

# Price Adjustments in New York State Centralized Contracts

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## Why Should One Consider Using Price Adjustment Provisions?

- Long Term Contracts (over a year)
- Volatile Market Conditions
- Keep Pace with Product Changes
- Time and Cost of Repeated Bids

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### Considerations

- What type of adjustments should be used?
- What price index should be used?
- How is the price adjustment calculated?

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### Also...

- When does an adjustment begin?
- How often should adjustments occur?
- Should Adjustments be Automatic *or* Adjusted upon request?

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### Types of Price Adjustments

- General Business Adjustments
- Product or Component Specific (Weighted) Adjustment
- Price List Updates
- Fuel Surcharges

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### General Business Adjustment

- May be considered when no one cost component dominates the price structure.
- Can be considered “Cost of Living Adjustment”
- US Bureau of Labor Statistics:  
<http://www.bls.gov/>
- ✓ CPI – Consumer Price Index
- ✓ PPI – Producer Price Index

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### NYS contracts with General Business Adjustments

<u>Award Number</u>	<u>Description</u>
■ 19198	School Buses
■ 20373	Prescription Forms
■ 20436	Kraft Envelopes
■ 20800	Milk
■ 20994	Facial Tissues
■ 21340	Elevator Maintenance

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### Product or Component Specific (Weighted) Adjustment

Used when one component accounts for the majority of the cost for a product or service, such as:

- Specific raw materials
- Certain types of fuel

Adjustments target the specific component or product.

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**NYS contracts containing Product or Component Specific (Weighted) Adjustments**

<u>Award Number</u>	<u>Description</u>
■ 20056	Glass Spheres for ReflectORIZED Pavement Marking
■ 20674	Guide/ Bridge Rails, End Sections & Accessories
■ 20859	Traffic Control Equipment
■ 20883	Road Salt
■ 21141	Hot Mixed Asphalt

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**Price List Updates**

- Price List Updates - a form of price adjustment that accounts for market changes within the vendor's normal course of business.
- Generally applies to Catalog Contracts or National Price Lists

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**New York State Catalog Contracts with Price List Updates**

- Many products from one source
- No one product dominates overall purchases
- Product continuity and integration is important

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### Golden Rule for Updating Price Lists

Discounts bid by the contractor can never be reduced but can always be increased!

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### Price List Update Reminders

Monitor the Commodity, Review ALL Updates

Are the changes reflective of the market?

Updates can be a tool to introduce new products and remove outdated ones

**Generally no** additional Price Adjustment Clauses should be used in conjunction with a Price List Update

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### New York State Contracts containing Price List Updates

<u>Award Number</u>	<u>Description</u>
■ 19745	Hazardous Incident Response Equipment
■ 20304	Industrial & Commercial Supplies & Equipment
■ 20385	Roadway Sign Supports
■ 20551	Furniture, All Types
■ 20867	Plastic Pavement Marking Material

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## Fuel Surcharge Adjustments

Fuel Surcharges are targeted adjustments designed to alleviate negative impact to the contractor for volatile fuel costs for transportation and shipping

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## New York State contracts containing Fuel Surcharges

<u>Award Number</u>	<u>Description</u>
■ 00179	Courier Services
■ 02832	Food, Household Items, Sundries
■ 20385	Roadway Sign Supports
■ 20338	Road Salt

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## What price mechanism should be used for price adjustments?

A Price Adjustment requires 3 puzzle pieces to be in place for an adjustment to occur.

1. a contract price
2. a basic index
3. a value change in the index

But...What is an index & where does one find an index?

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## What is an Index?

An index is a statistical value, not necessarily a price, that represents a specific set of data, which can be tracked over time.

