

GUIDANCE

Assessment of Abnormally Low Tenders for Works Contracts

1 August 2019

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Section I: Purpose

This document provides guidance on the “Assessment of Abnormally Low Tenders for Works Contracts” as referred to in para. 3.27 of the Bank’s Procurement Policies and Rules.

Section II: Definitions

N/A

Section III: Scope

1. Introduction

In August 2019, the Bank introduced provisions into the Bank’s Standard Procurement Documents for the Procurement of Works (SPDPW). These provisions permit clients to reject Abnormally Low Tenders (“ALTs”) following a comprehensive clarification and examination process. The provisions are consistent with para 3.27 of the Bank’s Procurement Policies and Rules (PP&R), 1 November 2017 edition, which states “*In the event that a tender for works is identified during the evaluation process as being considered as abnormally low and the tenderer is subsequently unable to demonstrate beyond reasonable doubt through a clarification process its capability to perform the contract for the offered price, the tender may be rejected subject to prior no-objection by the Bank*”. The Bank recognises that the grounds upon which an ALT may be rejected can be highly contentious and controversial. As such, any decision to reject a tender on this basis must be supported by robust documentary evidence and be able to withstand scrutiny. To assist clients in this regard, the Bank has produced this Guidance with the intention of clarifying the process that Bank clients shall follow during the tender evaluation process prior to making a decision as to whether an ALT shall be accepted or rejected.

2. Definition of an ALT

It is generally accepted that it is very difficult, if not impossible, to provide a definition of an ALT that captures all possible scenarios. For the purposes of this Guidance, and as a general rule, the Bank considers an ALT to be a tender submission where the tender price, in combination with other constituent elements of the submission, appears to be abnormally low in relation to the subject matter of the contract to the extent that the tender price raises material concerns with the procuring entity as to the capability of the tenderer to perform the contract for the offered tender price.

3. Identification of an ALT

In view of the general difficulty in establishing a common definition of an ALT, the first essential step in the tender evaluation process is to identify if the tender offering the lowest evaluated price may be an ALT and therefore requires further in-depth review and clarification. Typically there are two approaches that may be followed in this regard, the ‘absolute’ approach and the ‘relative’ approach. The ‘absolute’ approach generally entails the identification of an

ALT based on a comparison of a tender price, and its constituent parts, with the client's own cost estimate for the works, whilst the 'relative' approach provides for the identification of an ALT based on a comparison of a tender price with the average tender price submitted by other tenderers (whilst disregarding the client's own cost estimates) and taking into account the statistical deviation from the average using the rules of normal distribution in statistical analysis. Whilst the 'absolute' approach can theoretically be applied in any given situation (on the assumption that a reliable cost estimate exists), the 'relative' approach can only be considered reliable in a situation where a reasonable number of tenders have been submitted.

As a general rule, in situations where fewer than five (5) tenders have been submitted, the Bank advocates the use of the 'absolute' approach as a basis to identify ALTs. In situations where five (5) or more tenders have been submitted, the Bank advocates the use of the 'relative' approach which provides sound results. Nevertheless, it is considered that the 'relative' approach, albeit with less reliable results, may be used even if the number of tenders is as low as three (3).

In this regard, the Bank has developed a mathematical formula, for the purposes of attempting to identify tenders which fall into the ALT 'risk zone', which shall be used when the 'relative' approach is to be applied. The formula may be used in MS Excel, or similar applications, by entering the array of data (say A1...AN), the mean can be calculated by using the following function AVERAGE (A1:AN), and the standard deviation by using the formula STDEV(A1:AN). Thus the formula for calculation of the ALT risk zone threshold is: AVERAGE(A1:AN)-STDEV(A1:AN).

Following the 'relative approach', any tender that falls into the ALT risk zone (and is therefore potentially an ALT), and which is subsequently proposed for contract award, must be subjected to the ALT Evaluation and Clarification Process elaborated in Section 4 of this Guidance prior to the submission of a contract award recommendation to the Bank. In the event that fewer than 5 (five) tenders are submitted all tenders shall be considered to be in the ALT risk zone and the tender which is subsequently proposed for contract award must be subjected to the ALT Evaluation and Clarification Process.

