

# PANEL CONTRACTS IN THE PUBLIC SECTOR

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## INTRODUCTION

The Mandatory Rules (applicable to central Government procurement, with other public sector agencies encouraged to apply them) have focussed a spotlight on panel contracts.

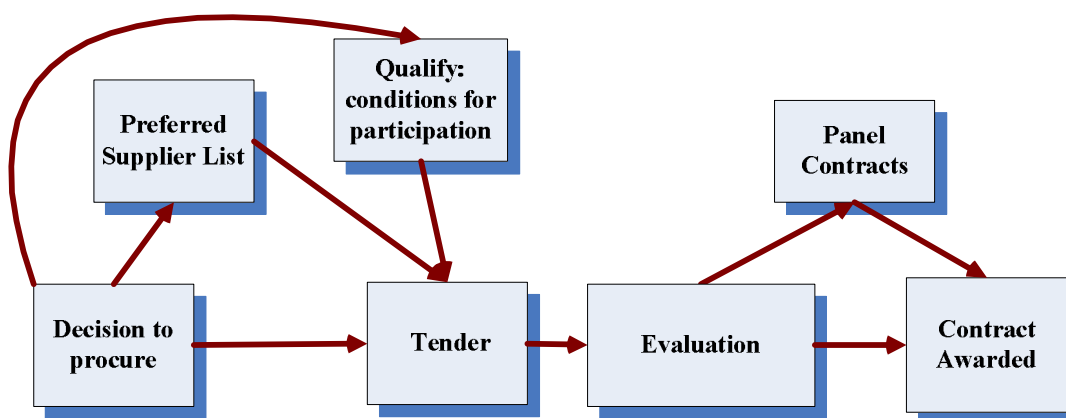
As an illustration of issues in respect of panel contracts, we deal with one issue that has come up in our dealings with agencies: can the agency unilaterally pick and choose from the selected panel? This question brings out some of the wider benefits and challenges of panel contracts.

We also use a professional services panel as an example to tease out the issues. (We consider that panel contracts have roles well beyond professional services).

Panel contracts, used well, have wide application, can markedly reduce time and cost, and benefit agencies, while being fair to suppliers as well.

## PANEL CONTRACTS ARE NOT PREFERRED SUPPLIER LISTS

Preferred supplier lists (rarely used as it happens) are a different beast. That is shown by this diagram, which sets out the flows under the Mandatory Rules:



## CAN THE AGENCY UNILATERALLY PICK AND CHOOSE FROM THE SELECTED PANEL?

Our experience is that agencies can try to push for this. They argue that fairness requirements end when the panel has been selected.

Except maybe in respect of smaller purchases (and maybe not even then), we think it would be unwise for agencies to pick and choose from the panel without relying on some sort of principled approach. That is so whether or not the agency is covered by the Mandatory Rules. There is a wide variety of potential ways of handling this. As often happens in procurement, each situation depends on its own circumstances.

So our comments in this paper are subject to the particular situation in each instance.

We agree with the OAG's view, in the new procurement guidelines, that, in the process to select the panel, the method of sharing the work should be articulated. However the processes listed in the new guidelines amount to one of the few points on which we diverge from those excellent OAG guidelines.

We consider that:

- particular circumstances can call for additional options to the three options listed by OAG; and
- using only the OAG's options may be unfair to suppliers, as well as not achieving optimal outcomes for the agency.

The OAG lists the following ways of sharing the work between the selected panellists:

- *Hierarchical* (one panel member gets most of the work; if it can't do it, others step in);
- *Equal division* of work between panel members (eg; when one supplier has done \$x work, the next supplier is chosen, and so on);
- *Rotational* basis (work is distributed to each panel member in turn, regardless of value and time).<sup>1</sup>

As we note below, apart from the first option in some circumstances, these three methods are neither fair (in most instances) nor do they deliver the ultimate goal: value-for-money goods and services.

Fortunately, there should in our view be sufficient flexibility under what are guidelines, not edicts, to take a different approach than outlined in the OAG guidelines, where that is appropriate. Also the OAG Guidelines are to be interpreted subject to, and in light of, rules such as the Mandatory Rules. So, there should be solutions to this to avoid using the three options listed above.

