Executive Summary

FAM100-001: Review of current procurement practice in the Facilities Management sector

This report describes the procurement processes currently followed within the Facility Management sector, and aims to assist in developing a greater understanding of opportunities and challenges in resource efficiency in the FM sector.
WRAP’s vision is a world without waste, where resources are used sustainably.

We work with businesses and individuals to help them reap the benefits of reducing waste, develop sustainable products and use resources in an efficient way.

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Executive summary

WRAP is currently engaging the Facilities Management (FM) sector with a view to developing enabling tools and guidance to facilitate improved resource efficiency within this sector. For the purpose of this project, WRAP has defined FM to incorporate building maintenance and refurbishment, operational waste, carbon/energy/water management, catering, furniture, ICT and textiles. As a key part of this work, it is proposed to build on existing WRAP resources to develop an effective and integrated approach to procuring resource-efficient delivery of FM services. This includes:

- Standards for procurement in the public sector (which could also be used by private sector clients and adopted by FM contractors as service standards);
- Model wording for clauses to include in documents at each stage of the procurement process which implement these standards;
- Common metrics and KPIs for monitoring contractor and sector outcomes over time;
- Practical guidance on implementation, such as templates for minimising and managing the waste of resources such as water and food; and
- Robust cost-benefit evidence for required levels of performance and management methods.

This report describes the procurement processes followed within the Facility Management sector, and will assist in developing a greater understanding of opportunities and challenges in resource efficiency in the FM sector.

FM Market size

Estimates of the size of the UK FM market vary widely. In 2007, a survey identified estimates of the FM market ranging from <£5Bn to >£170Bn. The reasons for this wide range in analyses is largely due to inconsistencies in the definition of the scope of the FM market with some researchers including wider outsourcing activities and management of infrastructure (e.g. utilities and civils) within the scope of FM.

Recent analysis by KPMG and MBD puts the outsourced ‘core FM service’ market at £81Bn in 2010. This includes building maintenance, M&E engineering, environment management, property management, cleaning, catering, security, gardening and landscaping and office services. In-house FM is estimated at a further £38Bn.

Value of FM Services

Whilst the reporting of FM expenditure varies between facility types, the data suggests that:

- Expenditure within the working definition of FM is around 50% of occupancy costs (excluding staff costs) in offices and 40% in schools. Remaining costs include administrative overheads, interest charges, travel and transportation costs, insurances, building rates, etc.
- Repair and maintenance comprises around 5% of occupancy costs in each facility type
- ICT expenditure in offices (22% of occupancy cost) is significantly higher than that in schools (~6%) however the proportion of office ICT expenditure on hardware is significantly lower at around 8% of occupancy costs
- Cleaning costs are around 2-3% of occupancy costs in schools and offices but significantly higher (~10% in healthcare). Waste disposal costs are typically less than 1% of occupancy costs in schools and below 0.5% in offices.

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1 For a complete working definition of FM used in this project please refer to Error! Reference source not found. on Page 24
2 Presentation to Workplace Futures Conference in February 2011.
4 Facilities management (FM) is the integration of processes within an organisation to maintain and develop the agreed services which support and improve the effectiveness of its primary activities
- Energy costs are 3-5% of occupancy costs for offices and schools, water and sewerage costs are less than 1%. No specific cost codes / or recorded expenditure for energy / carbon or water management were identified.
- Catering costs are 3-5% of occupancy costs for offices and schools but higher for healthcare (~9%)
- Overall expenditure on FM related services is significantly higher for offices as a class (£107Bn) than for hospitals (~£6.6Bn) or schools (~£12Bn).

**FM Service Delivery Models**

FM services can be delivered under a variety of commercial arrangements. Recent trends are for the increased acceptance of financial risk by the FM supplier through the use of target cost or guaranteed maximum price models. Some of the key approaches together with their commercial implications and impact on resource efficiency objectives are described in Table 1.

