



TOO MUCH OF A GOOD THING – REQUIREMENTS AS COST DRIVERS ON THE NORWEGIAN CONTINENTAL SHELF

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By Sveinung Fjose, partner and managing director
in Menon

Svensk polis-Passat: 490.000 kr. Norsk politi-Passat: 883.000 kr.

HENNING CARR EKROLL

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Norwegian police pay up to NOK 400 000 more for their police cars than the Swedes do – for almost exactly the same model. Requirements specific to Norway make the cars very expensive, chief of police says.

Byråkrati og kunnskapsmangel koster milliarder

CARL ALFRED DAHL

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The Norwegian public sector wastes more than NOK 30 billion in tax money when procuring goods and services.

WITH THE HELP OF GOOD PROCUREMENT, THE OIL COMPANIES HAVE LAID
THE BASE FOR ENORMOUS WEALTH CREATION



- **Summary**
- Specific and overlapping requirements result in higher costs
- Overlapping and inappropriate requirements do not improve safety
- The requirement process does not contribute to safety-critical learning
- The requirement process helps to strangle innovation

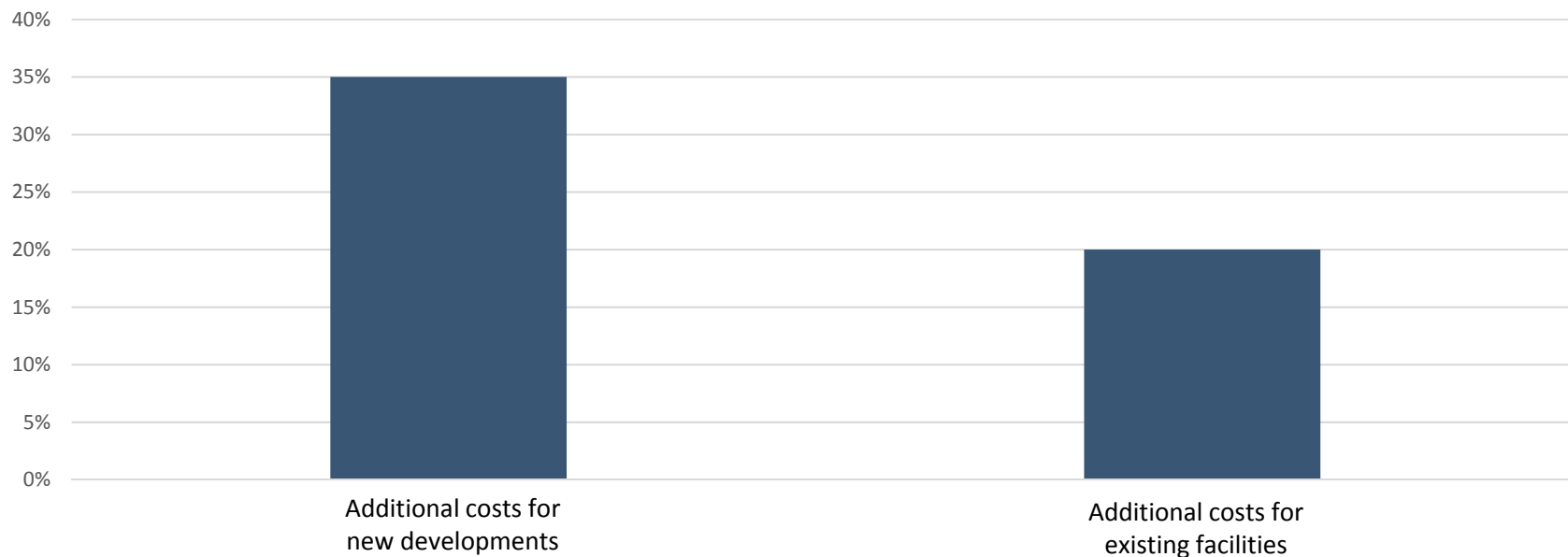
- Oil companies on the Norwegian continental shelf pay on average between 20 and 30 percent more than other companies for identical products.
- A significant part of this cost difference can be explained by requirements for specification and reporting.
- Costs for administration and documentation for deliveries to oil companies are several hundred percent higher than for deliveries to other companies in the industry.
- If it is true that costs for deliveries to oil companies are between 20 to 30 percent higher across the board, this means additional costs of more than NOK 50 billion on the Norwegian continental shelf in 2016.
- Specification and reporting requirements do not necessarily improve safety:
 - Irrelevant and contradictory specifications weaken safety
 - Reporting leads to «information overload»
 - Procurement routines impede safety-critical learning
- Menon's full report [in Norwegian] can be downloaded here:
<http://www.menon.no/wp-content/uploads/2016-39-Krav-som-kostnadsdriver-i-norsk-petroleumsn%C3%A6ring.pdf>

