DEPARTMENT OF ADMINISTRATION

Contract Price Adjustments

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Introduction

- Name
- Organization
- Role
- Number of Years in Contracting and Procurement

- Current Market Pressures
- Why Negotiating on Price is Important
- Proactive Contracting and Negotiation
- Market Analysis, Price Analysis, Cost Analysis
- Scenario
- Resources

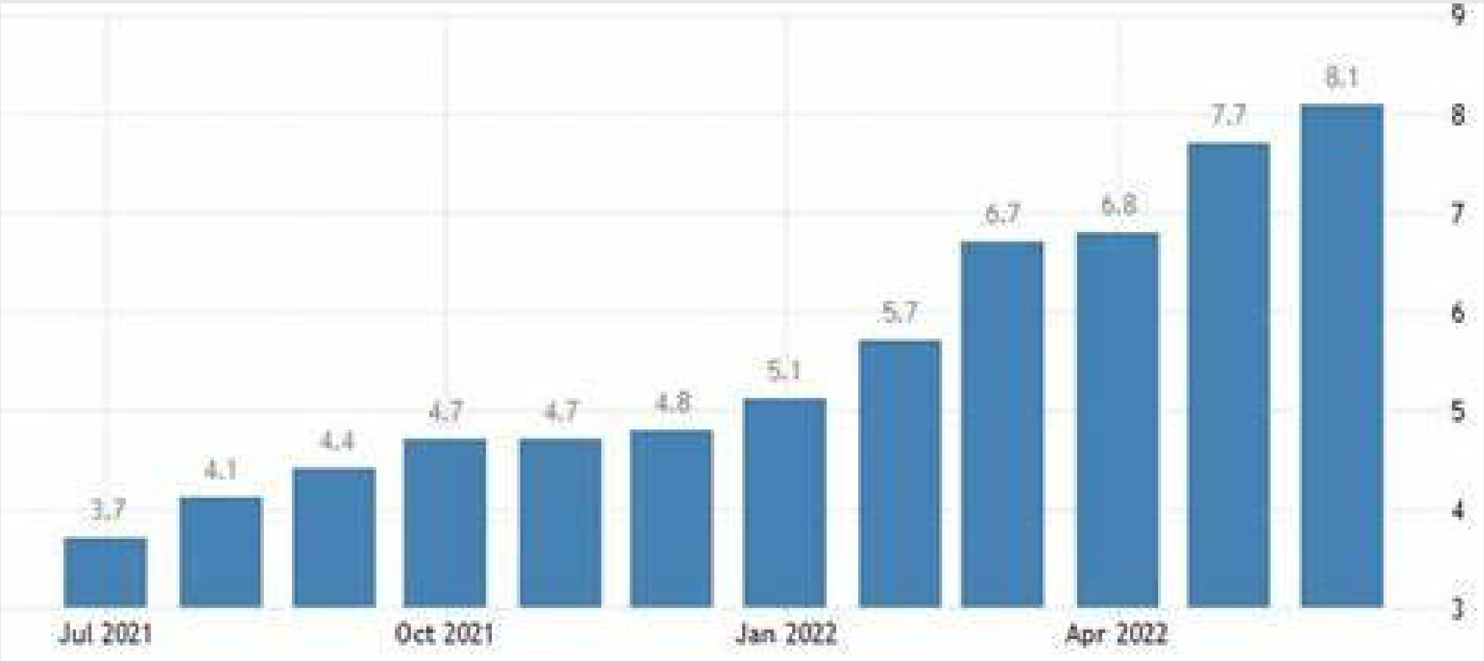
Current Market Pressures

Everything is Getting More Expensive

- Gas Prices
  - July 2021- $3.23
  - June 2022-$5.10
- Raw Materials and Commodities Up
- Rents have increased 6% since last June
- Wages have increased due to labor Shortages

*Bureau of Labor Statistics

Historic Inflation



Why Negotiating on Price is Important

Relevant Statutes

•**16C.02, Minnesota Statutes 2006**

•Subd. 12. **Request for proposal or RFP.** "Request for proposal" or "RFP" means a solicitation in which it is not advantageous to set forth all the actual, detailed requirements at the time of solicitation and <u>responses are subject to negotiation</u>.

•**16C.02, Minnesota Statutes 2007**

•Subd. 12. **Request for proposal or RFP.** "Request for proposal" or "RFP" means a solicitation in which it is not advantageous to set forth all the actual, detailed requirements at the time of solicitation and <u>responses are negotiated to achieve best value for the state</u>.

Why Negotiating on Price is Important

Government procurement officers serve as stewards of the taxpayers’ money.

“Best Value” is the method required by state statute for selecting contractors to perform professional and technical services. (See Minn. Stat. §16C.03, subd. 3)

It is our responsibility to make sure that the money is wisely spent.

