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Trade and Industry Committee

The future of UK manufacturing: public procurement

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Footnotes

In the footnotes of this Report, references to oral evidence are indicated by 'Q' followed by the question number. References to written evidence are indicated in the form 'Appendix x' with two exceptions indicated in footnotes 4 and 5. The oral and written evidence is printed in a separate volume, Future of UK manufacturing, Oral and Written Evidence, HC 161 of Session 2006-07.

Contents

Report	<i>Page</i>
Summary	3
1 Introduction	5
2 Government policy and international agreements	6
Government policy	6
International agreements	7
Preferential treatment?	8
3 Procurement practice in the UK	12
Bureaucracy and risk aversion	13
Working with the supply chain	17
Innovation and sustainability	18
Social Objectives	23
4 Barriers to SMEs	26
Late payment	27
Support to SMEs	28
SMEs and the Government's efficiency drive	30
5 Consistency and the role of the OGC	34
Conclusions and recommendations	37

Summary

UK government policy on public procurement is clear: to achieve value for money — taking account of whole-life cost and other requirements such as relevant economic, social or environmental objectives — through a fair and open competitive tendering process. However, applying this policy to every contract demands detailed guidance from an authoritative source and skilled and experienced personnel in all 2000 public bodies in the UK that procure goods and services.

We were told that too often public officials, faced with difficult decisions and afraid of criticism if the procurement went wrong, took refuge behind bureaucracy, failed to choose innovative or environmentally sustainable goods and services, and opted for the least cost not the best value bid. As well as costing more in the long term, this deterred competition and innovation among suppliers and was particularly harmful to small businesses which do not have the resources to sustain complex, prolonged tendering processes.

These failings are caused not by a flaw in public policy but by problems in its implementation. The Office of Government Commerce (OGC), the body charged with overseeing procurement policy, has issued a number of comprehensive guides to best practice and has drawn up useful standard forms, for example in relation to prequalification for tendering. However, until a few months ago it did not have the authority to enforce implementation of best practice. We expect it to do so now.

We are concerned that in one area — the use of public procurement to further the Government's social policy and equality aims — the OGC's guidance did not go far enough. We recommend that the guidance be reviewed.

In some respects, the Government's current efficiency drive — involving (amongst other things) centralising purchasing and the use of framework contracts — is making it more difficult for SMEs to compete for public contracts and reducing competition further. We were also told that public bodies had a poor record on timely payment of bills, which we deplore.

Despite the OGC's new focus and powers, it has a small staff and will find it difficult to police even the central government departments, let alone provide advice and guidance to other public sector bodies. Therefore, we emphasise the need for better trained and higher quality procurement officials throughout the public service, supported by floating teams of experts in particular procurement areas.

1 Introduction

1. The public sector spends nearly £125 billion, or 10% of GDP, a year purchasing goods and services in the UK economy.¹ The manufacturing sectors most heavily involved in selling to Government include food, paper and printing, pharmaceuticals, construction products, aerospace and environmental technology. In the autumn of 2006 we began a series of inquiries examining issues of concern to manufacturing industry under the broad heading of ‘The future of UK manufacturing’. We have already published Reports into two of these issues, skills shortages in manufacturing industry and government support for exporters.² We now turn to the question of whether the rules and practices relating to procurement of goods and services by public authorities hinder or help UK manufacturers in obtaining public contracts.

2. During this inquiry we took oral evidence from British Expertise, a trade organisation promoting the export of professional services from the UK; the Confederation of British Industry (‘CBI’); EEF, the Manufacturers’ Organisation (‘EEF’); the Forum of Private Business (‘FPB’), and Ms Leslie Kossoff, an Independent Executive Advisor; Intellect, a trade association for the IT, telecoms and electronics industries in the UK; the Trades Union Congress (‘TUC’); the trades union then called Amicus; and the Government, in the form of officials from the Department for Innovation, Universities and Skills³ (‘DIUS’) and the Office of Government Commerce (‘OGC’).⁴ We received written submissions from these and from a further nine professional associations, companies and trade organisations.⁵ We are grateful to all those who gave written or oral evidence to us.

¹ HM Treasury, *Transforming Government Procurement*, January 2007, para 1.4 (henceforth ‘Transforming government procurement’)

² Respectively, Trade and Industry Committee, *Better Skills for Manufacturing*, HC 493-I, Fifth Report of Session 2006–07; and Trade and Industry Committee, *Marketing UK plc — UKTI’s five-year strategy*, HC 557, Sixth Report of Session 2006–07.

³ The restructuring of government departments in June 2007 involved, amongst other things, the removal of the section of the Department of Trade and Industry dealing with promoting innovation to the DIUS; hence, the Government’s original Memorandum to us was submitted by the DTI, but the oral evidence and supplementary written evidence came from the DIUS.

⁴ With the exception of the evidence from Intellect and from DIUS and the OGC, all this oral evidence is printed as part of the volume covering all three manufacturing inquiries, Trade and Industry Committee, *Future of UK Manufacturing, Oral and Written Evidence*, HC 161 of Session 2006–07. Intellect’s oral evidence may be found in Trade and Industry Committee, *Europe moves East: The Impact of the New Member States on UK Businesses*, HC xx, Session 2006–07 (hereafter ‘Europe Moves East’). The oral evidence from DIUS and the OGC is published with this Report.

⁵ Association of the British Pharmaceutical Industry, British Furniture Confederation (Public Sector Working Group), British Printing Industries Federation, Federation of Small Businesses, Institution of Engineering and Technology and Institution of Mechanical Engineers (jointly), KPMG, Midlands Fashion Showcase, Royal Aeronautical Society, and Society of British Aerospace Companies. With the exception of the supplementary written evidence from DIUS and the OGC, which is published with this Report, all Memoranda were published in the *Future of UK Manufacturing* volume mentioned in footnote 4 above.

2 Government policy and international agreements

Government policy

3. The Government has recently described its procurement policy as follows:

“The Government’s overall procurement policy is centred on buying the products it needs under a fair and open competitive tendering process, guarding against corruption and achieving value for money. ...

“The purpose of procurement policy is to support the Government’s goal of delivering world-class public services that are value for money, and in a sustainable way. Effective procurement also has the capacity to drive the efficiency of suppliers and their supply chains...

“Good procurement means getting value for money — that is, buying a product that is fit for purpose, taking account of the whole-life cost. A good procurement process should also be delivered efficiently, to limit the time and expense for the parties involved. Successful procurement is good for the public, good for the taxpayer, and good for businesses supplying the government.”⁶

4. This policy is fleshed out in other documents. The then Department of Trade and Industry [‘DTI’]⁷ argued in its Memorandum to this inquiry that value for money was “not about securing the lowest upfront price”, but rather achieving the best possible combination of ‘whole life cost’ set against ‘quality’. In this context, the DTI intended ‘quality’ to mean the extent to which the contract met the purchaser’s requirements, which might include economic, social and environmental objectives that were relevant to the contract in question.⁸ Moreover, “goods, works and services should be acquired by competition unless there are convincing reasons to the contrary”, not only in order to achieve value for money for the taxpayer but also “contributing to the competitiveness of UK suppliers, ... improving their ability to participate in both domestic and overseas markets”.⁹

5. The principles of government procurement policy are therefore clear and we heard no objections to them, but implementation of them has proved more problematic. Following Sir Peter Gershon’s review of civil procurement by government in 1999, the Office of Government Commerce was set up as an ‘independent office of the Treasury’ to promote good procurement across government. Although the OGC formulated policy and issued best practice guidance to all central government bodies, responsibility for implementing

⁶ *Transforming government procurement*, paras 1.3, 1.5 and 1.6

⁷ Now Department for Business, Enterprise and Regulatory Reform

⁸ Appendix 18

⁹ *Ibid.*

the policy and, to a large extent, discretion over whether to follow the guidance remained with the individual purchasing authorities.¹⁰

6. The Government has undertaken a number of reviews that have developed procurement policy since the OGC was established. In 2003 the OGC itself conducted a review, headed by Sir Christopher Kelly, which concluded that government should take a more strategic role in increasing competition and building long-term capacity among suppliers. At the end of 2003 it published an action plan to achieve this.¹¹ The DTI's Innovation Review from the same year suggested that the public sector could do more to stimulate innovation, both through the design of the tendering process and by making it easier for smaller firms to tender for contracts. The Government's 2004 review of its Manufacturing Strategy reiterated the commitment to new procurement guidelines to achieve a "more coherent, transparent and predictable public procurement process resulting in innovative bids from UK manufacturers and better value for money for the public sector"; whilst the Sustainable Procurement Taskforce produced an action plan on environmental standards in June 2006 and HM Treasury published a report entitled *Transforming Government Procurement* on 23 January 2007.¹²

7. Despite these repeated attempts at development and clarification, those supplying goods and services to the public sector remain critical of procurement procedures and the way in which individual purchasing decisions are taken.