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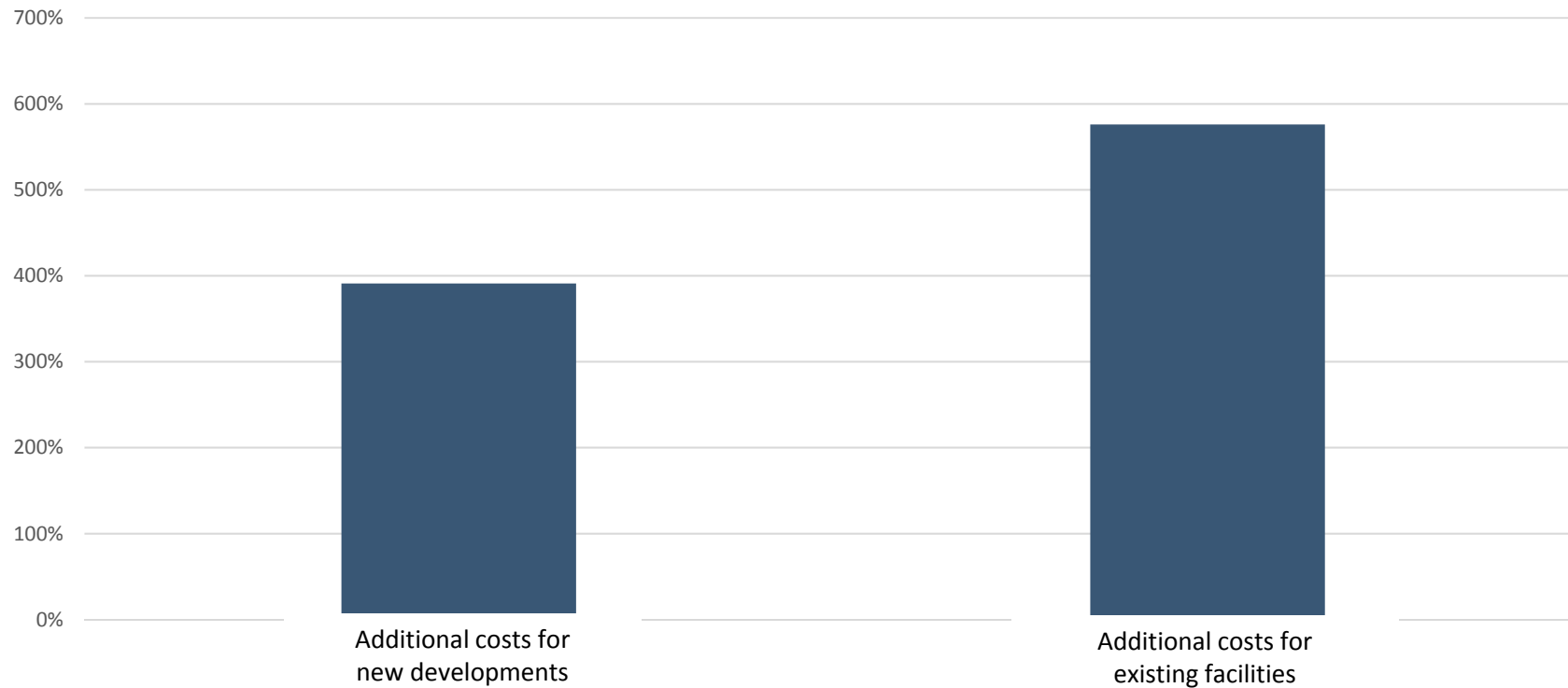
ADDITIONAL COSTS RESULTING FROM REQUIREMENTS

