Case Study
BAA Terminal 5 Project

Introduction

BAA’s Terminal 5 Programme at Heathrow Airport is currently one of Europe’s largest construction projects. When complete it will cater for approximately 30 million passengers a year and will provide additional terminal and aircraft parking capacity. The facility will be opening to the public on 30 March 2008 and represents a £4.2bn investment for BAA.

BAA as a client organisation had never undertaken a programme of this scale before or developed integrated assets on this scale. To achieve audacious targets in money and programme BAA had to consider a different contracting and procurement strategy. This step change would require pushing the boundaries of traditional construction thinking and delivery.

Procurement Strategy

In the early 90’s BAA embraced the ethos of partnering in their first generation partnering consequently BAA had already procured circa 50 construction and consultancy frameworks agreements in the mid 90s. These agreements had been advertised in the European Procurement Journal with the selection of suppliers being geared around delivering Terminal 5. However, the supply chain was not able to mobilise immediately due to the extended public planning enquiry.

BAA’s framework agreements are structured in a manner different to that of traditional construction contracts. Suppliers signing up to BAA agreements are expected to work in integrated teams and display the behaviours and values a kin to partnering. The opportunity based relational model needed to be developed further for T5.

Contracting Strategy

Before embarking on the Terminal 5 programme of works BAA looked at a number of UK construction major projects to ascertain lessons learnt historically particularly where they had gone wrong and how this should influence/affect BAA’s approach. BAA had to consider significant potential impacts such as risk, industrial relations, resources, interfaces and multiple suppliers. Change was something that also needed to be well managed as well as a flexible construction solution. Research and history had told BAA that traditional procurement thinking should be revisited and a move to a position where they were actively managing the cause of risk and not the effect of risk was the way forward. BAA decided that they had to have a contract that could deal with a living/adaptable approach, dealing with the unknown and embracing integrated teams. So BAA wrote their own bespoke contract, The T5 Agreement, which would underpin the strategy and not detract from it during delivery. The same conditions of contract apply for all key suppliers on T5 irrespective of type or usual position as a subcontract.

The T5 Agreement

As part of BAA's research into historic projects they looked at process, organisation and the behaviour of people. They wanted to promote and motivate success. History had told them that successful delivery was about project culture and the commercial environment and unfortunately traditional thinking most behaviours, good or bad, were mainly driven by the contract and supplier margin – not a common purpose. This is achieved by common terms and team planning.

Leadership was also key, especially in a changing environment. People will always look for guidance and behavioural traits from their leaders and the issues would be ten times the norm on this programme. The T5 Agreement asks all key audiences in the team to demonstrate commitment, trust and team work.

For BAA it is an enabler to exceptional performance, eg BAA holds all the risk all of the time – on time, in budget and to quality.

For the suppliers – it gives them opportunity to create competitive advantage for their business – using T5 as a showcase. It also enables a step change in performance.

To the teams it means working in highly effective integrated teams that are committed to achieving T5 milestones. It is about trusting each other and relying on each other to work together and it is about supplier teams and BAA staff working on one team.

Central to the T5 Agreement is a proactive approach to risk management and recognition that transfer of price risk under the traditional model was unworkable on a programme of this scale.

The Structure of the T5 Agreement

For this to work, BAA divided the programme into 18 projects ranging in size from £10m to £200m. They then split further into 150 sub-projects and then it was split into circa 1000 work packages. The suppliers are engaged as and when on plans of work where a supplier's capability is required.

The T5 Agreement is the terms and conditions for everybody working on T5 structured as follows:

- The Delivery Agreement is the legal deed and conditions of contract.

- The Supplement Agreement is the part which identifies the skill capability and capacity the supplier can bring to T5. It defines the potential scope of work on the programme.
- Functional Execution Plans detail the support required to enable Projects to deliver.
- Sub Project Execution Plans detail the team's plan of work.
- Work Package Execution Plan details the breakdown of work by each team member/individual supplier.
- The T5 Agreement is then supported by other documents such as the Commercial Policy and core processes, which define commercial environment and an appropriate commercial tension.

The key aim of the Agreement being that it is an unique legal contract which manages the cause and not the effect. It ensures success in an uncertain environment and focuses on managing risk rather than avoiding litigation.

