PROJECT MANAGEMENT

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PMP® Certification Training

Lesson 13: Project Procurement Management

This course is based on the Project Management Institute, *A Guide to the Project Management of Body of Knowledge (PMBOK® Guide)* – Sixth Edition.
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Objectives

- Define contract
- Differentiate between centralized and decentralized contracting
- Explain the different types of contract
- Identify the key terms used in Procurement Management
- Describe the Project Procurement Management processes

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Contracts

The definition of a *Contract is as follows:

A contract represents a mutually binding agreement that obligates the seller to provide the specified products, services, or results and obligates the buyer to provide the monetary or other valuable consideration in return. A contract can also be called an agreement, understanding, undertaking, or a purchase order.

The two parties involved in a contract are the buyer and the seller. A seller provides the goods and services and the buyer buys these for a compensation.

*Definition taken from the Glossary of the Project Management Institute, *A Guide to the Project Management Body of Knowledge, (PMBOK® Guide)* – Sixth Edition, Project Management Institute, Inc., 2017, Page 489

Characteristics of Contract

The characteristics of a contract are as follows:

- A contract must be formal and in written form.
- A contract must have legal remedies.
- Changes to contracts must also be subject to the same checks as the contract itself.
- A contract is created and managed by contract managers, also called the procurement managers.

Centralized vs. Decentralized Contracting

In centralized contracting, a single contract manager handles multiple projects, whereas in decentralized contracting, a contract manager is assigned to a project full time and reports to the project manager.

The advantages and disadvantages of the two methods are as follows:

Method	**Advantages**	**Disadvantages**
Centralized Contracting	• Increased expertise in contracting • Standardized company practices	• Difficult to get contracting help as the contractors may be involved in multiple projects
Decentralized Contracting	• More focus and control on the project • Easier access to contracting experience	• Duplication of expertise • Less standardization of contracting practices from one project to another

If British Petroleum is starting a project of setting up a new refinery plant in Nigeria, they can procure key machinery through centralized purchasing department and later have a full-time contract manager to procure smaller equipment, locally.

Types of Contract

Contracts can be of three types. They are as follows:

Cost Reimbursable (CR) or Cost Plus

The seller is paid based on the actuals. Cost plus, say, incentive or fixed fee will be paid in addition to the actuals.

Cost-based contracts can be classified as:

- Cost Plus Fee (CPF) or Cost Plus Fixed Fee (CPFF)
- Cost Plus Percentage of Costs (CPPC)
- Cost Plus Incentive Fee (CPIF)
- Cost Plus Award Fee (CPAF)

Time and Material (T and M) or Unit Price

Time and material (T and M) or unit price contracts are generally used for smaller projects, wherein customer pays per item, hour, or day.

Fixed Price (FP) or Lump Sum

Fixed price contracts (or lump sum contracts) are generally signed when the scope of work is very clear.

Fixed price contracts can be classified as:

- Fixed Price Incentive Fee (FPIF)
- Fixed Price – Economic Price Adjusted (FP – EPA)
- Firm Fixed Price (FFP)

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Business Scenario: Problem Statement

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- Scott is the Project Manager for a global project, which is very demanding and critical to his company. His Project Sponsor is confident in his team's ability to finish the project under budget and ahead of schedule.
- To manage the huge demand, Scott has to make a decision to procure additional resources.
- The additional resources would be responsible for activities requiring specific skills, which his project team lacks.
- The customer has an incentive clause in the project's agreement that yields a bonus for early completion. Scott has a vision for the work the additional resources will complete, but there is also an opportunity to expand their scope of work, especially if he runs into scheduling problems that will require him to crash the critical path.
- What contract should Scott establish to procure the additional resources?

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Business Scenario: Solution

- Although Scott wants to complete his project early so that the team can receive the bonus for early completion, he has to pick a contract that is less risky and based on the scope of work.
- Out of the available contracts, the best choice for Scott is the Time and Material Contract, which gives him more flexibility.
- Fixed Fee contracts require a well-defined scope of work, and Time and Material is the only option that accommodates open-ended work arrangements.