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## Common National Indexes

- The Plastics News
- Oil Price Information Service (OPIS) - gasoline
- The American Metals Market (AMM) – snowplow edges
- The New York Mercantile Exchange (NYMEX) - natural gas
- Journal of Commerce (JOC) - heating oil, kerosene, propane, diesel
- Energy Information Administration (EIA) - fuel surcharges
- US Department of Labor, Bureau of Labor Statistics (BLS) (PPI, CPI)
- RISI – pulp and paper

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## Indexed, Energy and related Contracts

- Diesel, biodiesel, ultra low sulfur diesel
- Natural gas
- Gasoline and E-85
- Propane (liquefied petroleum), kerosene
- Heating fuel oil and bioheating (B5)
- Renewable energy credits (biomass – organic material made from plants and animals. )
- Refined hydraulic and lubricating oil

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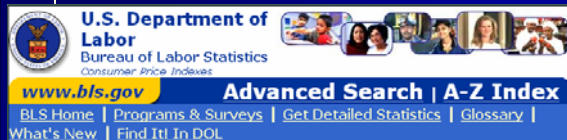
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## U.S. Dept. of Labor - BLS Website

<http://www.bls.gov>



This site is the Federal Government's directory of economic and business statistics

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## Use the BLS site for adjustments

Select from lists of statistics including:

- Average Price and Wage Data
- Consumer Price Index - urban (CPI-u)
  - Producer Price Index (PPI)

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## What are the CPI & PPI ?

The **Consumer Price Indexes (CPI)** program produces monthly data on changes in the prices paid by urban consumers for a representative basket of goods and services.

The **Producer Price Index (PPI)** program measures the average change over time in the selling prices received by domestic producers for their output.

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## CPI vs. PPI

**CPI reflects changes in prices for goods & services purchased for Personal Consumption by US households & measures changes in cost of living.**

- CPI includes both foreign & domestic products, & services
- CPI measures spending
- CPI includes Taxes, Transportation, Intermediate markups (Wholesale costs), and the costs of doing business.
- CPI is a 2 month average figure
- CPI reacts faster to conditions than PPI

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## CPI vs. PPI

**PPI measures changes in real production output.**

- PPI measures products not spending
- PPI is the revenue received by the producer for the product produced.
- PPI does not include taxes, transportation, overhead
- PPI includes non consumer products such as industrial products & capital equipment
- PPI is a monthly index but requires a 3 month calculation period before a final Index is posted, thereby reacting slower over time
- PPI immediately accounts for new products as sale and inventory levels are non-factors.

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## What is the best index for your specific situation?

- Ask the vendor community
- Research specific products
- Use the North American Industrial Classification System (NAICS)

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## Every US company has a NAICS number



- It is found at the top of page 2 of every company's Federal tax form
- There is nothing proprietary about it. It's a part of the U.S. Census Bureau:  
<http://www.census.gov/epcd/www/naics.html>

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## The NAICS # corresponds to a PPI number to obtain an index

### Use Caution!

- Some companies handle a number of different product lines
- Consequently there may not be an exact match
- Try to narrow the index to the specific product

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## OTHER CONSIDERATIONS

- Some indices are regional
- Some indices have seasonal factors
- Private Sector indices tend to react faster than the BLS indices
- Private Sector indices tend to be more volatile than BLS indices

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## How is the adjustment calculated?

Clearly develop and detail the calculation process in your bid document and apply it at the proper time

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## Calculation Golden Rules

### Never Change

The Base Date & The Index Base Value once established.

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### Consistency

Always go to the awarded price and adjust from there.

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## Calculating General Business Adjustments

1. Look up the current index value
  1. Calculate an Adjustment Factor

Divide the current index value by your established base index
  2. Calculate The Adjusted Price

Multiply the contract price by the adjustment factor

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### Hypothetical Example

Contract begin date is 01/01/08  
Price at beginning of contract is \$200  
CPI value for October 2007 is 150 (The BASE)  
CPI value for October 2008 is 160  
Divide 160 by 150, = 1.0667 (Adjustment Factor)  
Multiply 1.0667 times \$200.00  
The new price for 01/01/09 is \$213.34

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### Calculating a Weighted Adjustment

Apply a proportion based on costs for one or two main components.

