

<b>Project</b>	<b>A40 Llanddewi Velfrey to Penblewin Improvements</b>
<b>Subject</b>	Historic changes in scheme costs and cost overrun mitigation
<b>File Reference</b>	A40LVP-ARP-GEN-SWI-FN-J-0003
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<b>Status</b>	<b>S4   SUITABLE FOR STAGE APPROVAL</b>
<b>Revision   Date</b>	P01   18/03/20

## 1.1 Purpose of this document

1.1.1 On Wednesday 18 March 2020, while giving evidence at the Public Local Inquiry Mr Peett, of Caermaenau-Fawr, requested clarification on the changes to the scheme budget since the scheme was re-started by Welsh Government in 2016.

1.1.2 The purpose of this public inquiry document is to clarify changes in scheme cost estimates as the project progressed and to explain how budget overruns will be mitigated on this project.

## 1.2 Changes in historic scheme cost estimates

1.2.1 Mr Peett stated, in his oral evidence, that he had read that the scheme budget had previously been announced to be £57 million.

1.2.2 Following clarification, Mr Peett advised that, to the best of his knowledge, this scheme budget of £57 million related to the A40 Llanddewi Velfrey to Penblewin Improvements (the subject of this Public Local Inquiry) only. This did not include any costs associated with any other Welsh Government schemes being considered along the A40 between St Clears and Haverfordwest, notably the A40 Penblewin to Redstone Cross Improvements.

1.2.3 A potential source of the scheme budget stated by Mr Peett has been identified. The below article published on 16 January 2018 by the Western Telegraph<sup>1</sup>, following the liquidation of Carillion, stated

<sup>1</sup> <https://www.westerntelegraph.co.uk/news/15829460.collapse-of-carillion-will-not-delay-60m-pembrokeshire-bypass-project/>

*“The £57m contract for the 5km road was awarded to Carillion at the start of last year”.*

- 1.2.4 An additional source of the scheme budget stated by Mr Peett may also have been an article published by Construction News on 03 February 2017, which noted that Carillion had been awarded the “contract to design and build a £57m bypass” around Llanddewi Velfrey<sup>2</sup>.
- 1.2.5 Welsh Government formally announced the award of the contract to Carillion PLC on 09 January 2017. This can be viewed on Welsh Government’s website<sup>3</sup>.
- 1.2.6 The image below taken from the website shows the text of the announcement in full:



- 1.2.7 As can be seen from the text quoted above, the overall value of the contract was not included in the announcement. As such, it is assumed that Mr Peett’s source of information regarding the scheme budget is from news articles such as the ones referenced in paragraphs 1.2.3 and 1.2.4.
- 1.2.8 The Contract Notice initially published by Welsh Government on 25 March 2016, prior to the competitive tender process for Early Contractor Involvement project noted that the expected Contract

<sup>2</sup> <https://www.constructionnews.co.uk/civils/sectors-civils/exclusive-carillion-wins-57m-a40-bypass-in-wales-03-02-2017/>

<sup>3</sup> <https://gov.wales/decision-reports-2017>

Value would be between £55 million and £60 million<sup>4,5</sup>.

- 1.2.9 The value of the scheme budget of £57 million, as noted in the two news articles above, is within the range of between £55 million and £60 million as indicated in the Contract Notice for the ECI Contractor. Therefore, it is reasonable to conclude that the source of the information for the news articles was based on Welsh Governments understanding of the scheme costs in early 2016.
- 1.2.10 In June 2018, following the liquidation of Carillion in January 2018, there were various news articles in the press, which stated that “*Cabinet Member for Economy and Transport Ken Skates, in a letter to AMs, has confirmed that £35m will be invested to upgrade the route*”<sup>6</sup>.
- 1.2.11 These news articles were because of a letter from Ken Skates AM, the Cabinet Secretary for Economy and Transport, on 10 September 2018<sup>7</sup>.
- 1.2.12 In this letter Ken Skates AM states the following (quoted verbatim for the avoidance of doubt):
- 1.2.13 “I appreciate that the uncertainty created by Carillion’s liquidation has been frustrating for residents, but given that we have secured £22 million of EU funding to support delivery of this £35m scheme, I am delighted that we are now in a position to move forward.”
- 1.2.14 The reduction in the publicly quoted values of the scheme from between £55 million and £60 million (as stated in the initial Contract Notice) to £35 million (as stated in the letter from Ken Skates AM) was primarily due to a competitive tender process, which was undertaken between March 2016 and December 2016. The result of the competitive tender process was that the submitted budget estimates from all contractors were significantly less than Welsh Government’s initial budget which had informed the values in the

<sup>4</sup> [https://www.sell2wales.gov.wales/search/show/search\\_view.aspx?ID=MAR127730](https://www.sell2wales.gov.wales/search/show/search_view.aspx?ID=MAR127730)

<sup>5</sup> <https://ted.europa.eu/udl?uri=TED:NOTICE:102869-2016:HTML:EN:HTML&tabId=1&tabLang=en>

<sup>6</sup> <https://www.westerntelegraph.co.uk/news/16300023.35m-llanddewi-velfrey-to-penblewin-upgrade-confirmed/>

<sup>7</sup> <https://www.assembly.wales/deposited%20papers/dp-1736-16-21/dp-1736-16-21-en.pdf>

Contract Notice. As such, Welsh Government re-evaluated the scheme budget to align with the submitted tenders, with £35 million being the resultant scheme budget.