International agreements

8. All public procurement in the UK must comply with European Union law and international treaty obligations. The DTI summarised the most important requirements as follows:¹³

- EU Treaty principles¹⁴ which prohibit discrimination on grounds of nationality, restrictions on the free movement of goods and services, restrictions on the freedom of establishment and measures of equivalent effect. These Treaty obligations apply to all public procurement contracts, regardless of value;
- EU procurement directives, which reinforce the Treaty provisions for contracts above certain values (about £100,000 for central Government supplies and services and just under £4 million for works contracts) and which include detailed rules for advertising contracts, specifications, selection and award;¹⁵

¹⁰ Q 682 (OGC) See also para 71 below

¹¹ OGC, *Increasing Competition and Improving Long-Term Capacity Planning in the Government Market Place*, December 2003

¹² DTI, *Review of the Government's Manufacturing Strategy*, 2004, p 62 Sustainable Development Task Force, *Procuring the Future – The Sustainable Procurement Task Force National Action Plan*, June 2006

¹³ Appendix 18

¹⁴ As set out in Article 3 of the Treaty Establishing the European Community

¹⁵ A succinct description of the types of contract subject to EU procurement directives is given in the *Wood Review; investigating UK business experiences of competing for public contracts in other EU countries*, November 2004, paras 3.3.1-3.3.9 (hereafter 'Wood Review')

- Relevant case law, which clarifies aspects of the EU rules; and
- World Trade Organisation ('WTO') Government Procurement Agreement ('GPA') rules, which are similar to the EU rules but apply to the GPA signatories — a limited number of WTO members, including the USA, Japan and Canada — as well as to the EU. The GPA is intended chiefly to prevent discrimination between companies bidding for public contracts on the grounds of nationality. Parties to the Agreement are “required to give the products, services and suppliers of any other Party to the Agreement ‘no less favourable’ treatment than that which they give to their domestic suppliers”.¹⁶

9. New UK Regulations, which implement the consolidated EU public sector and utilities sector procurement Directives, came into force on 31 January 2006. These Regulations were intended to simplify and update the previous public procurement rules: for example, by providing clarification of the scope for taking social and environmental issues into account in public purchasing. They also recognised the use of modern procurement methods such as e-auctions, framework agreements and competitive dialogue for complex projects.¹⁷ The Government suggested to us: “The new procurement methods that the rules provide for, including electronic systems, together with the simpler and clearer rules generally, will reduce the burdens of the procurement process and should encourage suppliers within the manufacturing industry, including SMEs, to participate in public procurement opportunities either directly or as sub contractors, both in the UK and abroad.”¹⁸

10. Our witnesses accepted the need for international rules to discourage discrimination against suppliers on the grounds of nationality.¹⁹ However, most of them believed that, despite the EU procurement directives, there were differences in the way in which Member States approached public procurement from suppliers based outside their national boundaries. The FPB and Ms Leslie Kossoff were more concerned about the GPA. They considered that the restrictions imposed by the GPA were so disadvantageous to small and medium-sized companies (SMEs) in the UK that either the GPA should be amended or the EU should seek an opt-out from some of its provisions. We discuss the GPA and its effect on SMEs later in this Report.²⁰

Preferential treatment?

11. While public authorities in the EU Member States spend large sums procuring goods and services (estimated in 2003 at 1,500 billion euros a year, equivalent to 16% of EU GDP), little of this is accounted for by direct cross-border trade: only 10% of the total in 2003. This is half the rate found in the private sector.²¹

¹⁶ Appendix 25 (Forum of Private Business)

¹⁷ These methods are discussed in more detail below: paragraphs 61, 65-68 and 37 respectively

¹⁸ Appendix 18 and Q 685

¹⁹ See, for example, Q 65 and Appendix 22 (EEF) , Q 411 (Forum of Private Business)

²⁰ Paragraphs 62-63-

²¹ Wood Review, para 3.2.1, citing *Internal Market Strategy, Priorities 2003–2006*, Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the

12. A number of our witnesses were of the view that UK companies were significantly less likely to be awarded contracts by public authorities in other countries than foreign companies were in the UK. The Government has been aware of this concern for some years; and in 2003, it commissioned Mr Alan Wood, Chief Executive of Siemens UK plc, to conduct an inquiry into UK companies' experience of competing for public contracts in other EU Member States. The resulting report concluded that neither the rules themselves nor the application of them by Member States were considered the key problem by UK businesses. Few examples of clear breaches of EU law were found. However, as Mr Wood summarised in his foreword to the report, "there are many obstacles ranging from complex procedures to cultural differences and geographic distance that can hinder the success of UK firms. Crucially, there is still evidence of a lack of commitment to international competition and market liberalisation in some key sectors such as defence, energy and transportation. And there is room to improve the way public purchasers carry out their business, to ensure more transparency and effective competition."²² As the Wood report also points out, many of these difficulties (linguistic and cultural differences, geographical distance, reduced access to networks of relationships and less familiarity with institutions) are common to any export activities, and the EU "is by no means seen as the most difficult of export markets".²³

13. With the partial exception of Amicus, our witnesses accepted Wood's main conclusion, that difficulties arose from deep-seated differences in industrial policy and the culture of the procurement authorities, rather than from breaches of EU law.²⁴ Though it agreed that these 'grey areas' were significant, Amicus believed that other Member States were more inclined than the UK to flout EU law, and it attributed the paucity of specific examples of illegal activity to companies' decisions not to report breaches for fear of being excluded from future contracts.²⁵ Moreover, Amicus was of the view that: "Cultural differences are particularly prevalent where procurement is concerned, where buying locally is the norm and no amount of legislation or regulation from Brussels will change this."²⁶

14. A particular concern of some witnesses was how different Member States interpreted the partial exemption from the EU's procurement rules for defence-related procurement. Article 296 of the Treaty establishing the European Community says: "any Member State may take such measures as it considers necessary for the essential interests of its security which are connected with the production of or trade in arms, munitions and war material." This exemption is phrased in such a way that it does not apply to other types of goods or to anything not intended for specific military purposes even if purchased by a defence ministry. However, according to the TUC, "despite clarifications by the European Court of Justice, the low number of publications in the Official Journal of the European Union appears to imply that some Member States believe they can apply the derogation automatically. Since the concept of 'essential interests of security' is not defined either in

Regions, May 2003, COM (2003) 238 It is not clear from the Wood Review to what extent this figure may be biased by trade in protected sectors, such as defence or services of general interest.

²² Wood Review: See also paragraphs 1.2.1–1.2. and 1.4.1–1.5.1

²³ Wood Review, para 1.3.2

²⁴ Qq 62–65 (EEF), 108 (TUC), 185 (CBI), 219 (Amicus) and 685 (OGC)— but see also Qq 215 and 218 (Amicus)

²⁵ Q 218

²⁶ Appendix 2, para 3.9 See also para 3.8

Community Law or in the Case Law of the Court of Justice, in practice states allow themselves wide discretion in determining which contracts could damage them.”²⁷ A number of our witnesses considered that, in contrast, the UK failed to apply the derogation even when it was legitimate: one example given was that of a contract for battledress (although the complaint here was that the successful bidder sub-contracted production of the uniforms to a company in China); another was that in 2000 the Ministry of Defence had concluded that the Roll-On, Roll-Off ferries it wanted to acquire should not be classified as ‘war material’, and the tender was publicised under EU procurement rules and won by a German shipyard.²⁸ Government officials, however, told us that they had no reason to believe that the Ministry of Defence had done anything other than try to achieve best value for money for the UK taxpayer.²⁹ The TUC saw it rather differently, alleging that the Ministry just wanted the cheapest, rather than the best value, option.³⁰ This exemplifies two recurring themes in the evidence: how value for money can be judged, and whether procurement decisions should be made solely in terms of lifetime costs or whether they should also further other government policies.