Choose the appropriate weights by:

- Reviewing annual reports of companies in the industry
- Look at industry data
- Consult vendors, manufacturers, and suppliers of raw materials, etc.

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### Calculating a Weighted Adjustment

Similar method and calculations to General Business Adjustments

- Look at the specific situation to decide what needs to be adjusted
- Determine base values  
Adjustment Factor, Adjustable Amount, & Adjustment Amount
- Calculate the adjustment

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### Example

35% of Reflective Glass Spheres is for Natural Gas Energy and is adjusted proportionally

- The original contract/bid price for Glass Spheres is \$0.50 per pound
- The settlement value for Natural Gas at the time of the bid is \$8.40 (The Base Index)
- If price for Natural Gas increases to \$9.75

**How is the adjustment calculated?**

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### Find the Adjustment Factor

Take the New Index Value (\$9.75)  
Divide it by the Base Index Value (\$8.40)

**This is the Adjustment Factor = 1.16**

- **Find the Adjustable Amount:**

If 35% of price is energy related adjustable cost,  
Multiply the contract price (\$0.50) by 35%

**This is the Adjustable Amount = \$0.175**

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### Find the Adjustment Amount

Multiply the Adjustable Amount by the Adjustment Factor ( $\$0.175 \times 1.16 = \$0.203$ )  
Calculate the difference between the Product and the Adjustable Amount ( $\$0.203 - \$0.175 = \$0.028$ )  
rounded to 2 decimal places.

**This is the Adjustment Amount = \$0.03**

- **Add the Adjustment Amount to the Base Price**  
( $\$0.50 + \$0.03 = \$0.53$  per pound)  
**Price Adjusted!**

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## Best Practices

- **When writing a bid**
  - Clearly identify what is being adjusted
  - Clearly explain the Calculation Formula
  - Provide the formula in steps – show the math for ease of use
  - Clearly explain when adjustments begin and when adjustments take place
  - Clearly state if adjustment is automatic or request-based
  - If request-based, designate specified time period for requests and indicate to contractor that failure to request results in loss of price adjustment for that period

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## Best Practices

- **When writing a bid**
  - Clearly identify the Index (or Indices)
  - Clearly identify Base Index Values and Dates
  - Include a mechanism that allows flexibility
  - Provide language enabling changes in index, frequency of application, if necessary (ex. Fuel generally is weekly index but can convert to daily during extreme volatility)
  - Be consistent: use similar indexes, formulas and frequency for similar products
  - Listen to the industry (i.e. paper industry)

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## Best Practices

- **When writing a bid**
  - Clearly state Price Adjustments are both upward and DOWNWARD. Use terminology price adjustment, not price escalation
  - Do not include additional price adjustment clauses in a Price List bid
  - Specify clearly discount remains the same or better throughout the contract term
  - Standardize on a national price list, where possible

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## Things to Consider

- How often should adjustments be made?
  - at predetermined intervals?
    - Annually, Semi Annual, Quarterly, Monthly?
  - or with market need ?
    - upon request, or as manufacturers issue updated price lists

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## Things to Consider

### What is the Intent of the Adjustment

to maintain a balanced market  
to address transportation fluctuation  
to enable longer contract periods

### What is actually being Adjusted?

Should the full product price be adjusted or only a percentage (%)

### What caps and limits should be considered?

Consider a minimum 2% index movement before allowing an adjustment up or down

Should a maximum cap placed as a limitation (NYS Office of the State Comptroller recommends 5% cap)?

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## Research & Communicate

### IMPORTANT!

- Chart past prices using the index under consideration to determine past trends
- Share your information with involved parties
- Talk to both vendors & end users

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## Examples of Clauses

- Clauses that follow are examples of the various price adjustment categories

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## Natural Gas Price Adjustment

### PRICE ADJUSTMENT CLAUSE:

All contract pricing is adjustable after the first three (3) month period of the contract and every month thereafter, with the initial adjustment occurring on May 1, 20xx, or on the first day of the month following the initial three months of the contract should the Date of Issue of the contract award be later than Jan 31, 20xx.