However, as the "default" position is as set out in the Guidelines, the rationale for departing from them should be clearly set out and recorded by agencies. Any departure from the Guidelines, which is not justified, entails risk.

## **WHY USE PANEL CONTRACTS?**

In our research, the best and most comprehensive guidance we have found on panel contracts is the South Australian Government Guidelines. For those doing work in this area, we strongly recommend a close read, making necessary adjustments for NZ conditions. The Guidelines were updated in August 2009<sup>2</sup>.

Here is a useful summary, from South Australia, which explains why public sector agencies should be looking closely at this panel contract option (and why some agencies are actively engaging in this area):

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<sup>1</sup> OAG Guidelines on Procurement (2008) Para 4.49

<sup>2</sup> <http://www.spb.sa.gov.au/documents/Panel%20Contracts%20Guideline%20v1.0.pdf>

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"Panel contracts provide a framework agreement in which purchasing leverage is used to negotiate high levels of customer service; timely supply of quality goods and/or services; and highly competitive prices or capped prices with a selected number of suppliers. Legal aspects including the development of a draft standard contract are settled at the time of establishing the panel contract as are targets and measures for contract performance.

Use of panel contracts achieves substantial savings and benefits to government in reduced purchasing, administration and transactions costs and simplifies purchasing activity in agencies by:

- achieving best possible quality, service and prices through the combined purchasing leverage of agencies;
- ensuring high levels of agreed customer service are maintained;
- achieving savings in administrative costs for end users by avoiding duplication in preparing specifications, public requests for tender, calling and evaluating tenders and sourcing services;
- eliminating duplication of effort in re-approaching the market through open tender calls for repetitive supply needs;
- avoiding unnecessary market research;
- focusing on agency-specific requirements and not duplicating criteria already established, tested and met through the panel contract;
- stimulating relationships and opportunities for strategic alliances or partnerships with suppliers;
- achieving standardisation and consistency in tender processes and documentation; and
- reducing the costs to suppliers in responding to fewer tenders.<sup>8</sup>

## **HOW MUST AGENCIES CHOOSE FROM THE PANEL?**

The Mandatory Rules<sup>4</sup> apply compulsorily only to Government Departments and Ministries, but other public sector agencies are encouraged to use them. Although circumstances will differ (so each situation must be separately considered), other public sector entities should consider following similar principles, at least as to panel contracts.

Having noted that, the Mandatory Rules say little about what to do. Some interpretation is needed.

Under the Mandatory Rules, panel contracts allow the agency to purchase, from the panellists that have been selected: "*at its option ..., as and when required, identified goods or services ...*".<sup>5</sup>

If this is read in isolation, the agency appears to have unfettered discretion to pick and choose from the panel suppliers once they have been selected, by competitive process, to join the panel.

This would usually, however, be an unwise approach, not only legally but also for probity and other reasons, including potential criticism from the Auditor-General, reputational considerations, etc. There is the obvious but important point that, if the vendors on the panel consider they have been handled adequately, claims against the agency are unlikely.

It is generally prudent for agencies to avoid interpreting the Rules restrictively.

The Rules go overboard to minimise restricted application. We consider a narrow approach is risky. Agencies should adopt the spirit of the Rules.

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<sup>3</sup> Government of South Australia "Joint Procurement Arrangements: Panel Contracts" (State Supply Board Policies, number 4a) (September 1999) (these guidelines have since been superseded but they provide an excellent summary).

<sup>4</sup> See our article, Mandatory Rules for Procurement – One year on

<http://www.wigleylaw.com/Articles/LatestArticles/mandatory-rules-for-procurement-one-year-on/>

<sup>5</sup> Paragraph 42 Mandatory Rules.

Audit New Zealand, for example, has indicated that its audit in relation to the Rules will "... be looking for a proper consideration of underlying policies and how to put them into practice, rather than just a narrow compliance approach."