**Table 1: Overview of different commercial models used in FM contracts**

<table>
<thead>
<tr>
<th>Model</th>
<th>Description</th>
<th>Commercial implications</th>
<th>Impact on resource efficiency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost plus</td>
<td>Client pays for direct and overhead costs plus a prearranged profit margin</td>
<td>Typically used where it is difficult to tightly define the scope of work or outcomes desired. No incentive for the contractor to offer efficiencies.</td>
<td>Not well suited to obtaining proactive cost / resource reductions on behalf of the contractor as this would reduce their income. However, there is greater flexibility for the client to change scope of what is required at short notice i.e. to mandate the use of a more efficient process / product.</td>
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<tr>
<td>Target cost</td>
<td>A development of the cost plus approach to set a target cost for all activities within a specified scope of work or timescale. If the cost is greater or less than the target cost then the pain or gain is shared between client and contractor</td>
<td>Incentive in place for the contractor to work more efficiently as they can achieve additional profits if the work is below the target cost. Target cost might need to be revised frequently as the service evolves over the course of the contract. Target cost will need to be supported by clear performance standards / KPI’s to ensure that efforts to reduce cost do not compromise performance. Acceptance of gains at the end of the specified period is normally contingent on using the achieved efficiencies to set a new target cost for the subsequent period.</td>
<td>Incentive to reduce costs and resource use. If coupled with incentives around performance these measures can reduce client costs as the contractor is seeking ways to improve efficiency in order to achieve gain share or performance incentives.</td>
</tr>
<tr>
<td>Guaranteed maximum price</td>
<td>A maximum price is agreed with a defined profit margin. The contract claims all costs incurred and a fixed management fee (includes overheads and profit)</td>
<td>Client gets cost certainty and can encourage efficiencies / performance through a process of shared savings and performance penalties / incentives.</td>
<td>Similar to a target cost approach. Success in achieving efficiencies is linked to the design of the pain / gain and performance based payments mechanism.</td>
</tr>
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<tr>
<td>Fixed price</td>
<td>Client pays a fixed price for a defined scope of work</td>
<td>Contractors profit is fixed irrespective of volume; however they hold the risk of cost overruns.</td>
<td>Contractor profits increase if they can cut their costs therefore resource efficiency is encouraged. Less incentive for the contractor to offer alternative delivery options as these might result in negotiation of a new (lower) fixed price.</td>
</tr>
<tr>
<td>Partial or nil subsidy</td>
<td>Client provides space facilities and (typically) power for a contractor to undertake a commercial service (typically catering). They may also subsidise the cost of the service (partial subsidy) but will frequently seek to avoid any subsidy of costs (nil subsidy).</td>
<td>Client achieves the service with some or no subsidy (although they are receiving no payment for space, equipment and power). Service users pay a higher price than might otherwise be the case with a subsidised service. Contractor takes on a large portion of profitability risk on their expectation of sales. Effectiveness is dependent on scale and market conditions (e.g. presence of local competition).</td>
<td>These contracts incentivise the operator to act in the most economically efficient manner i.e. to maximise sales. This should increase service standards but may also result in higher levels of wastage as oversupply of relatively low cost items (e.g. food) is used to increase turnover and better defray fixed costs (staff and overheads).</td>
</tr>
</tbody>
</table>

A key element of successfully delivering each of the above models is that effective communications between the contractor and the client are maintained and that the contractor is required to provide proactive suggestions as to efficiencies. This is potentially less effective in a fixed price contract as this might result in agreement of a new price that is less favourable to the contractor.