The price adjustment on each item will be commensurate with the increase or decrease on the New York Mercantile Exchange's Most Recent Settlement price for Natural Gas Futures based on supply through the Henry Hub for next calendar month deliveries as calculated every business day by the New York Mercantile Exchange and published on their website at <http://www.nymer.com/index.nso.aspx> at 3:00pm Eastern Time, three (3) business days prior to the first calendar day of the month of adjustment. The index adheres to the trading rules as set forth by the New York Mercantile Exchange.

The index base will remain constant through the term of the contract.

Should the index be removed by NYMEX, the Procurement Services Group of the NYS Office of General Services retains the right to select and implement a new index deemed appropriate of their choosing. In such instance the base would change to that of the new referenced index.

The index base for this contract is the NYMEX settlement price of December 21, 20xx: \$14.080

For the purpose of this contract and the price adjustment described herein, Natural Gas price is estimated at 35% of the established contract.

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## Producer Price Index

**Price Adjustments:** All contract pricing is subject to an increase or decrease after May 31, 20xx and every three (3) months thereafter, with the initial adjustment occurring on June 1, 20xx. The price adjustment on each item will be commensurate with the increase or decrease in the United States Department of Labor Producer Price Index (PPI) for the classification covering Paint and Coating Manufacturing, Special Purpose Coatings, including Marine, Industrial, and Maintenance Coatings, etc. Series ID# PCU 3255103255107.

The State will not effect any price adjustments, either increases or decreases, for percentage changes of two (2%) percent, or less from the benchmark.

The benchmark value for the class upon which the adjustments are calculated is established as: **221.2**. This value is the most recently published value, whether or not indicated as "preliminary"; Producer Price Index (PPI) dated **December, 2006** as published by the U.S. Department of Labor on January 31, 2007, just prior to the date of publication of this IFB. Unless removed by the U.S. Department of Labor, this value remains constant throughout the term of the contract.

The most recently published (current) **Producer Price Index** (whether or not indicated as "preliminary") divided by the benchmark index (**221.2**) for the classification group PCU 3255103255107, rounded to 3 decimal places) equals a multiplier.

The contract award price multiplied by the multiplier equals the adjusted price.

As the State will not effect any price adjustments, either increases or decreases, for percentage changes of two percent (2%) or less, if the multiplier is a number between 0.98 and 1.02 there is no adjustment. A multiplier greater than 1.02 will result in an increase in price and a multiplier of less than 0.98 will result in a decrease in price.

A Purchasing Memorandum will then be issued by the Procurement Services Group to reflect the price increase or decrease which will be effective June 1, 2007, and every 3 months thereafter.

If any of the referenced indices changes or are removed, an index deemed appropriate by the Procurement Services Group will be used in its place. In such instance the base would change to that of the new referenced index.

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## Price List Update Clause (computers)

Price Increases - Price increases shall be effective as to orders placed after: i) the date on which such increase becomes effective under the appropriate benchmark the GSA Schedule or under other appropriate benchmark generally (i.e. US Commercial Price List) or ii) thirty days after the date on which OGS and the NYS Comptroller have received and approved the amended pricing, whichever is later. In no event can a price increase be posted to the Contractor's Internet site until after the effective date. Additionally, where the pricing submitted for services are not benchmarked to an approved GSA Supply Schedule, Contractor may request an increase in the pricing contained in Appendices D or E provided that Contractor certifies in writing that the price change for services applies to all U.S. customers using the same benchmark. Such adjustment shall not exceed the lesser of five (5%) percent or the percent increase in the latest copy of the "National Consumer Price Index for All Urban Consumers (CPI-U)", as published by the U.S. Department of Labor, Bureau of Labor Statistics, Washington, D.C. 20212. Contractor has the sole responsibility to submit to OGS a service rate adjustment request thirty (30) days prior to the effective date of the price increase, providing a copy of the index and other supporting documentation necessary to support the request. In the event that this index ceases to be published, the referent index shall be as issued by the U.S. Department of Labor in its place. In no case shall the percentage increase result in a NYS Price which exceeds Contractor's commercial price list.

