



Précis Paper

ECI Contracting

A discussion on how to optimise early contractor involvement, and the various stages of the process.

Discussion Includes

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ECI Contracting

1. In this edition of BenchTV, Geoff Wood (Of Counsel, Baker McKenzie) and Franco Aversa (Special Counsel, Baker McKenzie) discuss how to optimise early contractor involvement, and the various stages of the process.

What is ECI contracting?

2. ECI contracting stands for Early Contractor Involvement. It started to be used in the UK road industry. They were finding that with complex projects that it was very difficult to get people to bid, and the bids they were getting were very high. The industry started to develop a type of contracting which involved getting the contractors involved earlier in the process, hence Early Contractor Involvement.
3. It usually involves an owner taking the course of a procurement process which would usually deal with at least a couple of ECI contractors to have competitive pricing. Sometimes it is only one, and this is known as sole source ECI contracting.
4. The owner and the ECI contractors can work together during the ECI phase to workshop project risks and look at all of the nuances, complexities and challenges of the program, working together in a collaborative way, towards the ECI contractor making a risk-adjusted offer to do the second phase of the project.
5. Sometimes the ECI contractor will stay on a relational basis, however the typical ECI process is one where the phase one of relational involvement leads towards an offer to do the contract on a hard dollar basis. A project which does not use ECI will have a contract which has to make assumptions regarding possible risks.
6. The benefit that people see in ECI, and why it seems to be getting used more and more, is that it gives the contractors the chance to get right across a project, learn a lot more about what the principal really wants, learn a lot more about the site and the particular risks, and therefore be able to price in a much more confident and accurate way a bid to do the job on a hard dollar basis.

Advantages of ECI contracting

7. ECI contracting allows owner and contractor to work hand in glove to analyse the scope and complexities of the job and the specifics of the site, to take advantage of the owner's detailed knowledge of what they want and the design and interface aspects of what can be a complex job can be analysed a lot more before the contractor has to commit and give a price.

8. The potential for variations is said to be lessened because the contractor is more involved with the design development and therefore is not going to look for changes further down the line.

Disadvantages of ECI contracting

9. The main disadvantage which owners have to consider is that there is a lot of involvement for their senior staff during the first phase.
10. It can be a costly process to run. There can be costs for having a facilitator.
11. The owner can lose the direct advice of their advisory team because they go over to the contractor.
12. If the process is a lengthy one, if there is any staff turnover or breakdown in the relationship between the parties it can have a bad impact on this way of contracting.

Which factors determine if an ECI contract is appropriate?

13. If a job is complex ECI contracting gives contractors the chance to get across all of the complexities and allows them to factor risk into their pricing.
14. If there are design unknowns or if there are alternative technologies which might be pursued to put this project in place, then it gives the owner the chance to workshop and get to know people who are offering different technical solutions or different design approaches and decide which one is most suitable.
15. ECI contracting gives contractors the benefit of the owner's inside knowledge of their project and their needs, so that parties are much more aligned by the time they're coming to commit to a hard dollar contractual relationship.

Is ECI contracting used only in particular industries?

16. ECI contracting is being used across a very wide range of applications in the Australian market.
17. One industry where it has become very popular in Sydney recently is office fit-outs, when contractors come in to do something to a building that someone else has designed.
18. On brownfield sites where there is a lot of interface with other contractors or existing operations, whatever the industry is, ECI may be worth considering.

The ECI procurement process

19. Typically there are three phases to an ECI procurement process. Usually it begins with the owner going out and finding people who are interested in participating in such a process, with the right experience and skill set to be considered. From a shortlist, and then use a request for proposal process to get those people to make offers to participate in what would be the third phase, that phase being the ECI phase itself.
20. There is ultimately a fourth phase when someone makes an offer at the end of the third phase on a hard dollar basis.

Selection criteria for an ECI Contractor

21. Owners are typically going to be looking at the resumes of the different tenders, looking at their capabilities and seeing if they have worked in this particular industry before, looking at the personnel that they are offering to see if that is an appropriately skilled team. They will look at the systems that they use and the cost rates, for both direct and indirect cost.
22. It is important to see whether the contractor has actually done any relational contracting before, and can show a track record of working successfully in collaboration with an owner on this sort of process.

How many contractors?

23. It is far more typical for people to run competitive processes with at least two ECI contractors engaged to firm price offers received at the end of that process, selecting one of those two.
24. Single-source ECI does not have that competitive price tension in the process. There may however be a particular reason why an owner would have to go sole source, for instance there might be a very thin market for the sort of people needed to do the particular job. It may be that there is a challenging time-frame and there may not be the time to run parallel processes with two ECI contractors. It is also the case that sometimes if people have got a very good track record of working with a particular contractor then they may feel comfortable to do a sole source ECI.
25. Single-source ECI is being used more frequently in Sydney in recent years.

The ECI phase

26. ECI is a typical collaborative process. There will be a kickoff meeting with the ECI contractors where they are fully briefed about the project. There will be a relationship management plan developed. There will be discussion around the development of a charter or mission, and mutual goals and objectives that the parties want to get out of the process, then there will be an agreement of core values and goals will be set up for

the parties to pursue through that ECI process. These will be assessed and measured throughout the process.