- In order to isolate the effect resulting from requirements, we went into the accounting systems of suppliers selling products to oil companies and other parts of the industry
- We have only compared identical products

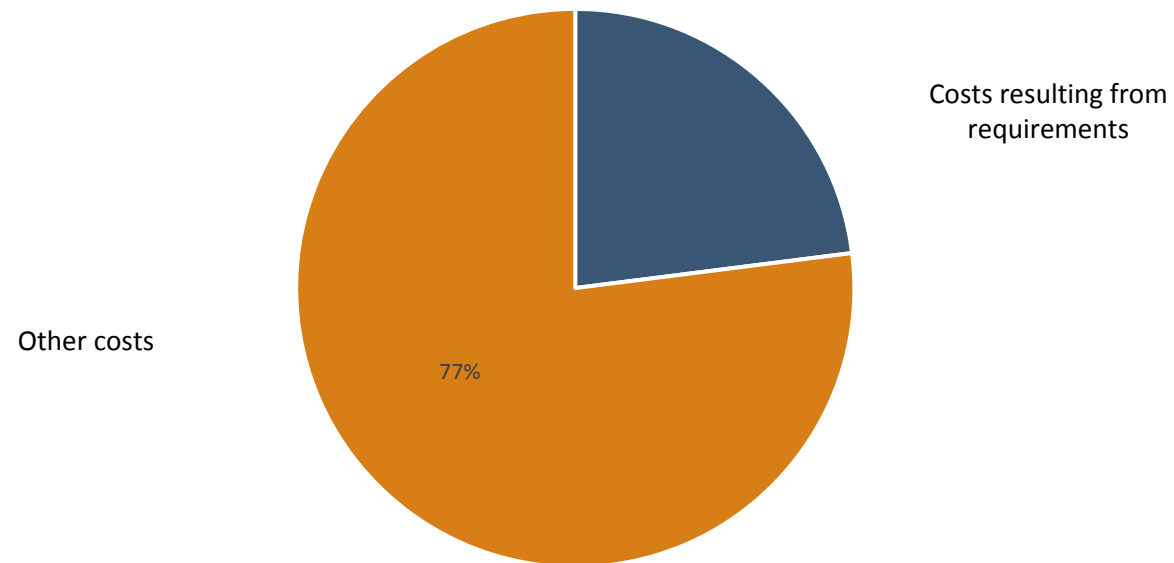
Additional costs for oil companies when buying identical products