15. Wood reported that the SME trade associations declined to take part in the Review on the grounds that European public procurement was not a high priority for their members, but also that the individual SMEs that responded to the Review considered their main need to be practical support and help from UK authorities or from other UK companies.³¹ He made a number of recommendations about how the UK Government could offer more practical advice and support to UK companies of all sizes and encourage the European Commission and other Member States to tackle the barriers to greater cross-border competition, partly through market opening of protected sectors and partly through the spread of best practice among procuring authorities.³² At the same time, he noted that some UK companies had adopted strategies which helped them to overcome the cultural and administrative difficulties in tendering for contracts abroad, in particular using a subsidiary, joint venture partner, distributor or sub-contractor located in the relevant Member State. The European Commission estimated that such ‘indirect cross-border trade’ — where the supplier, though local, was a subsidiary of a company based in another country — represented 30% of public procurement by EU Member States.³³ More specifically, it found that ‘local’ firms won on average 35% of tenders in their home markets even if they were under foreign ownership, while 30% were won by nationally owned companies and only 25% by companies bidding from a different country with no local connection.³⁴ Most of the rest of Wood’s list of ‘success factors’ for UK companies competing for public procurement contracts abroad amounted simply to normal good

²⁷ Appendix 48, para 3.3 See also Appendix 39, para 9 (Royal Aeronautical Society), although the aerospace industry was more exercised over lack of reciprocity with the USA than with the rest of the EU

²⁸ See, for example, Appendix 48, paras 4.1–4.5 (TUC)

²⁹ Q 726

³⁰ Qq 121-122 and 125–127

³¹ Wood Review, paras 4.1.3–4.1.4

³² See summary of conclusions in Chapter 6 of Wood Review Wood’s conclusions on the need for greater support by the UK Government for businesses seeking to sell into the EU were echoed by Amicus: Q 219 and Appendix 2, para 3.1

³³ Wood Review, para 3.2.2, citing *A Report on the Functioning of Public Procurement Markets in the EU: benefits from the application of EU Directives and challenges for the future*, European Commission, February 2004 (hereafter ‘European Commission, Public Procurement Markets’)

³⁴ Appendix 2, para 3.9 (Amicus) citing European Commission, Public Procurement Markets

business practice and commonsense: businesses should have good products or services to sell, ensure that these fitted customers' requirements, do some homework on the local market, seek help from relevant export support services, and have sales representatives who spoke the local language and understood the local business culture.³⁵ Amicus suggested there was scope for more co-operation between UK businesses, with those who had succeeded at winning public contracts elsewhere in the EU acting as mentors to those new to the process.³⁶

16. Mr Fanning of the OGC thought that there was a good case for updating the Wood Review on procurement in other EU Member States. We agree. We also accept that there may be more that companies could do to fit themselves for competing for overseas public procurement tenders, such as ensuring that their agents have appropriate language skills and seeking advice from bodies such as UK Trade and Investment. The UK Government must continue to encourage the spread of best practice in procurement by public authorities throughout Europe.³⁷ There is also a role for Chambers of Commerce or trade associations in helping to identify potential mentors for smaller or new-to-export companies.

17. The DTI's Memorandum lists activities taking place at European level to reduce barriers to cross-border public procurement and trade in general, and there have been well-publicised moves by the European Commission to open up some of the areas that Wood identified as particularly difficult for UK firms to penetrate — energy and defence.³⁸ However, our witnesses recognised that while formal barriers might be lifted, there was still room for legitimate differences of interpretation of EU procurement regulations, and that national governments varied in their approach to achieving value for money or, in EU terms, determining the “most economically advantageous tender”. Their main concern was that a rigid interpretation of EU rules in the UK led to UK companies being disadvantaged in their home market. We go on to discuss this in Chapter 3.

³⁵ Wood Review, para 4.17 See also Q 66 (EEF)

³⁶ Q 219 and Appendix 2, para 2.1

³⁷ Wood Review, paras 4.8.2, 4.11.10 and 4.11.12

³⁸ Appendix 18

3 Procurement practice in the UK

18. The Government's Memorandum emphasises that it "is committed to British manufacturing and helping manufacturers in Britain to gear up to compete for public procurement opportunities." It goes on to give details of "an extensive programme of work" to open the public sector marketplace to all suppliers, especially SMEs. These include: development of a web-based portal to advertise smaller value contracts (ie those below the EU threshold levels); creation of a standard, simplified pre-qualification questionnaire for below-threshold contracts; training for SMEs to enable them to become 'fit to supply' the public sector; the Small Business Concordat which forms part of the *National Procurement Strategy for Local Government*; identification of some of the barriers to suppliers created by third-party accreditation practice in the UK; and making both contracts and tendering procedures for the London 2012 Olympics as open as possible to SMEs. The Memorandum also mentions practical measures to encourage innovation and promote sustainability through public procurement, and sectoral initiatives such as the Defence Industrial Policy launched in December 2002.³⁹

19. While not disputing that the Government was trying to adapt rules and procedures to make it easier for companies to tender for and win public contracts, our witnesses in some instances felt that the changes had not gone far enough and argued that even more significant than the rules themselves was the narrow and rigid way in which they were interpreted by purchasers. Common criticisms were that:

- public sector buyers were insufficiently trained and skilled to interpret and implement the rules correctly, and that many had little or no detailed knowledge of the supply market;
- in particular, they did not understand the concept of best value, leading them either simply to award on the basis of lowest cost or to abandon criteria designed to achieve whole life value for money on the grounds that this made tenders more expensive up front;
- they did not make use of the leeway provided by EU procurement rules to pursue social, economic and environmental purposes in the letting of contracts;
- the UK's tendency to aggregate contracts excluded SMEs from competition;
- the system was still far too bureaucratic, with each of the 2000 public sector purchasers having different procedures and forms, terms and conditions for tendering; complex and repeated procedures for pre-qualification for tendering; requirements to provide irrelevant information; changes in specifications; delays in notification of whether tenders have been awarded;⁴⁰ and

³⁹ Appendix 18

⁴⁰ See, for example, Intellect's views: Q 163 in 'Europe moves East'

- over-detailed specifications in contracts inhibited innovative, or cost effective, or environmentally sustainable solutions.

Bureaucracy and risk aversion

20. One of the main difficulties facing those wishing to supply public authorities is the number of those authorities (according to one of our witnesses, in the UK alone at least 1600 local authorities and more than 350 central government bodies) and the lack of standard procedures and forms. Some of our witnesses went so far as to suggest that each of the authorities had its own procedures and forms; and that, while the OGC had produced some best practice documents, these were not widely used.⁴¹

21. The EEF argued that successful procurement — achieving value for money for the purchaser and developing a good working relationship with the supplier — depended heavily on the skills and confidence of those doing the procuring. Many of our witnesses believed that current skills levels among those involved in public procurement were inadequate, especially in central government and even more so in those departments not heavily involved in major procurement initiatives.⁴² Exceptions to this criticism of central government departments were the Ministry of Defence — whose improved performance was attributed to the change brought about by the Defence Industrial Strategy⁴³ — and, according to the contractors' organisation British Expertise, the Department for International Development.⁴⁴

22. Most of our witnesses commented on what they saw as the timidity of many of those engaged in public procurement. They suggested that, afraid of criticism if the procurement exercise 'went wrong', civil servants took refuge in highly complex, long tendering procedures, making the whole process significantly more costly in terms of both time and money to the would-be supplier than a comparable procurement exercise in the private sector.⁴⁵ We were told that many purchasing authorities had a single set of procedures and forms for all purchases, however simple or complex, which resulted in suppliers having to provide information that was over-detailed or irrelevant to that contract.⁴⁶ So complex were the tendering processes that an industry of intermediaries had grown up to assess the tenders. They charged fees to would-be suppliers, and the OGC had concluded in December 2005 that in themselves they formed a barrier to SMEs wishing to trade with the public sector. Elaborate tendering requirements were particularly irksome when companies had to follow exactly the same process to supply the same goods to another department. SMEs found the bureaucracy an even greater deterrent than larger companies, as the contracts for which they were bidding were often for smaller sums and they were less

⁴¹ Appendix 7 (British Furniture Confederation)

⁴² Qq 46 (EEF), 132 (TUC) and 176 (CBI), Appendices 22, para 25, and 23 (both EEF) and 28 (KPMG)

⁴³ Q 48 (EEF) and Appendix 44 (SBAC)

⁴⁴ Q 365

⁴⁵ The FPB suggested that the bureaucracy associated with completing a tender often takes one person three working days: Appendix 25

⁴⁶ Appendices 6 and 7 (British Furniture Confederation)

able to absorb the extra cost of the tendering process.⁴⁷ Moreover, some smaller procuring authorities, such as universities and local councils, required suppliers to pay a fee of anything between £30 and £118 for the tender documents, either to share the costs of EU-compliant procedures or to deter unrealistic applications.⁴⁸ The British Printing Industries Federation alleged that many high quality companies did not bother to compete for public sector contracts because the sector's approach was insufficiently dynamic, tendering procedures were too time-consuming, and the financial return was too low.⁴⁹