Types of Contract: Advantages and Disadvantages

The advantages and disadvantages of different types of contracts are as follows:

Type of Contract	Advantages	Disadvantages
Cost Reimbursement	• Less costly than fixed price because seller does not have to account for the risk • Simple to draft	• Requires auditing all the seller invoices and thus increases buyer efforts • Seller has less incentive to control cost and thus these contracts are inefficient, i.e., riskier for the buyer or the project manager
Fixed Price	• More efficient as the seller has strong incentive to control cost • Requires less effort by buyer to manage contracts as cost risk is with the seller	• Seller may underquote initially and later try to make high margins on change requests • Not having a proper Statement of Work (SOW) can result in seller not providing some of the deliverables
Time and Material	• Easy to create • Good for resource augmentation assignments, where cost risk is shared by buyer and seller	• Seller has no incentive to control costs • Requires monitoring of daily output • Can't be used in big projects

Key Terms

The following are the key terms used in Procurement Management:

Request for Information

Request for Information (RFI) is used to get potential sellers' information to see their capability.

Request for Proposal

Request for Proposal (RFP) is used to get proposals from prospective sellers.

Request for Quotation

Request for Quotation (RFQ) is used to get quotation from prospective sellers for standard products or services.

Request for Bid

Request for Bid (RFB) is used by the buyer to get bids from the shortlisted sellers.

Purchase Order

Purchase Order (PO) is the simplest type of commercial contract. PO is generally issued for small purchases.

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Key Terms (Contd.)

Statement of Work

Statement of Work (SOW) defines the scope of the deliverables according to the contract.

Quotation

A Quotation is the submission of response by the vendor to a request from the buyer.

Non-disclosure Agreement

Non-disclosure Agreement (NDA) is signed between two parties to maintain the confidentiality of the information of each other. They abide by the agreement and don't disclose the information with any of the competitors.

Letter of Intent

Letter of Intent (LOI) is issued by the buyer to indicate that he is interested to carry on work with the seller.

Terms and Conditions

A procurement agreement includes certain Terms and Conditions (T and C) and may incorporate other items that the buyer specifies regarding what the seller should perform or provide.

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Key Terms (Contd.)

Force majeure

It is a clause in contracts that frees both business parties from obligation in case of unavoidable events or an event described by the legal term as act of God (flood, hurricane, earthquake, and so on).

Doctrine of waiver

Doctrine of waiver is a voluntary act by a person or a party that surrenders a legal right.

Privity of contracts

The doctrine of Privity implies that the contract cannot confer rights or obligations to any party other than those directly involved in the contract.

Dispute resolution

It is about taking action or finding a resolution in case of disputes..

Termination for convenience of buyer

This involves termination of the contract by the buyer under any circumstances.

Project Procurement Management

The definition of *Project Procurement Management is as follows:

Project procurement management includes the processes necessary to purchase or acquire products, services, or results needed from outside the project team.

Project Procurement Management helps in determining the type of contract to be issued and guides in managing the contracts with the sellers.

*Definition taken from the Glossary of the Project Management Institute, *A Guide to the Project Management Body of Knowledge, (PMBOK® Guide)* – Sixth Edition, Project Management Institute, Inc., 2017, Page 459

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Project Procurement Management Processes