**Market trends**

Recent trends in the FM sector include:

- Falling margins amongst major suppliers – analysis of 2005-07 and 2007-09 turnover and margins suggests that turnover and profitability is down among major suppliers.¹
- Increased move towards multi-service and TFM contracting.²
- Consolidation of procurement across organisations (e.g. blue chips looking for single providers within a global region) and between public sector organisations
- Strong focus on cost cutting from clients – this includes reducing service provision, procurement efficiencies and use of alternative delivery options
- Use of two tier contract structures whereby there is a framework / strategic agreement supported by more specific agreements for individual facilities / classes of asset
- Transfer of risk to the supplier – whereby the supplier is responsible for delivering the required service levels within a target cost or guaranteed maximum price and therefore takes the associated risk (and benefits). The

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¹ Presentation to Workplace Futures Conference in February 2011.
catering service sector has shown a 75% increase in profit and loss based contracts, over previously used cost plus contracts, in the last 10 years. This also includes an increase in nil subsidy contracts where margins on turnover are sufficient to support the fixed costs of providing the service\(^2\).

- Use of financial incentives for good performance or penalties for failing to meet targets\(^8\)
- Use of shared savings models—some examples of these were identified although they are not routine

It is also worth noting that ICT is not generally considered an FM cost, and that textiles / furniture are not typically grouped within occupancy costs within major Public Sector property cost analyses (Refer Section 2.2). This differentiation between services considered in the scope of this study is borne out by interviews and survey responses. The further development of model procurement requirements for these service areas will need to be flexible enough to use primarily within standalone procurement routes, occasionally bundled with other services.

**FM Procurement**

The FM procurement process is described in some detail within this report, based on the outline described in the diagram below:

<table>
<thead>
<tr>
<th>Service Strategy</th>
<th>Delivery Strategy</th>
<th>Procurement Strategy</th>
<th>Monitoring Strategy</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Scoping and specifying service requirements</td>
<td>• Delivery models</td>
<td>• Project boundaries</td>
<td>• Key Performance Indicators</td>
</tr>
<tr>
<td>• Service levels</td>
<td>• Bundling of services</td>
<td>• Managing risk</td>
<td>• Reporting</td>
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<td></td>
<td></td>
<td>• Contract duration</td>
<td>• Financial controls</td>
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<tr>
<td></td>
<td></td>
<td>• Procurement route and contracting framework</td>
<td></td>
</tr>
</tbody>
</table>

The scoping and specifying of service stage within the procurement of FM services is vitally important in the identification of opportunities for resource efficiency. This stage in the FM process is similar to the ‘design stage’ in the building design and construction process, in that this stage represents the point at which key decisions are made which will influence the ability of the service to be tailored and managed for resource efficiency.

The separated procurement routes for IT, branded items (in many organisations), catering (in many organisations) and mainstream hard / soft FM is an important issue that should inform WRAP’s approach. Materials aimed at an FM audience may not appear relevant to a Chief Information Officer or Marketing Director.

\(^2\) How to run a nil subsidy contract. Caroline Fry, November 2010. Caterer and hotelkeeper.

\(^8\) This approach works best for services where the FM supplier is well placed to manage these risks. With respect to energy, for example, there are instances where the supplier is able to demonstrate ‘inappropriate’ behaviour on the part of building occupants (e.g. leaving lights or equipment on) and thereby avoid penalty clauses in contracts.
and the grouping of these services under an FM heading may make communication more difficult. Furthermore the nature of the FM role is such that it is less likely that FM practitioners, even if given information and training would seek to challenge an organisation’s IT or branding strategy. Therefore if WRAP wishes to influence the strategic approach to these issues (which ultimately underpins the procurement requirements) it will need to target other individuals outside the FM department.

Approaches to addressing this issue could include:

- **Terminology** - i.e. using a broader definition such as ‘resource efficiency in operations’
- **Producing separate materials for different audiences** – particularly in the private sector it would be beneficial to separate some of the key services into separate information packs; these would include IT, uniforms, furniture and catering. These services might still be included within FM related materials but would be available as standalone information
- **Structuring information** into ‘strategic service delivery’ information and ‘procurement implementation’ information. In some senses this is akin to the distinction between Designing out Waste and Site Waste Management in that the second cannot proceed effectively without the first. As with construction the individuals involved at the ‘design’ stage for many services will be different to those involved in procurement
- **Providing robust information on the impact on core services** – in addition to demonstrating a cost benefit case, it will be key for information on more resource efficient approaches to FM and other services to show that they in no way undermine the core service. The analysis in Section Error! Reference source not found. shows that expenditure on many of the FM services considered in this study is relatively small in the context of overall business costs and that even small impacts on core service would significantly outweigh other costs or benefits of an initiative.