23. Some witnesses suggested that purchasers made their decisions solely on the basis of lowest cost.⁵⁰ It was also alleged that ultimately officials accepted whatever was seen as the 'safest' bid, for reasons of convenience, to minimise civil service time in decision-making, and because of the inability of the public sector to make provisions for risk⁵¹ — summed up by one witness as an attitude of 'Nobody ever got sacked for hiring IBM'.⁵² The net result was that potential contractors were deterred and competition was diminished. As well as costing more overall, such decisions also discouraged innovation and undermined the Government's policy of sustainable procurement.⁵³ The British Furniture Confederation argued that tender documents should give a clear weighting to the various criteria the purchasers would apply when judging the bids, and that the contracts should be let in accordance with these criteria.⁵⁴ The Forum of Private Business suggested that public authorities should apply a decision-management process — either through special software or through recognised procedures — to ensure that they took appropriate account of factors other than short-term cost.⁵⁵

24. The CBI commented that in central government there was a lack of co-ordination between those commissioning and those running the procurement process for goods and services; a very high turnover of staff, which created even greater problems when the project was complex and lengthy, such as many construction and IT contracts; and a failure to identify a particular senior manager to span the commissioning/procuring roles and take responsibility for successful delivery of the project.⁵⁶ British Expertise praised the approach of the Department for International Development which had considerable experience of procurement and whose procurement staff were "very savvy". It noted with approval that considerable responsibility was devolved to the individual desk managers, who were able to procure goods and services worth less than the EU threshold levels without competition if they knew of a reliable supplier. This they contrasted with other

⁴⁷ Qq 49 (EEF), 128 (TUC) and 176 (CBI); Appendices 8, paras 22–23 (British Printing Industries Federation) and 25 (FPB)

⁴⁸ Appendix 8, Case Study 4 (British Printing Industries Federation)

⁴⁹ Appendix 8, para 19

⁵⁰ Appendices 6 and 7 (British Furniture Confederation) and 22, para 25 (EEF)

⁵¹ Such as bad debt provisions in their accounts, hedging risky investments, and a variety of sources of finance depending on the type of investment and the assessment of risk

⁵² Appendix 25 (FPB)

⁵³ On value for money see, for example, Appendix 22 (EEF) and the TUC's comments on procurement of battledress by the Ministry of Defence: Qq 121–122, 125–127 On innovation and sustainability, Qq 45–46 (EEF) We discuss the opportunities for innovation and sustainable procurement in more detail below, Paragraphs 33–46

⁵⁴ Appendices 6 and 7

⁵⁵ Appendix 25

⁵⁶ Q 176

departments which, they said, ran expensive and time-consuming competitions for everything.⁵⁷

25. The Forum of Private Business highlighted two general tendering requirements burdensome to small businesses: the first was the standard requirement that companies should prove their financial capacity for delivering the contract by producing three years' worth of audited accounts (which — they argued — disadvantaged new, innovative companies and small private businesses exempt under company law from the requirements for audited accounts, and also was “of questionable relevance to their ability to complete the job”); the second was the need to pre-qualify for every tender, rather than being certified as meeting the standard once and for all.⁵⁸ Pre-qualification procedures irked a number of our witnesses, who argued that the differing requirements of the various public authorities left would-be suppliers at the mercy of those providing accreditation services, for which fees were charged.⁵⁹ Ms Kossoff, an Independent Executive Advisor, praised the use in the USA of certificates of competence, which (as the name implies) were intended to give confidence that the holder met certain specified criteria — which could include not only general performance but also issues like environmental compliance — and were accepted as a pre-tender qualification across the public sector.⁶⁰ We asked whether it was difficult to ensure continued compliance with the criteria, but Ms Kossoff said that successful bidders were monitored during the course of the contract anyway, so any failure to comply became apparent.⁶¹ The FPB said that there had been attempts to introduce something along these lines in the UK, but so many different criteria were required by the various authorities that it had proved impossible to have a fully transferable guarantee of competence.⁶² The British Printing Industries Federation took a different route. It developed an online print portal, which would eliminate pre-qualification processes (as suppliers would have had to pre-qualify to enter the system), minimise the cost of seeking quotations and allow purchasers to sift suppliers according to additional criteria, such as high environmental standards or a commitment to training staff. However, discussions with public sector buyers brought to light the fact that, although they were enthusiastic about the potential of the system, they were not confident that it could be developed to comply with EU procurement regulations.⁶³

26. The EEF compared the situation in the public sector unfavourably with a number of business sectors such as aerospace and the automotive industry, where, it argued, large, complicated, risky procurement exercises were frequently undertaken with far less bureaucracy, based on better-established relationships between suppliers and purchasers and a greater understanding of the long-term balance between costs and benefits. The EEF thought that those undertaking public sector procurement needed specific training in risk

⁵⁷ Q 365 For the counter-argument, in favour of running competitions, see Paragraph 69 below

⁵⁸ Qq 421–3 and 425 see also Paragraphs 60–61 below

⁵⁹ See, for example, Appendices 7 (British Furniture Confederation Public Sector Working Group) and 8, paras 26–28 (British Printing Industries Federation)

⁶⁰ Qq 422–423

⁶¹ Q 429

⁶² Qq 425 and 430

⁶³ Appendix 8, Case Study 3

management.⁶⁴ The British Furniture Confederation noted that most public sector purchasers held no professional purchasing qualification: in 2004 only 5% held a qualification from CIPS (the Chartered Institute of Purchasing and Supply).⁶⁵

27. We asked officials whether they accepted the criticism that the public sector was too risk averse, and imposed unnecessary bureaucracy on suppliers. Mr Fanning, Acting Chief Executive of the Office of Government Commerce, stated: “it is a myth that it is government policy to go for the lowest price; the main issue is people. The reason why people go for the lowest price is because it is easy. If you want a more sophisticated approach to generating value using whole life costing, for example, which is the policy, you need more experienced, capable, sophisticated people who are willing to make more balanced judgements.”⁶⁶ He regarded the publication of *Transforming government procurement* as marking a watershed in the Government’s approach, on the grounds that: “Prior to that date OGC acted as a body at the centre which led and advised. It was not a body that directed and held to account. Following the publication of *Transforming government procurement* we will have new powers to set standards and require departments to adhere to those standards.”⁶⁷ As an example of this change, he mentioned the standard pre-qualification questionnaire that the OGC produced as a result of research into barriers to SME participation in public procurement. Until recently, the OGC had had no power to require central government departments to use this questionnaire, but now it had the power and, depending on evidence of uptake, it would consider using that power.⁶⁸ He also explained that the OGC had re-launched the Government Procurement Service through a concerted effort to recruit and train graduates (he said that 200 such recruits were ‘going through the system’).⁶⁹

28. Even a quick glance at the OGC’s website reveals a number of guidance and help notes for both buyers in and sellers to the public sector. We discuss some of these, and other elements of the Transforming Government Procurement process elsewhere in this Report. However, no matter how good the guidance, implementation depends on both whether the people involved are able and willing to follow it and whether the authority issuing the guidance has power to review what is happening in practice and enforce compliance where necessary. On the first of these, the sheer number and variety of people involved in public procurement poses a huge challenge, and the target proposed by one of our witnesses — and which we endorse — that the majority of public sector purchasers be professionally qualified is unlikely to be fulfilled for a very long time.⁷⁰

29. However, as some of those giving evidence to us acknowledged, we think that there is also scope for potential suppliers to help. While expressing concern about purchasers’ lack of knowledge of the supply market, KPMG suggested that UK

⁶⁴ Qq 51 and 49 and Appendix 23

⁶⁵ Appendix 7

⁶⁶ Q 720

⁶⁷ Q 695

⁶⁸ Qq 742–744

⁶⁹ Q 720

⁷⁰ Appendix 7 (British Furniture Confederation)

manufacturers could do more to inform public authorities of new products and other developments.⁷¹ The OGC reported that it was collecting information not only across government on the performance of suppliers but also from suppliers on the performance of government departments, as a basis for bringing about improvements. The first market it was examining was IT procurement.⁷²

Working with the supply chain

30. Our witnesses were in agreement that one of the major difficulties in supplying the public sector was the unpredictable nature of order flows.⁷³ The CBI commented that some sectors that were very heavily dependent on public procurement were unable to cope with protracted periods of low demand and, while it was unrealistic to expect demand to be constant, “more strategic planning and more information provided to the sector so that it can plan and manage its capacity against these swings in demand would be helpful”.⁷⁴ The TUC suggested that the Government should imitate the best major private sector companies that nurtured and worked with their supply chains.⁷⁵ Several witnesses praised the Defence Industrial Strategy for providing predictions of need that made planning by the sector easier, and the TUC argued that there should be ‘healthcare’ or ‘transport’ industrial strategies along similar lines.⁷⁶ The OGC said that it was attempting to marshall public sector demand and make likely future changes in levels of demand clearer to potential suppliers.⁷⁷ One way of doing this was through the so-called ‘frameworks’, which package up smaller pieces of work into larger programmes over longer periods. These are particularly common in the area of construction. Mr Fanning described frameworks as “very good for business and for government” — a view disputed by the National Federation of Builders on the grounds that they excluded SMEs⁷⁸ — and was proud that they were now enshrined in the EU’s procurement legislation.⁷⁹