Knowledge Areas		Project Integration Management	Project Scope Management	Project Schedule Management	Project Cost Management	Project Quality Management	Project Resource Management	Project Communications Management	Project Risk Management	Project Procurement Management	Project Stakeholder Management
Project Management Process Groups	Initiating	4.1 Develop Project Charter									13.1 Identify Stakeholders
	Planning	4.2 Develop Project Management Plan	5.1 Plan Scope 5.2 Collect Requirements 5.3 Define Scope 5.4 Create WBS	6.1 Plan Schedule Management 6.2 Define Activities 6.3 Sequence Activities 6.4 Estimate Activity Durations 6.5 Develop Schedule	7.1 Plan Cost Management 7.2 Estimate Costs 7.3 Determine Budget	8.1 Plan Quality Management	9.1 Plan Resource Management 9.2 Estimate Activity Resources	10.1 Plan Communications Management	11.1 Plan Risk Management 11.2 Identify Risks 11.3 Perform Qualitative Risk Analysis 11.4 Perform Quantitative Risk Analysis 11.5 Plan Risk Response	12.1 Plan Procurement Management	13.2 Plan Stakeholder Engagement
	Executing	4.3 Direct and Manage Project Work 4.4 Manage Project Knowledge				8.2 Manage Quality	9.3 Acquire Resources 9.4 Develop Team 9.5 Manage Team	10.2 Manage Communications	11.6 Implement Risk Response	12.2 Conduct Procurements	13.3 Manage Stakeholder Engagement
	Monitoring and Controlling	4.5 Monitor and Control Project Work 4.6 Perform Integrated Change Control	5.5 Validate Scope 5.6 Control Scope	6.6 Control Schedule	7.4 Control Costs	8.3 Control Quality	9.6 Control Resource	10.3 Monitor Communications	11.7 Monitor Risks	12.3 Control Procurements	13.4 Monitor Stakeholder Engagements
	Closing	4.7 Close Project or Phase									

Table 1-4. Project Management Process Group and Knowledge Area Mapping

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Plan Procurement Management

"Plan Procurement Management is the process of documenting project procurement decisions, specifying the procurement approach, and identifying potential sellers." It belongs to the Planning Process Group.