1.2.15 Since the statement by Ken Skates in September 2018, the Welsh Government team have developed a more detailed scheme cost estimate (£39.5m<sup>8</sup>), which is now based on the design which has informed the draft Orders and is presented before this Public Local Inquiry. The level of detail within the design is more significant than that referred to previously, which means a more accurate scheme cost estimate could be prepared.

1.2.16 In his proof of evidence, Philip Thiele (traffic & economics expert witness) in paragraph 7.58 to 7.62 explains how scheme costs have been prepared for input into the economic appraisal. In summary, this is based on the preparation of a base cost estimate, which captures elements such as the cost of labour and materials. Risk and optimism bias was quantified by following the methodology set out in guidance and added to the base cost estimate.

## 1.3 Mitigation of budget overrun

1.3.1 To manage the risks in the construction phase of the contract, both from a cost and programme perspective, Welsh Government have undertaken various additional surveys since September 2018. These additional surveys include:

- Topographical surveys;
- Ground investigation;
- Environmental surveys.

1.3.2 Welsh Government commissioned these surveys to be undertaken before a construction contract is awarded so that the information could be made available to the prospective tenderers. This approach will enable the tenderers to have a better understanding of the likely risks associated with the project which should lead to more realistic and robust tender submissions. This approach should also provide Welsh Government with higher levels of confidence that tenderers can

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<sup>8</sup> Refer to Philip Thiele's proof of evidence (WG 1.2.2) Table 8

deliver the scheme for the values stated in the tender submissions.

- 1.3.3 In addition to the up-front surveys undertaken by Welsh Government, there are various procurement strategies available to Welsh Government, which should lead to the submitted tenders being as realistic as possible. In the case of this project, the commercial model for the tender is that all tenderers who submit a cost at or below the average cost (of all submitted tenders) will receive maximum marks from a commercial perspective. This approach is intended to encourage the tenderers to price the works realistically and does not encourage tenderers to submit unrealistically low-cost estimates.
- 1.3.4 Additionally, if one tenderer submits a cost that is 80% or below the average of all tendered prices. Welsh Government has the right to reject the bid as being abnormally low under the Public Contracts Regulations 2015. Both these procurement strategies are aimed at encouraging the tenderers to be realistic with the commercial elements of their submissions.
- 1.3.5 As well as the procurement strategies outlined above, Welsh Government has decided to use the New Engineering Contract 4 (NEC4) Engineering and Construction Contract (ECC) for the next stage of the project, that being a Design and Build Contract. Within the NEC4 ECC contract, there are various options, which can be chosen. For this project, Welsh Government has chosen Option C – Target Cost with an Activity Schedule.
- 1.3.6 The basis of a Target Cost contract is that Welsh Government and the Contractor will share both the under-spend (often referred to as gain) and the over-spend (commonly referred to as pain) via a set of pre-defined share ranges which are applied to an agreed Target Cost. The Target Cost is set at tender and is subsequently only amended if the independent Project Manager instructs a change to the Scope.
- 1.3.7 If the Contractor can deliver the whole of the works for less than the agreed Target Cost, then both Welsh Government and the Contractor take a share of the under-spend. Similarly, if the Contractor is unable to deliver the whole of the works for the agreed Target Cost, both Welsh Government and the Contractor take a share of the over-spend.
- 1.3.8 For this project, Welsh Government require greater certainty over the costs, and as such, Welsh Government have opted to place a cap on

their liability for any overspend. As such, should the costs for the Contractor to deliver the whole of the works exceeds the cap on the Target Cost, the Contractor will be required to fund the entirety of this over-spend.

- 1.3.9 It should be noted, however, that this does not mean that the overall costs will not increase. There are often legitimate reasons where the Scope of the project should be amended, and the Contractor should be entitled to additional fees in these scenarios. However, if the project enters into an over-spend scenario Welsh Government are protected by the capped share range, which limits their overall costs as a percentage of the agreed Target Cost.

## Approvals

Revision	Status	Role	Name	Date
P01	S4	Author	Ellie Mitchell (X)	18/03/20
		Checker	Philip Thiele	18/03/20
		Approver	Tom Edwards	18/03/20
		Authoriser	Gary Davies	18/03/20