27. The design development, which may have already gotten to a certain stage prior to the ECI process, will be flipped over to the contractors, and there will be a very close collaboration between the ECI bidders and the designers as that process progresses
28. There will be a series of workshops ranging across all the different aspects of the project. For instance, early on there will be workshops about risks and opportunities that in the project. There will be workshops about schedule and about value engineering.

Settling the terms

29. The ECI scope that an ECI proponent will have to deliver during the ECI phase will vary from project to project but ultimately they'll always be pursuant to an ECI agreement, a definition of ECI services that will usually include all that came out of the various workshops between the parties.
30. Once a decision has been made, the parties can then enter into the second phase and the owner can decide whether or not they want to accept the firm proposal. These aspects certainly need to be captured within an ECI agreement.
31. As the parties want certainty as to how this second phase, the delivery phase, is going to operate, it needs to be known on what terms those works will be performed.
32. The principal will often out a term sheet of key terms of the stage to delivery.
33. At least some of those contract terms are going to be up for discussion and possible change, and the owner would be indicating that.

Pricing in the ECI phase

34. There are various pricing options available to a developer/owner embarking on an ECI process. They range from no payment all the way to full reimbursement of costs for the process.
35. Both ends of the spectrum are becoming less common. What is more usual is that a hybrid approach of part payment, for example a contractor will be able to claim a certain percentage of their costs. Another approach which is being seen more recently is that the contractors will be able to claim all of their costs up to a capped amount, and that capped amount is usually set earlier on in the tendering process.
36. It makes sense to offer some payment, partly because you actually want to have some contractual obligations enforceable at the end of the process.

Timing of payment

- 37. There are also various options available when it comes to the timing of payment as well. It is common these days for the payment not to actually happen until the end of the process. There is usually an obligation on a contractor to submit a firm offer in to make sure that they are committed to the process. The final payment is usually conditional upon various things including adherence to and compliance with the ECI contract.
- 38. This is quite important from an owner's perspective, particularly when it involves a sole-source ECI contract, because you may get to the end of a process and find that you are no closer to a contract than you were at day one, if it has not been set up appropriately in terms of both what it is that a contractor is being asked to deliver and how you are going to be remunerated for doing that.
- 39. The owner will, as they normally will on any scope of services, have a power of variation. They may change what a contractor wants to do. A variations provision is an important aspect of an ECI agreement, as one of the key advantages of an ECI contract is that the parties are coming together to try and workshop a solution on price, and as the ECI phase develops it is quite possible that where the project is going may be a little different from where the owner expected it to be at the outset, and this could be for very good reasons. There may be a wish to expand the ECI contractor scope or to change it, where for example there has been an agreed lump sum capped amount on remuneration and it makes sense to adjust that amount if the contractor is asked to perform more works in a particular area.

Indemnity, liability and confidentiality

- 40. In terms of security for performance, what has been seen more recently is having the final payment for the ECI services conditional upon actually submitting the binding offer, having actually performed the works in accordance with the contract, etc.
- 41. There are typically indemnities around breach of confidentiality, personal injury, infringement of third party IP rights.
- 42. A key risk for the owner, especially one who is sole-sourcing, is that if they don't get a risk adjusted offer at the end, then they will have wasted a lot of time and money.
- 43. There are other avenues of protection available to an owner/developer. For example, typically there is a termination for convenience at any point in the process in favour of the owner.
- 44. There is no compulsion for an owner to go and give an ECI contract at the end of the initial ECI process. If they don't like the offer or offers that they receive, they always reserve the right to not award any contract and pursue the project with someone else, or not at all.

45. The liability position in an ECI contract will depend upon two things : the liability situation of the preferred proponent, and the what will happen to an unsuccessful ECI proponent?
46. For a successful ECI proponent, the liability situation is usually quite easy. It is basically a clause that says that all of the liability will roll into the EPC contract, and anything that is performed under this contract will be rolled into that contract, and whatever the overall cap on liability is under the EPC contract or D&C contract.
47. From an owner's perspective, it is very important that an ECI contractor is not able to draw a line in the sand when they are successful and go through to the delivery phase and claim that their liabilities are capped at a lower amount due to works done in the earlier phase.
48. There will usually be a cap on liability for an unsuccessful ECI proponent, which is usually expressed as a percentage of the ECI services fee.
49. If a principal has a time critical project and needs to sole-source, and therefore let go of a few other options, there is a danger that contractor will then blatantly turn their head away, and there need to be incentives for a contractor not to do that.
50. Owners should look very closely at the specifics of their project and remember that ECI is a complicated process which can also be quite expensive.

BIOGRAPHY

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Franco specialises in major projects. As well as extensive experience at a senior level at Bakers and King and Wood Mallesons, Franco spent a number of years in house with tier 1 contractor Abigroup (now Lendlease Engineering). He is an industry focused lawyer who is dual qualified in the legal and engineering fields. Franco has wide-spread transactional experience in the documentation and negotiation of major Australian infrastructure projects

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Geoff Wood is Of Counsel in the Sydney office of Baker McKenzie where he specialises in construction, infrastructure and major projects. With more than 30 years' experience, Geoff is recognised as one of Australia's leading construction lawyers and is experienced in all aspects of the negotiation, documentation and administration of major construction, civil engineering, resources, defence and privately funded infrastructure projects, together with alliancing and the outsourcing of maintenance and other functions.