A key element of successfully implementing and managing FM services is that effective communications between the contractor and the client are maintained, and that the contractor is encouraged to provide proactive suggestions as to efficiencies.

Effective ‘pain / gain’ and ‘shared savings’ clauses may be included within the payment mechanisms for FM contracts tying payments to outcomes achieved. In both cases, it is important that the client should be able to effectively pass responsibility for achieving the performance measures on to the contractor. In some cases where there are multiple parties involved in achieving a performance standard it is more difficult to enforce any penalties for failing to meet performance targets (e.g. Energy consumption).

The FM market is diverse and fragmented. This can make it difficult to target resource efficiency opportunities during procurement. By understanding a few key elements of how both the private and public FM market procure their FM services would enable WRAP to prioritise their approach. These elements are listed below:

- **Property Portfolio FM Contracts** – The largest proportion of property landlords have multi-site portfolios. Commercial and retail landlords and large national companies will often let their FM contracts nationally to get the best value for money.
- **Official Journal of the European Union (OJEU) Advertised FM Contracts** – A potential FM contract for public sector FM clients would be advertised on the OJEU and it is unlikely that at this stage the full details of the contract would be defined. WRAP could approach the Contracting Authorities who are advertising their FM contract for consideration of integrating resource efficiency targets.
- **Procurement Buying Clubs** – An increasing volume of public sector FM contracts are going through Procurement Buying Clubs. These organisations have standard terms and conditions that could include resource efficiency targets.
- **Timing of Intervention** – As FM contracts tend to have a long duration it is important to identify when a contract renewal process is expected to happen. It is far more difficult to intervene and promote resource efficiency in FM contracts after contracts have been let unless the supplier is open to recognising the benefits
of incorporating resource efficiency in their FM services. Collaborative working has also been successfully employed to vary contract conditions in existing contracts;

- **Statement of Need / Procurement Strategy** – The earlier that resource efficiency can be identified as a facet of the FM contract the better the chance of incorporation into the working methods.

- **Contract Terms** – FM suppliers will have some form of formal contract agreement but there is not widespread use of standard forms as there are in the construction industry. Promoting resource efficiency through contractual obligations may be better instigated through consultation with procurement lawyers and mainstream FM suppliers for incorporation in their bespoke agreements.

- **Performance Monitoring Software** – There is an increased trend to use performance monitoring software to manage FM contract performance and ensure performance levels are as agreed in Service Level Agreements. Adapting resource efficiency targets so that they are in a format that suits the performance monitoring software systems would enhance the adoption of WRAP targets.

Feedback from interviews with clients and service providers confirms that sustainability and resource efficiency (RE) issues are important, within the context of cost effectiveness / pay-back and availability of sufficient knowledge or experience within the procurement team, operational management and service provider organisations. Larger FM Service Providers, report a high degree of internal knowledge and experience in RE, driven from Board level management of their organisation and service delivery.

The majority of Service Provider respondents answered that sustainability and resource efficiency within their services are tested at pre-qualification stage (sometimes at tender stage) and generally embedded into performance monitoring for Total FM, hard services and catering services.

Our report explores the supply chain structures within a selected group of FM services, indicating current practice in procurement and management. We also explore corporate environmental management systems within FM service providers and clients. In our team’s experience, ISO14001 is the most widely accepted and recognised environmental standard in the sector. Many organisations obtain it as part of their marketing and business development strategies, rather than as part of their core operational business programme. i.e.: They use it to win business not to change the operations of their organisation to improve their environmental performance.