Additional administration costs for deliveries to oil companies

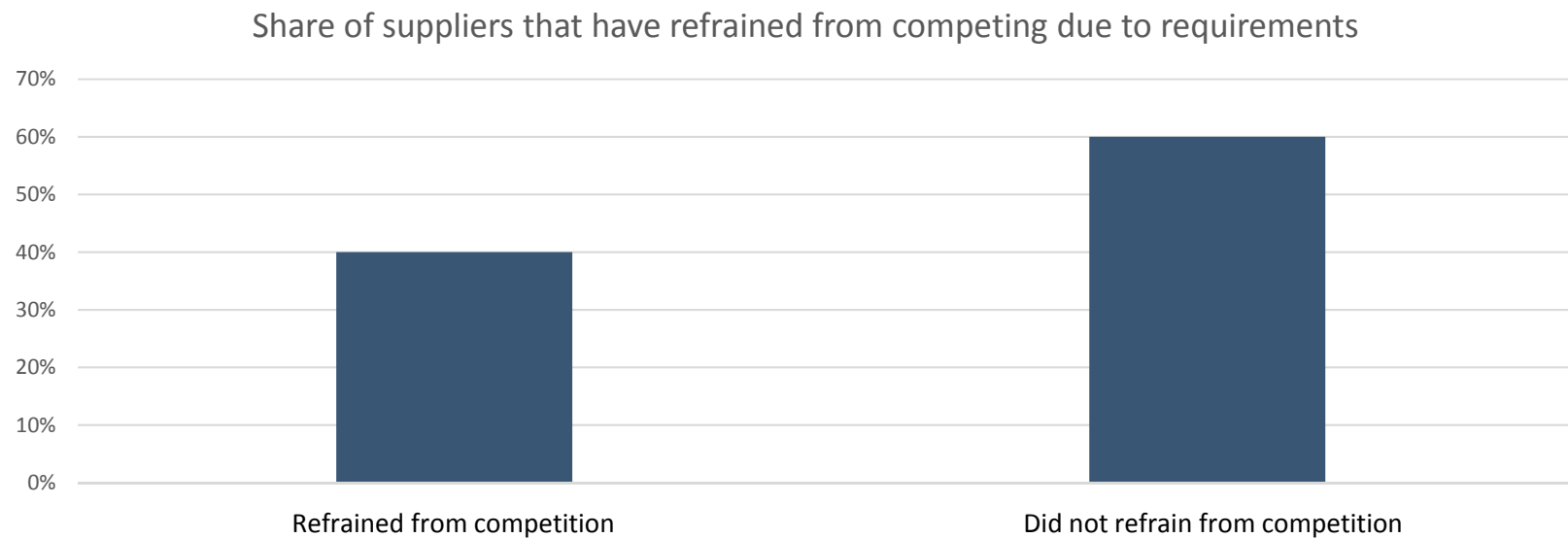


Average estimate of additional costs to suppliers resulting from requirements



SHARE OF SUPPLIERS THAT HAVE REFRAINED FROM COMPETING DUE TO THE AMOUNT OF REQUIREMENTS

- If suppliers refrain from participating in competitions, competition is reduced
- The consequence is higher cost and lower quality



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- The assessment on this point is made by the University of Oslo
- It is based on a review of recent contracts on the Norwegian continental shelf, plus data from the supplier survey
- The review shows:
- Large degree of overlap in requirements – the more, the better?
- Choice of requirements does not take cost-benefit considerations into account as much as it should
- Insufficient knowledge of regulations and a certain degree of risk aversion are part of the reason why alternative solutions are chosen away.

“Once we had to follow a requirement related to ozone protection for a product that was to be installed subsea ...”

“Sometimes we experience that requirements for the same delivery are in direct conflict with each other”

- The way the specification of requirements is designed makes the process of reviewing and interpreting requirements time-consuming and costly
- Overlap and contradictions contribute to insecurity:
 - Discussions about how to interpret requirements and how to handle potential inconsistencies are resource-intensive
 - This explains why administration costs related to requirements are higher by several hundred percent
- In a number of cases, we have found that contradictory and overlapping requirements have led to adaptations, resulting in a product that is less safe
- If that's the case, this violates the intent of the legislation

«The amount and the strictness of requirements reached a peak during the good times in the oil industry»

- Contracts in the delivery chain are designed «back-to-back»
 - Means that the terms of contract in the contract between the shipyard/overall supplier and sub-supplier reflect the terms of contract between the buyer and the shipyard/overall supplier.
- In case of faults or defects, the buyer may be entitled to hold back payment to the supplier, although the problem originates in a sub-part of the chain further down.
- The consequence of this is that the overall supplier poses more or stricter requirements to the equipment supplier in order to reduce own risk exposure.
- Requirements increase further down in the chain of suppliers.
- The combination of a contract based on hourly compensation and overall responsibility is unfortunate.

“Back-to-back” is problematic. We produce a small part of the total product, but are responsible for delays caused by others. If the main supplier does not get his delivery approved, we do not get paid either, although we have delivered in full and on time...”