In the event that an ALT has been identified in the tender evaluation process, the tender evaluation report shall contain full details of the 'absolute' or 'relative' basis upon which an ALT (or ALTs) has or have been identified.

Notwithstanding whether an 'absolute' or a 'relative' approach is applied to identify a potential ALT, clients shall be aware that the Bank will not, under any circumstances whatsoever, accept or agree to the automatic rejection of a tender suspected to be an ALT in a situation where no attempt to clarify the basis for the suspected ALT has been made by the client. Equally, no tenderer shall be permitted by a client to withdraw its tender (without the forfeiture of its tender security) during the tender validity period purely on the basis of its own determination that its tender is an ALT (for example, based on a comparison of its own tender price with the read-out prices of the other tenderers).

4. ALT Evaluation and Clarification Process

Following a determination by a client that a tenderer has submitted a tender that is potentially an ALT, in the event that a client subsequently proposes to recommend award of contract to that tenderer, the client has a mandatory requirement to establish the capability of the tenderer to perform the contract within its total tender price, before submitting the tender evaluation

report to the Bank for no-objection (for contracts subject to prior review), or, finalising the tender evaluation process and awarding the contract (for contracts subject to post review).

The process of establishing whether a tenderer is capable to perform a contract within its total tender price can be highly complex and subjective, particularly for design-build type contracts. In instances where Bank clients do not have the necessary in-house capability and expertise, clients may require the input of independent consultants with substantial knowledge and experience in the relevant sector. Nevertheless, the Bank will be unable to provide its no-objection to a proposal to reject a tender on the basis that it is an ALT until such time as it is satisfied that the client has undertaken the necessary analysis and due diligence as detailed in this Guidance.

The following provides details of a sample procedure that could be applied to works contracts of an average complexity, and particularly where a detailed design and Bill of Quantity (B/Q) exists. For more complex works contracts, for example those requiring a substantial level of innovation from tenderers, a more appropriate procedure may need to be developed with the support and assistance of suitably qualified consultants (if applicable, due consideration to this aspect should be considered during the project planning stage to ensure that the 'Terms of Reference' for any implementation consultant(s) include an appropriate provision at the outset of the project).

The determination as to whether an ALT shall be rejected shall be made in accordance with Section III: Evaluation Methodology of the SPDPW which states *“If in the opinion of the Client, the Tender which results in the most economically advantageous priced Tender, is seriously unbalanced or front loaded or determined to be abnormally low, the Client may require the Participant to produce detailed price analyses for any or all items of the Price Schedules, and supplementary evidence, to demonstrate the internal consistency of those prices with the information provided in the Participant’s technical proposal. After evaluation of the price analyses, and taking into consideration the contract cash flow forecast, in the event that the Client still considers that the Tender is seriously unbalanced or front loaded, the Client shall clarify its concerns with the Participant in writing. In the event that the Participant is subsequently unable to demonstrate beyond reasonable doubt its capability to perform the contract for the offered price, the Tender shall be rejected as non-responsive”*.

Requests to tenderers to produce and submit “detailed price analyses” and/or “supplementary evidence” shall be carried out in accordance with the procedure contained in ITT 25 – Clarification of Tenders of the SPDPW. Clients shall ensure that tenderers are provided with a reasonable period within which to provide any requested clarifications, detailed price analyses and/or supplementary evidence. Under normal circumstances, and dependent upon the volume/complexity of information to be provided by a tenderer, a period of 5 - 10 business days shall be considered to generally constitute a reasonable period.

The price analysis would normally comprise of the following basic cost components: Tender Price = Cost of Works (materials and labour) + Overhead Expenses + Contingency + Profit. Therefore, the Employer’s evaluation of the capability of a tenderer to perform the contract within its total tender price shall focus on the price analysis of any or all the items of the works to be performed by the tenderer and their internal consistency with the tenderer’s estimate of the resource inputs required for the performance of the works and/or associated pricing by the tenderer.