The majority of Service Provider respondents described their organisations as having an ISO14000 EMS in place across their whole organisation, some applying this to certain sites only. EMAS and BS8555 are not widely used by respondent organisations. However, these systems often do not consider the full impacts of procurement and therefore may fail to address significant product life-cycle or supply chain impacts. An exception to this, which perhaps proves the rule, is the London Fire Brigade, where the scope of their ISO14001 certification includes the procurement function.

When asked about barriers to implementing resource efficiency in their FM service contracts, clients and service providers described the following barriers:

- **Availability of funding** for investment where this is required to improve efficiency;
- **Inflexible budget constraints** – limits the procurement of capital equipment on lease, since capital may be available but not operational funding;
- **Evidence of opportunities** including business case examples and case studies;
- **Resistance to change** underpinned by a perception that sustainability requires more work to implement;
- **Lack of client driven incentives** to implement resource efficiency in service contracts – needs to be incorporated early on in the procurement of these services;
- **Lack of control** over the use of resources within the facility by the client / facility users.

**Industry challenges and opportunities**

Challenges and opportunities identified in this report, for different client segments, include:

- Growth amongst financial, IT and support services client groups
- Reduced expenditure and uncertainty in the healthcare sector
Significant cost pressures in education balanced by opportunities for contracts with academies / free schools

Significant cost pressures in other private sector client segments (e.g., utilities, primary industry, manufacturing, entertainment and real estate)

Opportunities in public sector through shared procurement of local services and a move to increased outsourcing to reduce costs.

Across each key market segment there is a drive towards greater outsourcing, consolidation of procurement and cost savings. In Central Government, and major corporations, measurable ‘sustainability’ performance is a driver but for all groups cost savings are paramount. Accessing different segments will vary and outside central government there is no easy way to influence a whole segment via one organisation.

Key opportunities for accessing larger quantities of FM Client spend include:

- Government departments and agencies – ideally working through the Government Property Unit (GPU) in England, Scottish Procurement Directorate and buy4wales, the Welsh Government’s procurement portal.
- Local authority collaborative purchasing hubs
- Major NHS trusts or collaborative procurement initiatives
- Major owner occupiers and large corporations with extensive property portfolios and high Corporate Social Responsibility (CSR) drivers (e.g., banks, major consultancies, infrastructure / transport companies)
- Partnership for Schools (PFS) output specifications
- Academy chains and super chains

Key opportunities to access FM Service Providers include:

- Engagement with PFI investors presents a good opportunity to impact on FM activities in major contracts. PFI investors may be affiliated with major PFI contractors but are often separate from the construction part of the business and engagement would need to be separate from any involvement with the contracting arm.
- There are relatively few large FM providers and these organisations will be the key providers of the increasing number of multi-service / TFM contracts. In 2007, the turnover of the 50 largest FM companies was in the region of £17Bn. Using the KPMG / MBD estimates, the largest UK suppliers represent around 20% of outsourced activity in the sector and around 15% of total FM expenditure.
- Other providers are likely to subcontract to a TFM provider for larger projects or will work on smaller less integrated contracts. Outside the multi-service / TFM sector separate large providers of IT and catering are more likely to contract direct to the client rather than via TFM.

Further research

Research conducted during this project indicates that ICT, Furniture and textiles tend not to be regularly procured within the context of bundled services. In most cases the procurement of these services tends to be carried out from within the Core Business Operation, rather than the Facility Operation. As a result, we believe that these service areas require further investigation, from the perspective of procurement by business process rather than FM, but bearing in mind that there are definite impacts on FM and FM service provider activities resulting from IT, furniture and textiles.

The focus of this research centred mainly on commercial and institutional facilities. Specialised FM operations do, however, occur within the Hospitality and Leisure sectors. These operations tend to be firmly integrated within the operational management of the facility with respect to service procurement and management. Many of the service areas considered to be non-core business in the commercial and institutional sectors are, in fact, core to the hospitality and leisure facility. For example, guest catering is often deeply embedded into the branding of the leisure operator. This broad sector should be considered for further investigation, with a view to developing industry specific resource efficiency guidance and good practice advice.

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