial strategy session with the client established that a sustainable resolution would require two issues be addressed:

- ▶ a resolution of the historical disputes and outstanding payments
- ▶ a clearer and more commercial contract moving forward.

The client's predilection was to resolve the disputes, then go to competitive tender—considered the traditional and safe option. In strategy sessions an alternate plan was developed that provided: greater options, flexibility and negotiating power; and rapid cost reductions for a less expensive program of work.

The client adopted a strategy to offer dispute resolution and to negotiate a longer term contract for revised services and price that would be accepted if it was proven to be value for money. It was also proposed to work with the contractor to redefine the scope of work for the most cost-effective and commercial delivery without imposing unnecessary constraints. The client would reserve the right to go to competitive tender should a compelling value for money proposition not be forthcoming. This approach provided for both a reward and sanction to the contractor.

The strategy adopted two fundamentals principles of commercial resolution: proposals solve problems, and the organisation making the proposal seizes the initiative and defines the landscape in which a solution will be found. This was ultimately the case.

The third and fourth principles Kiah espoused were thorough preparation, and realistic expectations. Kiah needed to understand what would be an acceptable 'value for money' future solution, and what were realistic expectations for the resolution of the historical disputes.

Legal advice on disputed matters was sought. While some issues were clear, most were ambiguous, confused by long-term behaviours.

OPPORTUNITY FROM ADVERSITY – A 30 PER CENT COST SAVING

Commercially, all things are negotiable and given the carrot of a longer term contract, a better outcome was possible. Resolution of disputes need not be a wholly legal matter, and while legal input is essential, disputes are fundamentally commercial and business issues. The value of well-framed arguments, the traditional legal approach, has much less significance in a commercial negotiation where the objective is to trade 'value' so that both parties walk away with acceptable outcomes.

In the public sector not all business factors are commercial, and acceptable value is often driven by other factors. Legal, commercial and public sector advice was workshopped to produce a game plan. Before engaging with the contractor, the client knew what reasonable offer could be made, what the likely responses might be, what was acceptable/unacceptable, and how the responses would be handled.

Our approach to understanding 'value for money' for the future contract was to build a commercial model for the delivery of the services as if we were the contractor. Consulting support was engaged to forensically analyse accessible client data including historical transaction volumes and trends. A complete business model was independently built to understand the cost of service delivery. This is a very similar technique to the 'Red Team' so often used by industry in preparing major tender responses where a solution is tested against requirements and competitor information.

Not only did this provide powerful knowledge to be used in negotiation, it gave the client comfort that they could justify commercial decisions against a benchmarked and costed solution. Only after having done this work was the contractor engaged. On behalf of the client we offered a full proposal – integrating historical disputes resolution, and a proposed future contractual solution within an anticipated price range. The initial meetings were not easy.

The contractor initially saw the cost reductions as unreasonable, and believed a 10 per cent reduction would be more achievable. This was not unexpected, the proposal was a direct attack on their margin. The value of the strategy was that our client had effective options, a timetable,

and was making defensible statements based on knowledge. The offer was reasonable and commercially valuable to the contractor – the alternatives were much less attractive.

Within six weeks all disputed matters were resolved and a future concept agreed. It took several months to carefully translate the concept into a sustainable legal agreement, in which the obligations of each party was clear. This was a joint activity, that allowed both parties to work together to ensure the removal of areas of discontent, and the inclusion of shared learnings.

Project consulting and legal support costs were in the range of \$350,000–400,000. Immediate savings of \$1 million per annum were negotiated and were realised when the future agreement was finalised. Overall, the contract price was reduced by in excess of \$30 million per annum!

The rapidly developed original contract was highly priced, short-term, ill-defined and high-risk, but reasonable for what was needed at the time. Won by competitive tender, it was assessed as value for money. The contractor delivered on what they were contracted to, and while possibly somewhat opportunistic, they had no obligation to lower prices or amend the contract to their detriment. To change the situation, the customer must take the initiative. It is highly unlikely that a new competitive process would have achieved a better outcome, as the price struck was calculated on actual service delivery costs, and resolved all disputed matters fairly. Realistically, a competitive process could have cost the client 12 months and \$30 million in excessive payments.

As circumstances change so should contracts. Disputes don't mean disaster – strategically they can offer opportunities, especially if managed holistically, focussing on the overall relationship and outcomes being sought. Planning and preparation, as in everything, is the key. Seize the initiative, propose the way forward.

Conventional wisdom says that best price comes from competitive approaches, and usually this is a valid approach to engagement, but it only guarantees the best competitive price, not the best achievable price. That outcome is best achieved through strategic negotiation and, sometimes, unorthodox approaches. 