The evaluation process shall commence with an arithmetical check of each tender followed by a preliminary evaluation of the tender price. The purpose of this preliminary evaluation is to identify any particular parts of the works which may have been grossly underestimated by the tenderer and which would therefore merit further detailed evaluation of the tenderer's estimate of resource inputs and associated pricing incorporated in the tenderer's total tender price. This preliminary examination should look to identify issues such as;

- Has the tenderer omitted to price some items and does this appear to have been intentional or accidental?
- Are some items priced significantly lower than estimated? And if so, is this a consequence of an arithmetical error or a misplacement of a decimal point or has the tenderer misunderstood what is to be included in the rate?
- Are certain items/types of items consistently under-priced across the B/Q (e.g. cost per metre of laying pipes in a trench) and are there any indications why this may be the case?

Following this preliminary evaluation the following steps shall be undertaken:

Step 1

- **Evaluation of the Tenderer's Estimate of Resource Inputs associated with Performance of the Works.** Contractors may perform identical works using differing volumes, sequencing, timing and combination of resource inputs, such as construction equipment, staff and labour, materials. A tenderer's estimate of such resource inputs, which would be required for the performance of the works, shall be the first step in the evaluation of the tenderer's capability to perform the contract. All tenderers should have estimated the volume of the resource inputs required for the performance of the works on the basis of the construction methods, sequence and timing of the various construction activities, sources of materials etc, i.e. on the basis of the tenderer's preliminary work programme. Accordingly, the Employer shall first examine the preliminary work programme submitted in the lowest priced tender and determine if it is in fact realistic, taking into account the specific circumstances of the project site.

For example, a tenderer may choose topsoil removal works to be executed using self-propelled scrapers. If successful, the tenderer should be able to execute several construction activities using the selected equipment and construction method and ultimately perform the works faster, with less support equipment, fewer operators and lower operating costs as compared to other construction methods. Consequently, the selected construction method should have a direct impact on the prospective cost of the works to the tenderer and ultimately its tender price. However, should the tenderer misjudge the specific circumstances of the project location e.g. availability of the equipment, transportation distances to the designated dumping sites, concentration of rocks in the topsoil, etc, the tenderer may not be capable of following the selected construction method and, if awarded the contract, will suffer substantial cost overruns during the execution of the works on account of having to: a) modify or substitute the selected construction method; and b) cover the cost of additional support or new equipment, operating costs, etc. Moreover, if the Employer were to accept the tenderer's tender price, having full knowledge that it is based on a flawed preliminary work programme, then the possibility arises that following contract award to the tenderer, any inability to execute the works in accordance with such a programme could give rise to a claim or variation by the tenderer.

In view of the above, if the Employer determines that the preliminary work programme submitted by the lowest price tenderer for any part or all of the works is not realistic, the Employer shall evaluate whether the tenderer will be capable to modify or substitute the proposed construction method(s) therein within the tenderer's total tender price whilst remaining consistent with the mandatory requirements of the contract. It should be noted that such evaluation can be carried out by the Employer without violation of the Banks' procurement rules (i.e. "Tenderers shall not be allowed or asked change their tender..... during evaluation or as a condition of award) only if the preliminary work programme accompanies, but does not form a part of, the tenderer's tender. (*Note: This provision is also consistent with the FIDIC recommended Example Form of Instruction to Tenderers, according to which, "the tenderer shall also submit the following supplementary information accompanying, but not forming part of, his Tender:" --- "(d) details of the arrangements and methods which the tenderer proposes to adopt for the execution of the Works"*).

Step 2

- **Statistical Evaluation.** All tenderers will have individually determined the prospective cost of the works prior to the submission of their tenders. Therefore, providing that the preliminary work programmes adopted by the tenderers are comparable (see above paragraph), the average subtotal of rates (subtotals) quoted by the tenderers for various parts of the works should be representative of the actual cost of the works and constitute a sound benchmark for the preliminary assessment of the sufficiency of subtotals quoted by the lowest price tenderer for the respective parts of the works.
- **Line Chart of Subtotals Quoted for Various Parts of Works by other Tenderers.** With the exception of subtotals quoted by the lowest price tenderer, the Employer shall first enter all subtotals quoted by other tenderers for various parts of the works into a combined line chart. The Employer's estimated subtotals for the respective parts of the works should also be inserted into the line chart.