We save money we can use for other purposes

We get what we want and need

Why Negotiating on Price is Important

Numerical Summary	Acquisitions	P/T Contracts	MMCAP	Totals
Negotiation resulted in Cost Avoidance (and may have included Better Terms)	34	1	N/A	35
Negotiation did not result in Cost Avoidance (but included Better Terms or other benefit)	15	5	N/A	20
Total of Number of Negotiations	49	17	144 (176 new items)	66

Cost Avoidance Summary	Acquisitions	P/T Contracts	MMCAP	Totals by Line
Cost Avoidance at time of Contract	$2,934,227	$70,003	N/A	$3,004,230
Projected Cost Avoidance	$234,313	$0	N/A	$234,313
Total Cost Avoidance	$3,168,540	$70,003	30.69% (est.)	$3,238,543

Barriers to Negotiation

Not sure what we can negotiate!

If we negotiate with the top-ranked vendor, do we need to offer the same terms to the other responders?

We don't want to ask for anything

We want to be "nice" or offend

We don't want to damage the relationship

Proactive Contracting and Negotiation

What contract mechanisms are your organization using to address price adjustments?

Drafting Contract Terms

Consider:

Incorporating your Solicitation in your Contract

Limiting instances that allow a contract increase

- Implementing a price guarantee period (1 year)
- Tying a price adjustment to an applicable price index (i.e., consumer price index (CPI))

Putting the "Burden of Proof" on the vendor to justify any price increase

- Vendor retains burden to provide "sufficient documentation" supporting the requested increase

Example Contract Terms

"Offeror must guarantee its pricing for 1-year. Following the guarantee period, any request for price adjustment must be for an equal guarantee period, and must be made at least 30 days prior to the effective date."

"A request for price adjustment must include sufficient documentation (market analysis) supporting the request."

"Rates cannot increase more than the Consumer Price Index (CPI) or three percent (3%), whichever is less, year over year (annually)."

Market Analysis

Market Characteristics	Buyer Power Score
Availability of Substitutes	High=Good for buyers, more competition, lower Prices Low=Bad for buyers, less competition, higher prices
Market Share Concentration	High=Bad for buyers, less competition, higher prices Low=Good for buyers, more competition, lower prices
Product Specialization	High=Bad for buyers, leads to higher prices Low=Good for buyers and lower prices
Switching Costs	High=Bad for buyers, locks buyers into one vendor Low=Good for buyers, increases the ability to switch vendors
Recent Demand Driver Volatility	High=Bad for buyers, price fluctuates significantly based on demand Low=Good for buyers, price and demand is stable
Recent Price Volatility	High=Bad for buyers, prices constantly fluctuating Low=Good for buyers, prices are stable
Vendor Financial Risk	High=Bad for buyers, increases buyers' risk Low=Good for buyers, financial risk not a factor in price
Supply Chain Risk	High=Bad for buyers, increases risks Low=Good for buyers, decreases risks

Price Analysis

Compare prices with:

- Previous Year Price
- Current Price
- New proposed price
- Competitor pricing
- Similar commodities / services
- Price Indexes

Cost Analysis

Is the requested increase the right increase?”

Key Price Drivers:

- Labor rates
- Industry regulations
- Raw materials
- Price of fuel / transportation
- Profit margins, Break even
- Applicable Index

Compare vendor’s costs with 3rd party (engineer) estimates, or competitor’s costs, if available.

Example

"Vendor proposes adjusting the price of Road Salt from the current $117.00 per ton delivered to $140.00 per ton delivered beginning January 1, 2023." 20% increase.

"The primary reason for this increase is the substantial increase in the cost of mining and transporting road salt. All other aspects and pricing contained in the existing contract would remain as is."

Market Research

We use market research to answer 2 questions:

- Is a price adjustment warranted?
- Is the proposed price increase the right increase?

Is the price increase warranted?

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Compare prices with:

• Previous Year Price	$113.50 / T. Del.
• Current Price	$117.00 / T. Del
• New proposed price	$140.00 / T. Del.
• Competitor pricing	Comparable
• Similar commodities / services	None
• Price Indexes	9.1% increase

Results

Salt-Cost Per Ton	Delivery	Total
$104.00	$32.00	$136.00

- 16% increase in price
- Cost savings of $1.5 Million

Overview of Best Practices

Best Practices when Vendor Requests Price Increase:

- Contract Terms
  - **Price Guarantee Period**
  - **Vendor Documentation**
  - **Tying Price Adjustment to an Index**
  - **Vendor's Burden of Proof**
- Competitor Pricing
- Market Characteristics (refer to chart)
- Indexes – http://www.bls.gov/data/
- IBIS World – http://www.ibisworld.com/

Thank you again!

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