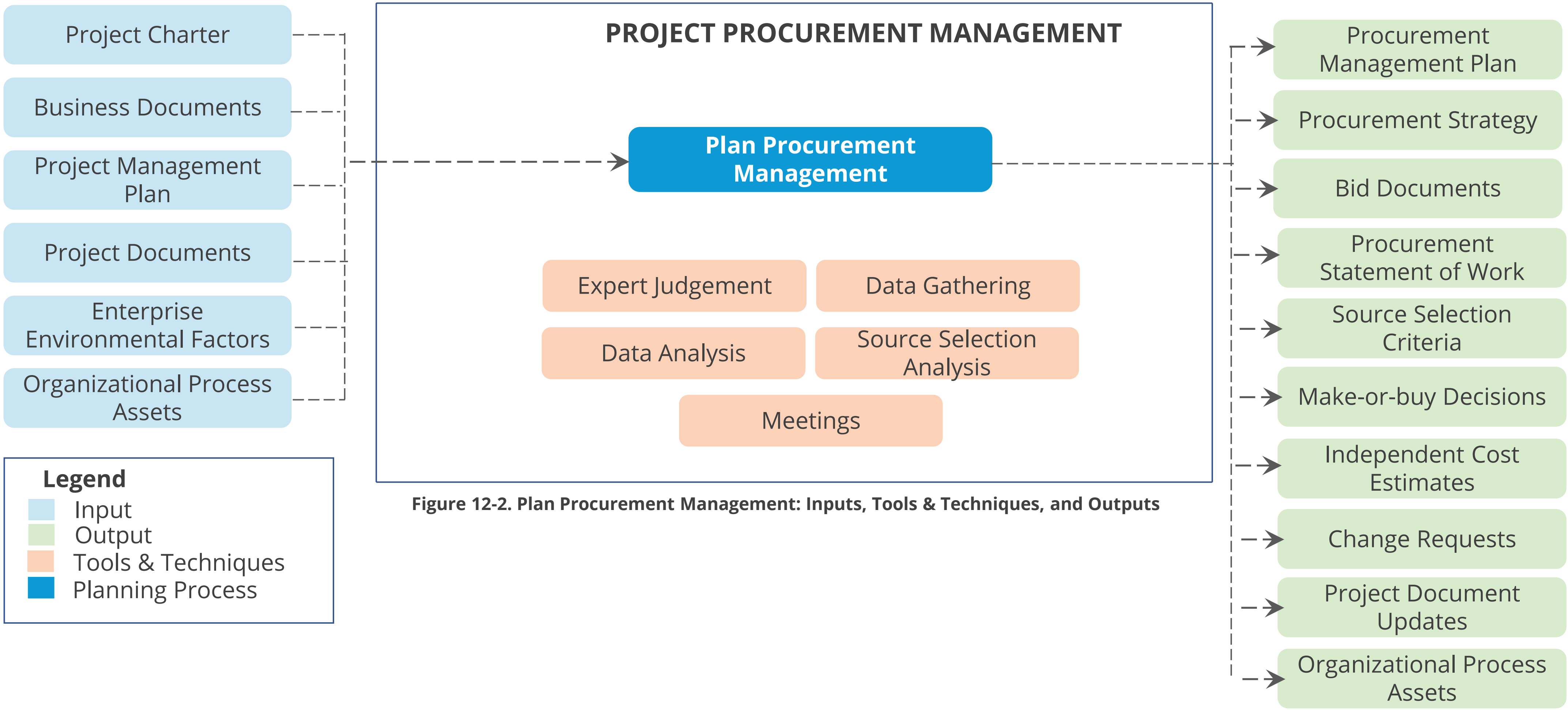

Figure 12-2. Plan Procurement Management: Inputs, Tools & Techniques, and Outputs

Project Management Institute, *A Guide to the Project Management Body of Knowledge, (PMBOK® Guide)* – Sixth Edition, Project Management Institute, Inc., 2017, Page 466

Conduct Procurements

"Conduct procurements is the process of obtaining seller responses, selecting a seller, and awarding a contract." It belongs to the executing process group.

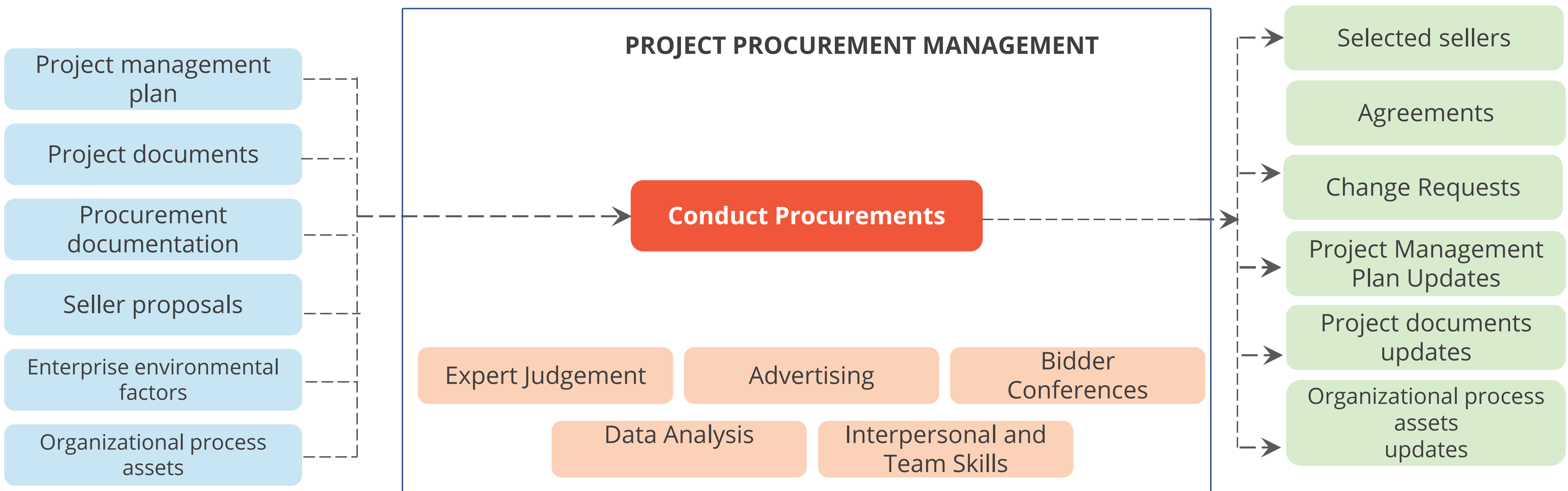

Figure 12-4. Conduct Procurements: Inputs, Tools & Techniques, and Outputs

Legend
- Input
- Output
- Tools & Techniques
- Executing Process

Bidder Conferences

Bidder conferences are scheduled reviews for interested suppliers to ask questions and receive information on a Request for Proposal, Quotation, or Information. They ensure that all bidders receive the same information at the same time

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Control Procurements

"Control Procurements is the process of managing procurement relationships, monitoring contract performance, and making changes and corrections to contracts as appropriate."[3] It belongs to the Monitoring and Controlling Process Group.