The Employer shall compare all subtotals for each part of the works in the line chart and note the nature of any inconsistencies with the view to:

- (a) identify any evidence of frontloading; and
- (b) determine the average representative subtotal of rates for each part of the works (average subtotals).

All line charts should normally be balanced providing that the preliminary work programmes adopted by the respective tenderers are comparable. A substantially unbalanced subtotal should generally constitute evidence of frontloading by a tenderer or incidence of a gross error in the tenderer's estimate of the actual cost of the respective part of the works. For comparison purposes, such individual subtotals should be adjusted within the total price quoted by the respective tenderer or, as the case may be, the Employer's estimate for the entire works, in proportion with the average subtotals for the respective parts of the works quoted by other tenderers and the Employer's estimates.

- **Comparison of Subtotals Quoted by Lowest Price Tenderer with those Quoted by other Tenderers.** Once the Employer has determined the average representative subtotals for each part of the works (average subtotals), these shall be compared with the respective subtotals quoted by the lowest price tenderer.

In the event that all the subtotals quoted by the lowest price tenderer transpire to be consistently below the average subtotals, such a price ranking may constitute evidence that the lowest price tenderer has grossly underestimated its overhead expenses and/or chosen to incorporate an exceptionally low profit margin and contingencies in its rates. In such instances, the Employer's further evaluation should concentrate on the breakdown of the tenderer's overhead expenses and clarification of the basis for determining its profit margin and contingencies.

In the event of any exceptional shortfall between the average subtotal and the subtotal quoted by the lowest price tenderer for any individual part of the works, the Employer's further evaluation should concentrate on the detailed price analyses and assessment of its internal consistency with the estimate of resource inputs and pricing of the respective individual part of the works.

- **Preliminary Clarification and Request for Tenderers' Detailed Price Analyses for the Works.** Following the preliminary evaluation, if the Employer considers that further clarification from the tenderer is required, the Employer may request the tenderer to produce detailed price analyses for any part of the works in accordance with ITT 25 of the SPDPW.
- **Content of the Employer's Clarification Request for Price Analyses.** The Employer's clarification request for price analyses shall focus on the issues that will have been identified during the preliminary evaluation and clarify the basis on which the Employer determined that the tenderer's pricing of the works may be abnormally low. The contents of the Employer's clarification request shall ensure that the tenderer will be in a position to provide an equally focused response to the Employer. In order to expedite the tender evaluation, the Employer shall also provide the tenderer with the format in which the tenderer will be expected to submit its price analysis. In this regard, a sample 'Form for Detailed Analysis of Unit Rates' that may be used for this purpose, if appropriate, is attached at Annex 1.
- **Clarification of the Tenderer's Overhead Expenses and Contingency.** It should be noted that the basis upon which a tenderer may factor overhead expenses into its tender prices can be substantially different from that used by other tenderers. The respective value of the individual overhead expenses may therefore fluctuate within considerable margins. This can be evidenced with reference to the outcome of tendering exercises held on a "slice and package" basis, which show that tenderers' discounts for the award of more than one contract can range between 0-30% of the tender price. Hence, the margin of overhead expenses may vary substantially and can be manipulated by any tenderer after the date of tender submission taking into account the ranking of its tender price vis-à-vis other tenderers. The Employer should therefore require that all tenderers shall provide detailed information pertaining to their overhead expenses as part of the tender submission. The same position should be taken with regard to contingencies for the same reason.