31. Some of our witnesses went further, suggesting that if public authorities engaged in early discussion of potential procurement projects with industrial partners, this would increase the authorities’ awareness of the variety of goods and services available and would help the authorities to draw up their requirements in the tender documents.⁸⁰ The EEF and CBI argued that this practice was more common in other countries, and it gave their local companies an advantage in competitive tendering as they had a clear understanding of what the procurement authorities wanted.⁸¹ However, other witnesses were concerned that such close relationships between some suppliers and the purchaser could disadvantage

⁷¹ Appendix 28

⁷² Q 748

⁷³ See, for example, Appendix 22, para 25 (EEF) and Qq 713 and 740 (OGC)

⁷⁴ Q 179 and Appendix 10, para 4.3-4.4 See also Q 52 and Appendix 23 (EEF) and Appendix 2, para 2.1 (Amicus)

⁷⁵ Q 115

⁷⁶ Qq 108 (TUC) and 177 (CBI), developed further in Appendix 48, paras 5.2–5.6 (TUC)

⁷⁷ Q 713

⁷⁸ See paragraphs 65-68 below

⁷⁹ Q 740

⁸⁰ Qq 165 and 171–172 (Intellect) and Appendix 10, para 4.2 (CBI)

⁸¹ Qq 46 (EEF) and 176–179 (CBI) and Appendix 22, para 25, and Appendix 23 (both EEF)

competitors, either simply because they did not have similarly detailed knowledge of the requirements or because the ‘insiders’ had helped draw up specifications that favoured themselves. The EEF admitted that this was a possible danger, but said that it wanted each contract to be assessed as to what would be most efficient: some large-scale, complex contracts, for example, would be better developed through such discussion, whereas it would be easy for procurement authorities to draw up the specifications for many comparatively straightforward smaller contracts without advice or further research into the market.⁸²

32. We agree that the unpredictability of order flows from the public sector creates problems for suppliers and endorse the efforts to provide more information about likely future demand. Although it is useful for purchasing authorities to deepen their understanding of the markets in which they are buying and, in some cases, to develop their contract specifications after engagement with potential suppliers, they should be aware of the danger of ‘capture’ by suppliers, with possible deleterious effects on competition in future.

Innovation and sustainability

33. Given competition from lower-cost countries, the Government is anxious to encourage manufacturing industry to develop higher value products, and to this end it aims to promote innovation. The Government could use its purchasing power to support innovation. However, we were told that, as well as resulting in bureaucratic tendering and procurement processes, risk-aversion in the public sector led to over-specification of requirements in contracts, meaning that more innovative, better value or more environmentally sustainable solutions were rejected. The argument put to us was, in essence, that government contracts concentrate on specifying exactly what is required at the cheapest price, even if this is not the best means of delivering the desired end; whereas if they specified what they wanted to achieve but not how to achieve it, this would stimulate innovation by the private sector which could potentially devise many different ways of delivering the requirement, some of which might provide better value for money over their lifetime. This is one example of an approach known as ‘Smart’ or ‘Intelligent’ Procurement.⁸³

34. The OGC emphasised to us that its advice was that specifications should be drawn up in terms of the required end rather than the means.⁸⁴ Furthermore, the Government’s Memorandum mentioned various activities designed to promote innovation and ensure sustainability in the context of public procurement: the Small Business Research Initiative, under which government departments were given the target of purchasing at least 2.5% of their R&D from SMEs; work on using public procurement to drive markets for innovative environmental goods and services;⁸⁵ the Department for Environment, Food and Rural Affairs’s Public Sector Food Procurement Initiative to highlight practical ways in which the public sector could use its £1.8 billion annual food budget to promote a world-class

⁸² Qq 58–59

⁸³ Appendix 25 (FPB) and Q 52 (EEF)

⁸⁴ Q 746

⁸⁵ Led by the joint DTI-DEFRA Environmental Innovations Advisory Group

sustainable farming and food sector; and a joint OGC/DTI project to identify and publicise best practice using as examples these schemes and the experience of other bodies such as the NHS National Innovation Centre.⁸⁶ The EEF said that, judging from research among its members, companies that had been awarded public sector contracts were significantly more likely to have increased spending on innovation than those which had not, which it argued underlined the importance of ensuring access by SMEs to publicly-funded R&D contracts.⁸⁷ We asked the OGC about progress in relation to the Small Business Research Initiative. It reported that in 2005–06, 9% of central government expenditure on procuring R&D had been spent with SMEs, exceeding both the Government’s target and the proportion achieved by the federal government of the USA. However, officials conceded both that they would like to see the UK Government achieve an even higher proportion, and that there was some doubt over whether the research projects awarded to SMEs were very innovative and whether they really would generate much economic value in wider markets.⁸⁸ The officials noted that this was likely to be the conclusion of the review by Lord Sainsbury of Turville, which has since reported to this effect.⁸⁹

35. Despite these initiatives, our witnesses considered that the Government had a poor record on promoting innovation through public procurement. The EEF cited a survey of 500 manufacturers which found that more than twice as many thought public procurement practices harmed innovation as that they promoted innovation.⁹⁰ This finding was echoed in a survey on innovation carried out jointly by the CBI and QinetiQ in 2005, in which nearly 80% of respondents thought that the Government failed to support innovation through acting as an early adopter of new ideas.⁹¹ The CBI regretted this: “A focus within public procurement on acquiring innovative products, services and processes would be a major driver for business investment in innovation.”⁹² Intellect considered that in IT procurement: “there is not an overall attitude to encourage innovative solutions — procurements are based very much on the here and now more than looking five, ten years in advance” with the result that possible developments in technology and wider benefits in terms of modernising public services were overlooked.⁹³ Intellect suggested that at present government departments did not have long enough lead-times to explore technology under development by both large multinationals and smaller niche providers and to understand “not just the capability but also the capacity of the technology industry to deliver [alternative] solution[s].”⁹⁴ The EEF recommended that in future the Technology Strategy Board should have an enhanced role in co-ordinating the Government’s research

⁸⁶ Appendix 18

⁸⁷ Appendix 22, para 24

⁸⁸ Qq 733–734

⁸⁹ HM Treasury, *The Race to the Top: A Review of Government’s Science and Innovation Policies*, 5 October 2007 Lord Sainsbury recommended that the Small Business Research initiative should be remodelled to resemble the US equivalent more closely.

⁹⁰ Appendix 21, para 23 See also Qq 45–46 (EEF)

⁹¹ Appendix 10, para 4.7

⁹² Appendix 10, para 4.6

⁹³ Q 163 in ‘Europe moves East’ [

⁹⁴ Q 164 in ‘Europe moves East’

priorities and in communicating these to business.⁹⁵ This has been recommended by Lord Sainsbury.

36. Some of our witnesses provided explicit examples of purchasers failing to think creatively either when drawing up specifications or when taking decisions.⁹⁶ Others gave examples of successful procurement, such as the decision to fit to London buses an exhaust system with very good emission-reduction properties, which had enabled the company producing the system to reach a critical mass so that it could expand into a wider market.⁹⁷ The EEF believed that innovation would be encouraged if, instead of providing very detailed specifications, purchasers in the public sector made greater use of product standards (a combination of mandatory government requirements and voluntary industry standards) to describe the desired outcome.⁹⁸

37. The DIUS agreed that there was insufficient innovative procurement, and that the main cause of this was not legal restrictions but an unwillingness by buyers to take risks.⁹⁹ It hoped that this would be rectified through improved guidance which it was compiling with the OGC, and which has since been published as *Finding and Procuring Innovative Solutions — Evidence-based practical approaches*.¹⁰⁰ One process now open to procuring authorities under the amended EU Directives was ‘competitive dialogue’ between buyers and sellers, under which the specifications were developed to reflect the buyer’s aims as a result of discussions. This was also intended to have the effect of stimulating innovation. An early adopter of the process was the Olympic Delivery Authority.¹⁰¹ The officials also referred to the role of the Technology Strategy Board in promoting innovation, giving as an example the collaboration between the DIUS and the Department for Communities and Local Government in developing an R&D programme on low environmental impact buildings, with both public and private procurement in mind.¹⁰²

38. While accepting that the public might benefit from more innovative procurement decisions, we noted the criticism that had arisen from delays and difficulties in delivering some ambitious, innovative projects, especially in the IT field, and queried whether the public sector should really be a guineapig for some types of high risk projects. Intellect suggested that much of the criticism arose from a failure to convince the public of the need to take risk by explaining what benefits they, as individuals, would gain from such projects, and from a failure to convince public servants that such projects would improve services not just replace jobs.¹⁰³