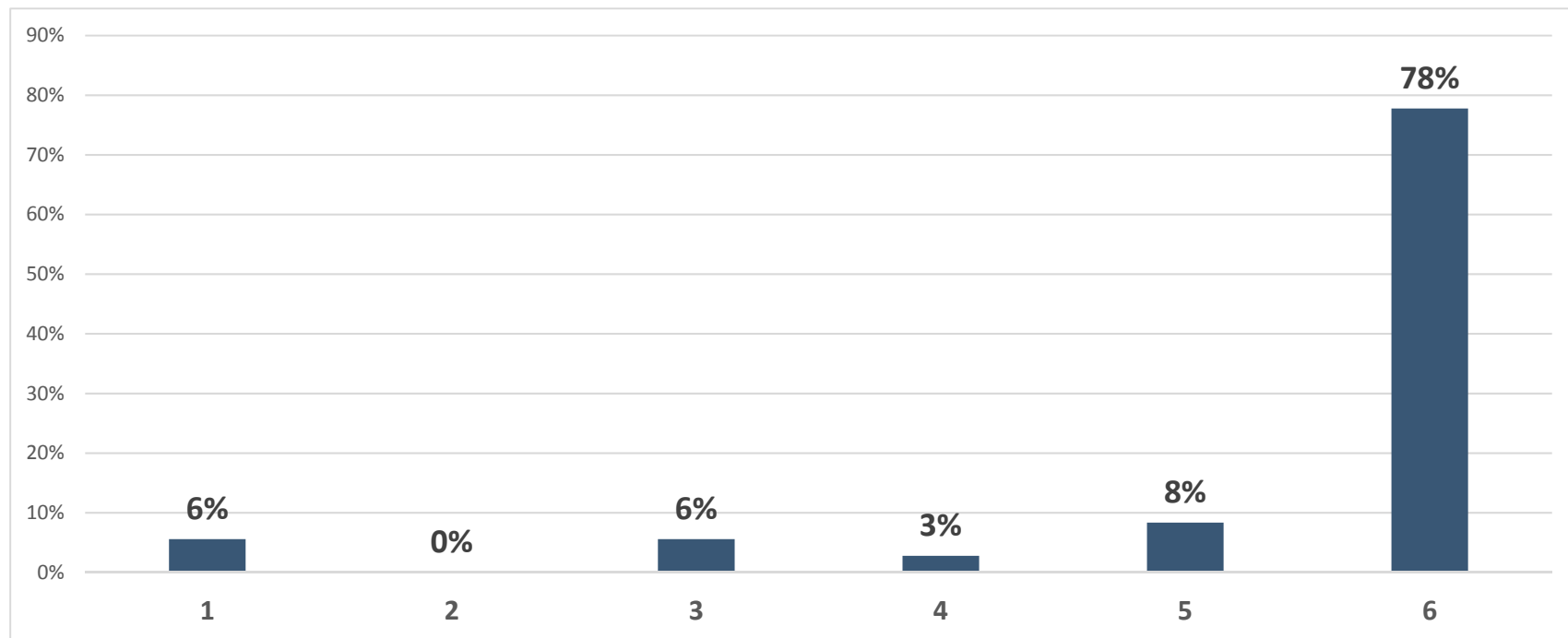
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- Too much information and information that is not safety-critical lead to «information overload»
 - Users use Google to find information rather than using the information material
- The Petroleum Safety Authority's review of accidents on the Norwegian continental shelf shows that every fourth incident is due to incorrect use of equipment.
 - In many instances, equipment has been used in a way that is in direct contradiction with the equipment supplier's user manual

“Offshore technicians that have to order new parts omit to search through the documentation, but read the part number off the part that is supposed to be replaced, and look for it on the producer’s website.”

RESPONDENTS THINK THAT THEY COULD DELIVER SAFER AND CHEAPER PRODUCTS

Distribution of interview objects' answers to the following statement: «We could have produced products that are equally safe, but cheaper, with less strict specification and documentation requirements». On a scale of response options from 1 to 6, alternative 1 stands for 'totally disagree', while 6 means 'totally agree'



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- *If you specify in detail what you want to have, you are likely to get exactly what you order*
- *You get yesterday's solutions, not tomorrow's*
- *Regime should be more performance-based:*
 - *describing what functions a product or service should provide*
 - *makes it possible for the oil companies to reap the benefits of new technological solutions*
 - *take advantage of technology development that takes place in completely different industries, in the same way as other industries have benefited enormously from technological developments in the oil and gas industry (Rambøll, 2015).*
- *Would it be possible to achieve a new Troll-development under the current requirement regime?*