Step 3

- **Detailed Clarification and Request for further Tenderer's Price Analyses for the Works.** Following the receipt of the tenderer's detailed price analyses, the Employer shall determine if the tenderer's estimates of the resource inputs and the pricing of the works provided therein are consistent with the Employer's respective assumptions. If the Employer determines a potential shortfall in any of the items of the tenderer's price

analyses the Employer shall request further clarification from the tenderer which may include appropriate documentary evidence that would validate the tenderer's price analyses. The Employer's clarification request shall focus on the issues that have been identified during the detailed evaluation of the tenderer's initial price analyses and clarify the basis upon which the Employer determined that the tenderer's assessment of the works may be abnormally low. The Employer should also convey to the tenderer that any attempt of misrepresentation by the tenderer within the framework of the tender evaluation may fall within the definition of the prohibited practices and may be subject to the Banks' respective Enforcement Policy and Procedures.

- **Clarification of the Tenderer's Estimate of Resource Inputs.** If the Employer determines that the tenderer's estimate of a resource input associated with particular part of the works may not be realistic or is substantially below the Employer's respective assumption, the Employer shall request the tenderer to clarify to the Employer's satisfaction the basis on which the tenderer has:

- (a) estimated the respective resource input; or;
- (b) determined that the underlying work programme arrangements can be modified or substituted within its total tender price;

The tenderer's clarification may include its estimate of labour requirements, sources and volume of materials, construction plant and equipment, transportation distances, etc required for the performance of the part of the works for which the Employer requires clarification.

- **Clarification of the Tenderer's Estimate of Pricing.** If the Employer determines that the tenderer's estimate of the cost of a resource input may not be realistic or is substantially below the Employer's respective assumption, the Employer shall request the tenderer to submit appropriate evidence that would substantiate its pricing of the respective resource input including, as may be necessary, further detailed price analyses in respect of the resource input questioned by the Employer.

The tenderer's clarification may also include a description of the nature of the tenderer's access to the proposed construction equipment e.g. hire, lease, purchase agreement, etc and any documentary evidence that the tenderer utilised for determining its tender price during the tendering period.

- **Report of Evaluation of Tenderer's Detailed Price Analyses and Employer's Recommendation.** At the end of the detailed evaluation of the tenderer's price analyses the Employer shall produce a concise report that shall form an annex to the Tender Evaluation Report (TER) and that shall include the following summary information:

- a) The value of the tenderer's estimates of the resource items and respective pricing which the Employer determined to be unrealistic or substantially below the level required for satisfactory performance of the works;
- b) The value of the Employer's estimates and assumptions in relation to the resource items and respective pricing required for satisfactory performance of other works;
- c) The value of the shortfall identified in the tenderer's tender; and
- d) The recommended outcome of the 'Detailed Evaluation of the Tenderer's Price Analyses'.

The report shall also include details of any objection that the tenderer may have highlighted with regard to the Employer's estimates and assumptions in relation to the resource items and their respective pricing and appropriate justification of the grounds on which the Employer has rejected the tenderer's objections. The Employer's recommendation shall be included in the report. In addition, the tender evaluation report shall incorporate copies of all clarification exchanges between the client and the tenderer.

Step 4

- **Employer's Recommendation.** Following evaluation of the tenderer's price analyses and detailed clarification thereof, in the event that the client has established that the tenderer is unable to demonstrate, beyond reasonable doubt, its capability to perform the contract within its total tender price, reject the tender submitted by the lowest evaluated substantially responsive tenderer in accordance with the relevant provision contained in Section III: Evaluation Methodology of the SPDPW.

Clients should be aware that, as a part of the Banks' fiduciary oversight, for complex/high value/contentious cases it may be necessary for the Bank to seek an independent opinion with regard to the basis and logic behind any decision to reject an ALT prior to the Bank being in a position to issue the Bank's no-objection to the proposed contract award.

Section III: Disclosure

This Guidance will be disclosed on Bank's website.

Section IV: Effective Date

This Guidance is effective from 1 August 2019

Section V: Decision Making Framework

Associate Director, Operations, Procurement Policy and Advisory Department is accountable for this Guidance

Director, Procurement Policy and Advisory Department, is responsible for this Guidance

Section VI: Related Documents

EBRD Procurement Policies and Rules (POL/2017/3)

EBRD Standard Procurement Document for the Procurement of Works (August 2019 edition)