39. Mr Evans of the DIUS considered there was an objective reason why purchasers were unwilling to take risks by innovating: because it was taxpayers’ money that was being used,

⁹⁵ Appendix 21, para 25

⁹⁶ eg Q 180 (CBI) on the replacement for tax stamps on spirits

⁹⁷ Q 115 (TUC)

⁹⁸ Appendix 22, para 23, Appendix 23 and Q 52

⁹⁹ Qq 689–690

¹⁰⁰ OGC and DIUS, August 2007, at www.ogc.gov.uk/documents/finding_and_procuring_innovative_solutions

¹⁰¹ Q 747 (OGC)

¹⁰² Q 696

¹⁰³ Qq 166–167 in ‘Europe moves East’

it was considered unacceptable politically that a proportion of projects would fail, even if those that succeeded saved so much money that overall the result would be better.¹⁰⁴ Intellect accepted that if projects ‘went wrong’, civil servants were more likely to be criticised than their private sector counterparts, and that such criticism was more public. It also argued that it was far easier to name failed projects than successful ones, citing a report by the National Audit Office that had listed 25 projects which the NAO considered successful and were now taken for granted, but “the media coverage [the report] received was minimal. It is not a surprise, but that is the environment.”¹⁰⁵

40. We believe that many of those involved in public procurement are too timid, and that taxpayers may often fail to receive best value for money. This is because those buying goods and services are either insufficiently well-acquainted with the sector concerned to know or understand what options are, or could become, available, or are too afraid of failure to try anything new even if it would provide better lifetime costs or additional benefits. We were particularly struck by the evidence that, by concentrating on specifying means rather than ends, purchasers were both reducing competition among tenderers and failing to promote innovation and sustainability. We recommend the OGC to use its powers to promote best practice in this area in the course of its procurement capability reviews.

41. However, as Intellect recognised,¹⁰⁶ there will always be tension between encouraging innovation and risk and trying to ensure efficient use of taxpayers’ money. There is not, nor should there be, as much appetite for taking risks in the public sector as in the more high-tech parts of the private sector. In the latter, it is generally accepted that a certain percentage of projects may fail, and there are usually competitors who can supply alternative goods or services if one company experiences difficulties with an innovative product. In the public sector, there is much greater emphasis on public accountability for money spent, and often there are no generally-available alternatives to the goods and services being provided by public authorities. As a result any failure has a direct effect on the public, and often a disproportionate effect on the most vulnerable sectors of society. This underlines the need for those procuring innovative goods and services to work very closely with their colleagues who will use them and to have a deep understanding of the market so that they can assess risk properly. As it is impossible for all purchasers to be knowledgeable in all procurement areas, there is a need for teams of experts who could be called in to assist with specific procurement decisions. We understand that this is being developed within the Transforming Government Procurement process.

42. The UK Government’s Sustainable Development Strategy set the goal for the UK to be recognised as one of the leaders among EU Member States in sustainable procurement by 2009.¹⁰⁷ It is therefore disappointing that a particular area of criticism by our witnesses was the failure by some procuring authorities to take into account the environmental consequences of procurement decisions, in terms of both following the Government’s

¹⁰⁴ Q 690 See also Qq 691–3

¹⁰⁵ Q 169 in ‘Europe moves East’

¹⁰⁶ Qq 170 and 174 in ‘Europe moves East’

¹⁰⁷ *Securing the Future* (March 2005), Executive Summary, p2

policy of sustainable procurement and supporting new ‘green’ technologies as an early adopter. The EEF reported that its members had repeatedly lost contracts even though their products had been more energy efficient than their competitors’ because there was no ‘weighting’ for energy efficiency in the tender specifications.¹⁰⁸ Intellect suggested that the Government was not achieving as much as it could in the area of sustainability, especially in terms of ‘future proofing’. It saw the main barriers as being failures to disseminate best practice and of consistency across government.¹⁰⁹ The National Audit Office has recently criticised the Government’s failure to meet its own sustainability standards for the construction and refurbishment of buildings on the government estate, which the NAO attributed to four principal causes:

- the fragmentation of policy responsibility among government bodies and the lack of a coherent approach to monitoring progress and ensuring compliance;
- the relatively small scale of many projects (especially in refurbishment) and the fact that many of the staff responsible for these projects lacked knowledge and experience of sustainable procurement;
- the “widespread perception of a conflict between sustainability and value for money”, partly because the long term costs and benefits of more sustainable approaches were not taken into account; and
- the failure to conduct rigorous performance reviews after the projects were completed to inform appraisals for new projects.¹¹⁰

43. The Action Plan developed by the Sustainable Development Task Force and published in July 2006 cited examples of other national governments that had achieved environmental objectives and had supported innovation in their countries’ manufacturing industries: the USA’s Energy Star labelling for computers and other electronic goods; and Japan’s legislation on energy efficient purchasing which has resulted in the whole of its government vehicle fleet comprising low emission vehicles.¹¹¹ The TUC considered that, compared with the German and some Scandinavian governments, the UK Government was poor at using public procurement to promote green technologies. However, other than in the case of road transport (where it felt government vehicle purchases offered an opportunity to support the Low Carbon Vehicle Partnership) the examples given by the TUC of how the UK Government could stimulate innovation and meet environmental objectives — clean coal and water treatment technologies — related to industries where the purchasing bodies are now in the private rather than the public sector.¹¹²

44. Several witnesses suggested responses to these problems. The TUC described one model balancing risk and value for money as follows. Public sector purchasers offer to buy in the future a product or service which delivers specific environmental benefits at a specific cost. This stimulates innovation, products are made and marketed, and

¹⁰⁸ Q 46 and Appendix 21, para 23

¹⁰⁹ Q 173 in ‘Europe moves East’

¹¹⁰ National Audit Office, *Building for the future: sustainable construction and refurbishment*, HC 324 of Session 2006–07

¹¹¹ Appendix 48, para 7.6 (TUC)

¹¹² Qq 113-114 and Appendix 48, para 7.7

subsequently normal market forces determine the price and the amount of competition.¹¹³ Intellect argued that “once a tender is published it is too late” to explore the possibility of innovative technological solutions; what was needed was much earlier engagement between the technology industry and the procuring government department.¹¹⁴ Both the CBI and the British Furniture Confederation considered public sector purchasers would be justified in paying rather higher prices for locally produced goods compared with those transported over greater distances because of the savings in transport emissions; and government officials indicated ways in which this could be achieved within EU procurement rules.¹¹⁵

45. Mr Fanning of the OGC gave two recent examples of how the Government was improving procurement practice in relation to energy efficiency and sustainability. The first was a collaborative deal, led and sponsored by the OGC, which had enabled government departments to buy ‘green’ energy at no cost premium. The second was the OGC’s response to the NAO’s report on government buildings, which was to write informing the head of every government department that they were required to take part in the OGC’s property benchmarking scheme to measure the performance of all 9000 buildings on the government estate against sustainability criteria. This was intended to provide both the OGC and the Sustainable Development Commission with the information they needed to drive improvements and hold individual departments to account.¹¹⁶

46. There can be tension between achieving environmental goals and procuring goods and services at low initial cost. The OGC has produced guidance on sustainable procurement, and government departments have initiated a number of projects designed to promote innovation, environmental objectives and sustainability. Again, the problem appears to be disseminating best practice more widely. The OGC’s determined response to the NAO report on the government estate is to be commended. It will take longer to engage departments fully in the task of preventing, rather than curing, such failures. However, we believe the OGC’s approach of involving the heads of department to be the right strategy.

Social Objectives

47. Article 33 of the EU’s Public Procurement Directive, states:

“Contract performance conditions are compatible with this Directive provided that they are not directly or indirectly discriminatory and are indicated in the contract notice or in the contract documents. They may, in particular, be intended to favour on-site vocational training, the employment of people experiencing particular difficulty in achieving integration, the fight against unemployment or the protection of the environment. For instance, mention may be made, amongst other things, of the requirements—applicable during performance of the contract—to recruit long-

¹¹³ Appendix 48, para 7.9

¹¹⁴ Q 164 in ‘Europe moves East’

¹¹⁵ Appendix 10, para 4.12, Appendix 6 and Q 715, respectively

¹¹⁶ Qq 695–696

term job-seekers or to implement training measures for the unemployed or young persons, to comply in substance with the provisions of the basic International Labour Organisation (ILO) Conventions, assuming that such provisions have not been implemented in national law, and to recruit more handicapped persons than are required under national legislation.”