Other parts of the Mandatory Rules<sup>6</sup> indicate that the choice from the panel should seek best value for money for the particular purchase. This includes consideration of efficient process (the point of establishing the panel in the first place), while having regard to fairness as between suppliers, and viability of the panel as a competitive supply base.

A balanced approach in other words which in our view applies to panel contracts beyond selection of the panel.

This is readily achievable while optimising one of the key goals: reducing the time and cost of the procurement process overall.

We agree with the following comment from an experienced procurement specialist in Government:

*"Admittedly the [Mandatory] rules are not explicit on the selection of a supplier from a panel for a particular purchase, but there is implicit guidance in Clause 4 of the Rules i.e. the decision [about how to purchase from the panel] should be consistent with the general principles of policy and good practice as referred to in Clause 4. This means the choice from the panel should seek best value for money for the particular purchase, which includes efficient process (the point of establishing the panel in the first place), while having regard to fairness as between suppliers, and viability of the panel as a competitive supply base. A balanced approach in other words."*

There are different ways in which a principled approach can be taken, ranging from the most extreme (seeking a quote or equivalent proposal from each of the panellists in respect of the particular job) through to some sort of rotational approach as between panel members.

There should be a broad measure of discretion however: so long as the approach is relatively principled and fair, it can be pragmatic, with room for some variations in approach. The importance of minimising project risk should not be lost sight of, while trying to minimise probity risk. Often, the suitable panel member will clearly be only one of the providers. The model needs to be flexible enough to allow for this.

Additionally, what seems at first sight to be fair (such as a "rotational" approach), may in fact be quite unfair. For example, a panel may have a range of providers, big and small, with different forms of expertise within each provider. To work simply on a rotational basis (or even to give equal payments to all providers over time), may in itself be unfair. In any event, that could be counter-productive for the agency in terms of getting best outcomes and value for money. That is a major problem in most instances with a fixed approach such as equal division or a rotational approach. Almost invariably, there will be reasons other than price why one vendor on the panel will be more suitable for a particular job.

Requiring what looks like "equality" (such as a rotational or equal payment approach) can also drive a real problem with panels: the idea that a small number of panellists should be appointed of similar size and expertise. This can cut out other options such as panels comprising big and small providers, and suppliers with general and with specialist expertise.

That can, in itself, end up breaching probity requirements and there are plenty of poor examples of this.

There are a number of other options and also ways in which agencies can minimise risk.

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<sup>6</sup> Such as clause 4, as to consistency with general principles of policy and good practice.

As with many issues in the procurement space, each situation will vary. However, attention to broad requirements of fairness – and sensitivity to the expectations of the vendors on the panel - will often provide the right and pragmatic answer. Clearly setting up the methods to be used (and any flexibility) in the panel framework contract is highly desirable to reduce risk. The framework contract is the contract signed by the successful panel members. It is the contract under which individual jobs are allocated (often by an exchange of emails (sometimes with some formality such as an order form, but still on-line). The method should be as expeditious and cost-efficient as circumstances allow.

### **APPLES COMPARED WITH APPLES OR PEARS?**

In a perfect world, the panel should comprise providers that provide largely the same type of services (apples and apples). In this way, the framework agreement signed by all panellists will have more agreed, thereby reducing time and cost involved in negotiating further detail. Sometimes however, an apples and pears approach is better, or necessary as it is not possible to get that level of granularity on the panel.

Most panels will have pears along with apples, meaning that an equal-allocation-of-work method will be unworkable.

### **AN EXAMPLE: A PANEL CONTRACT FOR PROFESSIONAL SERVICES**

Let's work through the example of professional services provided by a range of consultants from different disciplines. This illustrates some of the issues and reflects advice we would give. It is important to recognise that panel contracts are designed to speed up the process, reduce cost, etc, and there is a measure of balance between going to the market on a competitive basis (post-appointment of the panel contract) and efficiency on the other. This is particularly relevant where the goods or services being purchased have relatively small dollar values.

The South Australian Guidelines provide some helpful advice on the optimal approach, by setting out types of purchases, broken down into four categories within a quadrant (ranging from low risk/low value to high risk/high value). However we differ from the South Australian guidelines on one point as to the quadrant. Although services provided by consultants may fit into the low value/high risk area (for which competitive procurement as between the panel members is recommended in South Australia), we consider that there are other ways of doing this. Often (or even generally) we consider the customer does not need to go to more than one provider on the panel.