Engaging their suppliers

- Commercially T5 Agreement presumes a common understanding of cost as a starting point or "given" because of BAA's unique approach to managing risk they are able to really get inside a supplier organisation and look in-depth at their cost structures. They feel justified in doing so because they have to carry any risk, therefore their argument is that they have to assure themselves the supplier can do the job.
- There is a requirement for a high level of transparency between BAA and their suppliers. If the contractors were carrying more of the risk then BAA wouldn't expect to have such transparency.
- This has been culturally very challenging for some suppliers. The culture of transparency was effectively built over the first 18 months – 2 years. They had to consistently enforce their working philosophy across a wide range of people. It has to be constantly enforced in line with changes to the supplier base over the project's development.

Relationships

- From the very start BAA requested that suppliers work together in completing the projects (even those that are traditionally rivals) or lower tier subcontractors.
- BAA had to be sure that contractors understood the contract they had signed and to do so tested expected behaviours through scenario-based tests.
- At a corporate level BAA made sure both parties understood that both corporate objectives were aligned; to achieve a high quality product, within expected costs and enhance reputations.
- BAA faced quite a challenge in encouraging the entire workforce to understand, appreciate and trust the working relationship both between contractors and BAA. They constantly have to reinforce this message to the workforce.

Commercial

- BAA replaced the negative content of traditional, often confrontational contracts (who pays when things go wrong) with a commercial model agreement and commercial policy which creates commercial tension but not a commercial barrier. This was underpinned by BAA's unique insurance policy against risk.
- BAA pays actual prime cost in accordance with the CMA , agrees the overhead cost with the supplier and agree a profit level on top of that. The strategy has four key elements;
    - The client holds all the risk and actively managed by all in the team
    - They will underpin all financial risks so contractors need not worry that they will be held financially accountable when things go wrong.
    - Contractors work to pre-determined fixed profit levels.
    - Contractors are expected to work in partnership.
- BAA has promised as much to the contractors as they have promised to them. This balanced agreement aids relationships and behaviours and uniquely has a focus on being successful together, on managing failure.
- BAA is always looking to reduce waste in their supply chain. They achieve this through using collaborative and competitive market forces to lower costs on components.
- Due to the inherent risks buried in second and third tier contractors, BAA stipulate in the contract with the 1st tier contractors their expectations on how 2nd tier suppliers are engaged. While this has its inherent difficulties BAA feel that as they are carrying the risk they don't want key supplier(s) contracts being let at fixed prices in high risk areas if it presents a deliver risk to T5. BAA has even gone so far as to produce a draft 2nd tier supplier contract template in some instances in an effort to drive the T5 Agreement ethos down the supply chain.

Incentives

- Profit is the key driver of supplier incentives. By taking away the risk, BAA is taking away the key commercial constraint so suppliers can focus on technical delivery.
- BAA creates an incentive fund from targets on all projects. BAA tries to price risks and opportunities and agree a price with suppliers to incentivise active risk/opportunity management without introducing pain. The incentive fund is there to encourage suppliers to better the agreed plan. The fund is there as a means for suppliers to increase their profit provided they perform and to respond to non performance risks.
- Contractor teams share the liability on a project. Targets are set by the team and all share in the success or failure. It is a team target.

Insurance

BAA's approach to insuring against the impact of risks is very innovative and looks to become a template in other construction programmes.

- Its not so much about the cost of the BAA policy but the value it releases. It did not in fact increase the cost of the project as the insurance covers the supply chain on T5.
- In taking out the insurance policy and taking ownership of all the insurable risks, BAA have effectively regulated the project environment itself, breaking the cycle of risk transfer.
- The insurers want other clients to adopt a similar approach, using T5 as a reference site. The insurance market is after all they argue, in the game of risk management and properly managed projects.

Performance Management

Business as usual performance is not acceptable under the T5 Agreement. BAA's expectation is that Best Practice must be achieved. However, BAA's ambition is for Exceptional Performance from the supply chain ie World Class.

- BAA face an ongoing challenge to monitor performance. Ongoing data collection and active risk management go hand in hand to create a conversion to opportunity.
- BAA carry out monthly performance management assessments.
- There are controls and procedures in place to ensure transparency between contractors, sub-contractors and BAA throughout the project.
- They are on time, on budget, quality standards are being met and they have a good safety record.

Summary

BAA realised there was no book on the shelf that addressed how to successfully deliver the scale of programme it contemplated in the late 90's. It took a brace decision to adopt a contract strategy that enabled suppliers to focus on delivery – the T5 Agreement and commercial policy being the enabler. It now represents a serious alternative procurement route for major programmes of work.