48. The Government’s guidance on the treatment of social issues, *Social issues in purchasing*, issued in February 2006, emphasises that, to avoid any danger of legal challenge on the grounds of discrimination, social requirements must be relevant to the subject of the contract.¹¹⁷ It also

- recommends that any social requirements should be built into the process as early as possible (“There is most scope available early on in the process, in the business case or when defining needs and specifications, and early action is more likely to be successful”¹¹⁸);
- states that social clauses must not discriminate against providers from other Member States (for example, EU case law had established that a contracting authority could stipulate that a successful tenderer must employ a certain proportion of apprentices or unemployed people provided that it did not require the apprentices or unemployed to be from a particular region or registered with a national body, thus discriminating against companies owned or based in other Member States¹¹⁹); and
- warns that purchasers should beware of making requirements too complex and onerous for fear of disadvantaging SMEs.¹²⁰

49. The guidance is very complicated, and it is obvious that the OGC foresees a large number of potential pitfalls for procurement bodies. Mr Fanning explained, for example, that the principle that any specifications had to be relevant to the contract and provide benefit to the purchaser normally ruled out simple clauses requiring the employment of local labour, but it was possible to achieve the same end without making it a requirement in the specification.¹²¹ He emphasised the need to be imaginative.¹²²

50. The trade unionists who gave evidence to us considered that the Government could benefit UK manufacturing businesses by making greater use of the various provisions in EU legislation for promoting environmental and social ends, as used by other EU Member States. They considered that, even when such provisions were carefully worded to ensure that they were not discriminatory against foreign companies, experience in other Member States showed that in practice local companies tended to be better able and more willing to comply with such requirements.¹²³ They cited the Olympic Delivery Authority as a

¹¹⁷ p1

¹¹⁸ p9

¹¹⁹ p32

¹²⁰ *Passim* All these points are also made in the Supplementary Memorandum given to us by the OGC: Appendix 54

¹²¹ Q 704

¹²² Qq 699–700

¹²³ Qq 109–110 and 118–120 (TUC), 224 (Amicus) Appendices 2, paras 3.2–3.3 (Amicus) and 48, paras 6.1–6.4 (TUC)

model.¹²⁴ The TUC suggested that local authorities were better at promoting social ends through procurement than central government, by, for example, ensuring that contractors provided apprenticeships and vocational training.¹²⁵ KPMG also thought that there was scope for public procurement agencies to use social issues to support UK manufacturers, and argued that the key need was to educate those in charge of procurement in the legitimate ways of using those provisions.¹²⁶ The CBI, on the other hand, opposed the greater use of ‘social clauses’ in contracts on the grounds that they were surplus to requirements as companies already had to comply with anti-discrimination, health and safety and employment protection legislation; these clauses hindered the primary purpose of achieving value for money and were therefore “confusing and unhelpful”; they increased the complexity and bureaucracy of the tendering process, which ran the risk of deterring SMEs in particular; and there was little evidence of social clauses benefiting business.¹²⁷ Other witnesses were also concerned about anything that added complexity to the tendering process.¹²⁸ Amicus, on the other hand, argued that it would be wrong to assume that the use of social clauses would automatically lead to greater bureaucracy.¹²⁹

51. There is clearly scope for greater use of public procurement to promote social policies such as vocational training and the public duty to promote equality. However, there are awkward legal requirements and the best practice guidance just highlights the complexity of the area and the difficulty of complying with the rules. We recommend that the Government look again at its best practice guidance to see if more helpful advice can be given as to how public authorities could pursue social policy and the promotion of equality through procurement.

¹²⁴ As did Mr Fanning of the OGC: Q 702

¹²⁵ Q 123

¹²⁶ Appendix 28

¹²⁷ Qq 183–184, Appendix 10, para 4.13

¹²⁸ eg Appendix 6 (British Furniture Confederation)

¹²⁹ Q 224

4 Barriers to SMEs

52. Government policy has been to “improve small business access to public sector procurement”, a responsibility enshrined in the then Small Business Service’s key performance indicators.¹³⁰ A study by the Small Business Service concluded that there was potential for greater innovation and competition as a result of increased SME involvement in public sector procurement, but it was reluctant to quantify such benefits in the absence of reliable data on the size of government contractors.¹³¹ The FPB, which represents many smaller businesses, argued that government could achieve better value for money and would stimulate innovation by taking action to open more contracts to competition from SMEs.¹³²

53. A substantial number of small businesses supply goods and services to the public sector. According to the Federation of Small Businesses, 24% of its members supplied local authorities directly, while the single most prominent purchaser of goods from small manufacturing businesses was the Ministry of Defence. This small business association considered that there was a “healthy participation” by SMEs in public sector procurement.¹³³ According to the Government’s Small Business Service, in 2004/2005, 58% of central government procurement contracts were awarded to SMEs. This amounted to 22% of the total contract value of central government procurement, compared to 18% in the previous year.¹³⁴ The FPB suggested that this figure of 22% was insignificant given that 99.8% of businesses were SMEs.¹³⁵ We asked the FPB whether the 99.8%/22% comparison was entirely fair, given that many SMEs operated in areas like small-scale retailing or the provision of services to households and did not provide goods or services of the sort or in the quantity that the public sector would procure. The FPB put forward another comparator, that while SMEs accounted for 49.6% of private sector GDP in 2003–04, they won 22% of central government contracts by value.¹³⁶ We consider this a fairer comparison.

54. The European Commission published data from 2001 suggesting that the UK gave fewer contracts to micro and small companies than the European average, but around 4% more to medium sized companies. Overall, the UK awarded 15% fewer government contracts to SMEs than the EU average.¹³⁷ The FPB compared the UK’s performance unfavourably with the USA’s, where for the last 60 years public authorities have been required to adopt specific practices designed to increase participation by SMEs in government contracts.¹³⁸ However, it is not clear whether the UK’s performance is

¹³⁰ DTI’s *Departmental Annual Report 2006*, p 145

¹³¹ Small Business Service, *A Study of the Benefits of Public Sector Procurement from Small Businesses*, 2005, pp 101–103

¹³² Appendix 25 (FPB) See also Appendix 29 (Leslie Kossoff)

¹³³ Appendix 24

¹³⁴ Small Business Service (2005) *Access to Public Procurement for Small and Medium Sized Enterprises Progress Report – December 2005* p. 4 In both cases the statistics exclude Health Service and Ministry of Defence spending.

¹³⁵ Appendix 25 (FPB) See also Appendix 29 (Leslie Kossoff)

¹³⁶ Qq 401–403

¹³⁷ European Commission (2004) *The Access of SMEs to Public Procurement Contracts* p. 240–242

¹³⁸ Some aspects of the USA’s approach are discussed in Paragraphs 61, 62 and 64 below For details of the USA’s procurement policy since 1942, see Appendix 25

noticeably worse than that of its competitors: the FPB said it was on a par with a number of European countries, and cited the example of France awarding 21% of government contracts to SMEs.¹³⁹ The Federation of Small Businesses reported that the UK ranked third in the EU for the number of public sector contracts awarded to SMEs, behind Germany and France.¹⁴⁰ The FPB also admitted that, following changes designed to streamline procurement processes, SME participation had fallen to 23.6% of USA government procurement contracts in 2003.¹⁴¹ There is also the question of whether like is being compared with like: one of the measures used to define SMEs within the EU is that the company has fewer than 250 employees; but in the USA small business size is defined by comparison to other companies within the sector, with the result that “a manufacturing firm in the United States can have thousands of employees and still be defined as a ‘small business’.”¹⁴²

55. While there is no doubt considerable room for improvement in the UK’s record for the award of government contracts to SMEs, evidence of how it compares with similar countries is mixed. We believe that serious efforts should be made to improve the situation in order to capture the benefits identified by the Small Business Service of greater innovation and competition.