A key point is to try to strike the right sort of balance as between panel members so that they each, over time, get a reasonable share of the work. That assumes that you take that type of approach of seeking some sort of proportionality. The South Australian guidelines correctly suggest a number of options. It is quite conceivable that circumstances arise by which one supplier gets all the work and others get none (for example, because particular expertise is needed during the time period of the panel contract).

This does not mean that each of the panel members will get the same dollar value over the term of the panel contract arrangement. That in itself would often be unfair, unequal, and produce unsatisfactory outcomes for the agency. For example:

- We expect customers will often want to have a range of providers on a panel, varying, maybe, from smaller one-person firms through to larger multi-disciplinary practices. If a small provider has to get the same dollar value of services over the three year term as the large provider, this may not only be unequal but it will also encourage perverse outcomes by encouraging appointment of only the larger providers and not smaller providers.
  - Often there is going to be an array of providers on the panel with differing types and levels of expertise. Additionally, they may have different charge-out rates and other methods of charging (and it does not at all follow that all panel contracts require all providers to have the
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same pricing) This could lead to a large degree of inequality as between the panel members, in terms of the work they get.

- Of particular importance is not to put the projects unduly at risk as a consequence of a need to meet some perceived but unnecessary probity requirement. The ultimate and dominant aim is to get value for money and great outcomes for the customer. Additionally, panel contracts are aimed at speeding things up and reducing procurement cost.

For these reasons, the volume of work going to particular providers could vary considerably, yet that would be legitimate and appropriate.<sup>7</sup> To minimise the risk and to help meet probity requirements, we suggest:

- The agency endeavours to take a reasonably fair approach as between the panel members but that its approach is dominated by the needs of particular projects, recognition of different skill sets, etc.
- If it appears that some providers are getting significantly less work than others, particular sensitivity and care is needed, even if the asymmetry is justified.
- The “value for money” driver for public sector procurement will often be met by having a higher charging consultant doing the work compared with a lower priced consultant, given the former’s expertise and experience. Charge out rates are but one factor in the equation.

This is a convenient point to draw one conclusion in relation to the consultants. Frequently in relation to panel contracts, public sector entities will try to get a standard charging basis across all providers. That will not be possible where different disciplines and skills are involved. There may be a situation where, even within a discipline, a specialist may charge more than another. This just means that the customer doesn’t get one of the potential benefits of panel contracts: aligning all pricing. But other advantages remain.

It is particularly important to set up an expectation as to what is to happen in the RFP, with this ultimately reflected in the panel contract signed by the successful panel members (that is, in the framework contract before individual jobs are allocated). Setting this up in an RFP and a contract will not eliminate all legal and probity risk, but it will go a long way toward protecting the customer.

We also think it is particularly useful to keep the panel members informed of what is happening, in relation to ongoing developments, and even the detail around who wins which projects if that is appropriate.

Contract management (an area focused upon in the South Australian Guidelines) is often something that falls away after contracts (including panel contracts) are awarded. As the South Australian Guidelines point out, one of the strengths of panel contracts is the ability to keep panel members involved, informed, and enable them to contribute to the way in which services can be provided in the future. Some public sector entities are even going to the extent of setting up specific add-ons to their contract arrangements which involve concepts equivalent to non-binding “partnership” structures. If the customer wants to go down that path, however, that needs to be carefully teased out as there is a lot of misapprehension and misapplication of this concept.

In relation to particularly large contracts, the customer may consider going out to get estimates or quotes from several or all members of the panel. As ever, some judgment can be exercised as to when to do this. Another way of proceeding is to set internal and/or external dollar or other dividing lines as to where the customer will or will not go to two or more of the panel on particular projects.

Have a good paper trail at all times, especially to document why the agency has decided to go ahead with particular provider, particularly where it might be potentially controversial.

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<sup>7</sup> Note also that simply using rotational appointments is not satisfactory, generally.