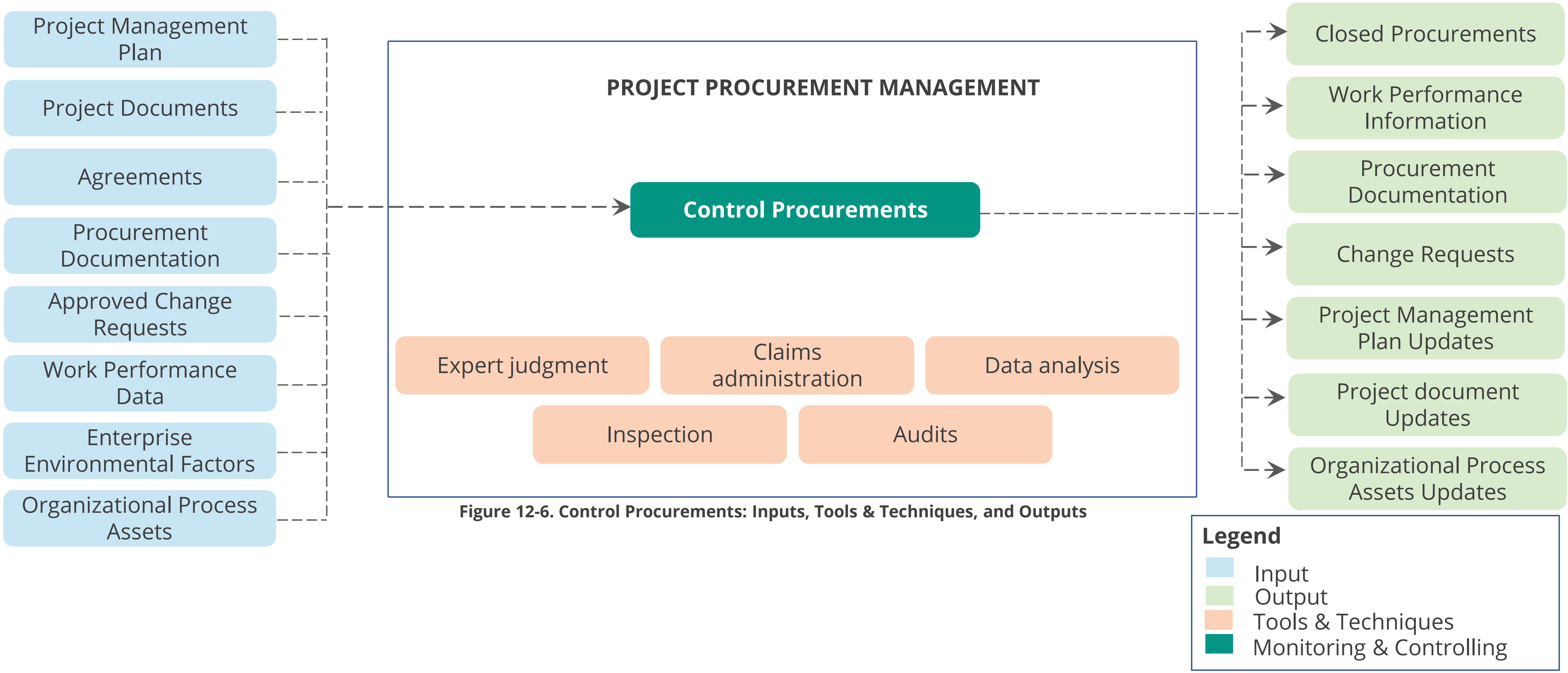

Figure 12-6. Control Procurements: Inputs, Tools & Techniques, and Outputs

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