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## Fuel Surcharge Clause (Food)

The State shall consider the implementation of a fuel surcharge as a result of worldwide catastrophe that causes the "Weekly Retail on-Highway Diesel Prices" for the Central Atlantic (New York State) region to exceed 50% of the price per gallon. The State shall use the following "Weekly Retail on-Highway Diesel Prices Index." The "Weekly Retail on-Highway Diesel Prices," in cents per gallon, for the Central Atlantic (New York State) region shall be tracked using information obtained through the Energy Information Administration, United States Department of Energy's (EIA DOE) web site: <http://onto.eia.doe.gov/coal/retail/centralatlantic.asp>

For every \$1.00 cents per gallon that the price exceeds 50% of the cost of the referenced diesel fuel price at the time of bid opening, a delivery surcharge of \$1.00 per invoice will be allowed. For example, if \$1.49 is the price of diesel on date of bid opening and \$2.47 is current price, the difference above 50% of the bid price is \$.23. Therefore, a surcharge of \$2.00 (\$1.00 for every \$.10) may be added. The increase shall be figured in whole increments only. It is the responsibility of the Contractor to notify the Office of General Services Procurement Services Group (OGS/PSG) of any request. All fuel surcharges shall take effect after approval by OGS/PSG.

Once the "Weekly Retail on-Highway Diesel Prices" for the Central Atlantic (New York State) region drops below 50% of the price per gallon threshold based upon the original bid opening date, the fuel surcharges shall be removed.

In the event fuel prices decrease by more than 50% of the price per gallon based upon the price in effect at the time of the Bid Opening using the "Weekly Retail on-Highway Diesel Prices Index," the State shall apply a credit to each invoice as per the above example.

The "Weekly Retail on-Highway Diesel Prices" in cents per gallon, for the Central Atlantic (New York State) region at the time of the bid opening (March 6, 2003) was \$1.021 per gallon.

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## Economic Price Adjustment – non-NYS clause (NYC regional)

Price adjustments to unit prices shall be in accordance with (AAA Daily Fuel Report published on-line at <http://www.fuelgaugereport.com/C0metro.asp> for the xxx metro area), no more frequently than after the initial base period as defined in the Contract, hereafter referred to as the Review Period, and shall not exceed the most recent or the latest published percent change from the base number of (one percent (1%) shift, up or down in unit prices for every twenty-five cents (\$0.25) that Gas Regular Unleaded shifts from the current baseline price per gallon of \$3.90 and Diesel No. 2 shifts from the current baseline price per gallon of \$4.68) established for the initial contract pricing. In the event the index ceases, another index shall be mutually agreed upon. If a replacement index or price change cannot be agreed upon, the Contract shall be escalated to the respective xxx and SELLER management. Prices shall not change if the cumulative index change is one percent (1%) less, up or down based on frequency of reviews.

All proposed price adjustments based on the designated index above shall be limited to the most favorable market prices prevailing at the time of such proposal. If changes are proposed, appropriate documentation must be submitted with your proposed prices for the next Review Period. Either party can initiate a price adjustment request for the next Review Period, so long as such request is submitted no earlier than 90 calendar days prior and no later than 60 calendar days prior to the start of the next Review Period. In no event will any contract line item price adjustment exceed the percentage change in the index set forth above.

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## Supplemental Bid Instructions Related to Economic Price Adjustment

- Respondents shall identify with their bid the specific items subject to future price adjustment during the life of the contract, including all options thereto, and shall describe the methodology that will be used to calculate future price changes and how this approach will also comply with the Price Warranty provisions of the sample contract provided herein. The Economic Price Adjustment Supplemental Condition applies to both escalation and de-escalation of the designated price index.

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