Late payment

56. In addition to bureaucracy, complex pre-tendering requirements, unpredictability of orders, and lack of courage or vision in the taking of procurement decisions (which are problems faced by all types of companies wishing to sell goods or services to the public sector), SMEs, we were told, were specially disadvantaged by some procurement practices. One was the poor record on timely payment of bills by public authorities.¹⁴³ The FPB drew our attention to the wide variation in standards throughout the public service: not only were some NHS trusts and certain local authorities significantly worse than others at timely payment of bills (especially in relation to construction projects), but payment practices varied even within government departments, depending on the person in charge of procurement for each contract. The FPB acknowledged that payment practices were not sufficiently bad to deter its members from competing for public service contracts altogether, but they were bad enough to make companies wary of doing business with some public authorities.¹⁴⁴

57. Government policy has long been that public authorities should set a good example by paying bills promptly — a policy underlined by actions such as the Late Payment of Commercial Debts (Interest) Act 1998.¹⁴⁵ Statistics compiled by the Government show that government departments consistently fail to meet the required standard.¹⁴⁶ There

¹³⁹ Appendix 25

¹⁴⁰ Appendix 24

¹⁴¹ Appendix 25 (FPB)

¹⁴² Appendix 29 (Ms Kossoff)

¹⁴³ Appendix 25 (FPB)

¹⁴⁴ Qq 454–456 See also ‘NHS suppliers hit by late payment of bills’, *Financial Times*, 13 February 2007, p4

¹⁴⁵ C20

¹⁴⁶ Of payment within 30 days. See, for example, the figures for financial year 2005-06 in HC Deb, 24 July 2006, col 93 WS

is no excuse for this: apart from questions of justice, such exercise of power by purchasers is likely to deter potential suppliers and diminish competition. It is not clear whether departments' poor performance is attributable to inefficiency on the part of their finance departments or the perverse incentive to retain money owed in order to make their financial position appear better than it is. Whichever is true, HM Treasury has a responsibility for implementing government policy in this area; it needs to adopt a more vigorous approach and it could start by giving a better example itself.

58. While prompt payment would help sustain competition within the procurement process, the FPB made a further recommendation reflecting the fact that maintaining adequate cash-flow is often a problem for SMEs. **It suggested that there should be research to determine whether, if practices were changed so that payment could be made incrementally for work in progress, more small businesses would be able to compete for long-term contracts.**¹⁴⁷ **We consider this idea worth pursuing.**

59. The FPB also raised the problem — discussed by our predecessors in relation to the construction industry¹⁴⁸ and acknowledged by the OGC as a continuing feature of that industry¹⁴⁹ — that principal contractors often did not pass on payments to sub-contractors in a proportionate and timely manner. Our predecessors noted considerable variations in the willingness of government departments, and of individual project managers, to insist on contractual provisions requiring contractors to pass on payments to sub-contractors as and when the latter completed their work. The FPB suggested that the National Audit Office should check whether such provisions had been made in any contracts on which it was reporting. The FPB also argued that public authorities had a duty in relation to sub-contractors who were not being paid because, for example, the prime contractor had become insolvent. It suggested that there should be a clause in government contracts to the effect that, in certain defined circumstances, the purchaser could pay amounts owed directly to the sub-contractors.¹⁵⁰ **We shall return to this issue in connection with our parallel inquiry into the construction industry.**

Support to SMEs

60. The Government's initiatives to encourage SMEs to compete for government contracts included

- establishing a website (Supply2Gov) through which lower value contracts (worth less than £100,000) can be accessed. The OGC reported that, since its launch in March 2006, more than 50,000 businesses and over 3,500 public sector authorities had registered, and nearly 50,000 contracts had been published, on the website;
- the introduction of a Small Business Concordat for Local Government;

¹⁴⁷ Appendix 25 (FPB)

¹⁴⁸ Trade and Industry Committee, Second Report of Session 2002-03. *The Use of Retentions in the UK Construction Industry*, HC 127 and Fifteenth Report of Session 2002-03, *Retaining Retentions?*, HC 976

¹⁴⁹ Q 750

¹⁵⁰ Q 453

- the standardisation of the pre-qualification questionnaire for smaller contracts;¹⁵¹ and
- a training programme, piloted in the West Midlands, for SMEs in the public procurement process.¹⁵²

61. The FPB felt that, while welcome, these developments did not go far enough.¹⁵³ It said that SMEs needed more information and training on how to access government contracts, noting that in the USA this was supplied partly through the Small Business Association and partly through the government, which had paid for training for potential suppliers, both small and large. The US government had also required its primary contractors to work with their sub-contractors to improve their understanding of and ability to tender for public contracts.¹⁵⁴ On the other hand, Midlands Fashion Showcase, a regional trade association for the textile and clothing industry, thought there was scope for small specialist contractors to work together on a regional or even inter-regional basis to secure procurement contracts.¹⁵⁵ Other witnesses, such as Amicus, thought that tendering processes might be simplified further by greater use of information technology, though they did not specify which parts of the process could be improved in this way.¹⁵⁶ Conversely, the British Furniture Confederation Public Sector Working Group cautioned against e-auctions on the basis that they precluded any development of a relationship between purchaser and potential supplier, ruling out any possibility of improvements to specification or delivering environmental or other benefits additional to the specification, because they operated merely on the basis of the lowest bid.¹⁵⁷ The OGC argued that e-auctions did not have any effect on specifications or the employment of environmental criteria, etc, because they were undertaken only at the very end of the procurement process, when all other factors had been taken into account and the sole difference between bids was the price. It also pointed out that e-auctions had produced significant savings: in the half dozen or so IT projects that had been subject to e-auctions, savings of 20–50% had been achieved.¹⁵⁸

62. The FPB proposed other changes: the setting of a target percentage — not, it emphasised, a quota — of government contracts to be awarded to SMEs; ‘set asides’, limiting tendering for contracts to small businesses where, for example, the small firms in an industry are so economically dependent on one or two large companies that the small companies would be deterred from bidding if the large companies took part; limits on non-competitive tendering (or ‘preferred bidders’); more public consultation on procurement regulations; and guidelines on the use of lists of qualified bidders.¹⁵⁹ The FPB argued that several of these, together with provisions enabling ‘smart’ procurement, would be likely to

¹⁵¹ See paragraph 18 above

¹⁵² Appendix 18 and Q 711

¹⁵³ Appendix 25

¹⁵⁴ Qq 444–445 (Ms Kossoff) and Appendix 25 (FPB)

¹⁵⁵ Appendix 36

¹⁵⁶ Q 220

¹⁵⁷ Appendix 6

¹⁵⁸ Q 751

¹⁵⁹ Appendix 25; on set aside, see also Q 441

be ruled illegal under the WTO Agreement on Government Procurement ('AGP'), which was why it considered the UK should seek opt-outs from the AGP.¹⁶⁰ It denied that an opt-out could be equated with simple protectionism: the goal was to give special support to small companies, whatever the nationality of the owner or the country where the goods or services were produced.¹⁶¹ Nor did it think that any opt-out would have a significant effect on the ability of UK businesses to win public contracts abroad.¹⁶²

63. None of our other witnesses claimed that the AGP formed a significant barrier to adopting practices that might better assist SMEs to compete for public sector contracts. Furthermore, the opportunity for seeking an EU opt-out from provisions of the AGP has now passed. We, therefore, leave the issue of the AGP to one side.

64. The FPB argued vehemently that only a target for the award of contracts to SMEs would suffice to entrench best practice in the many government organisations that have to procure goods and services.¹⁶³ It suggested that the target should be set above the current level of participation but below that prevalent in the private sector.¹⁶⁴ The Small Business Service specifically rejected targets for SME involvement, arguing that case-by-case comparisons were a more effective form of analysis.¹⁶⁵ The OGC repeated the Small Business Service's view — that it was impossible to decide what the right level of SME participation was — so, by implication, a target was not only difficult to establish but also unhelpful.¹⁶⁶ In practice SMEs in the UK have almost reached the target set in the USA for SME participation in public procurement — of 23% of direct procurement and 40% of sub-contracted procurement.¹⁶⁷ Also, the target for SME participation in government-procured R&D in the UK has been not only met but exceeded, but it appears that quality — the benefits to the Government and to the companies themselves — has been more difficult to achieve than quantity. **We doubt whether the establishment of a target in relation to general procurement would greatly assist small businesses.**

SMEs and the Government's efficiency drive

65. We also examined the effects on small businesses of the Gershon programme of efficiency savings, part of which involves the centralisation and rationalisation of procurement. We have already mentioned that the OGC considered the framework approach — the bundling of contracts into larger, longer-term ones — to offer a reduction in bureaucracy and to benefit both government and business. This view was disputed by several organisations. The FPB argued that there might be economies of scale in the short run from centralising procurement, but in the long term, as potential suppliers were squeezed out of the market, there would be less competition in the supply of goods and

¹⁶⁰ Q 411; Appendix 25 gives details of the AGP Articles that may preclude specific changes to the UK's procurement rules

¹⁶¹ Qq 407–410 and Appendix 25

¹⁶² Q 412

¹⁶³ Appendix 25

¹⁶⁴ Q 405 and Appendix 25

¹⁶⁵ Small Business Service, *A Study of the Benefits of Public Sector Procurement from Small Businesses*, 2005, pp 101–103

¹⁶⁶ Q 714

¹⁶⁷ Q 405

services to the public sector, with a resulting increase in cost and reduction in quality.¹⁶⁸ The FPB gave an example of where it thought better value for money and greater competition might have ensued from the breaking down, rather than bundling up, of contracts: the provision of 69 regional interview offices for the issue of biometric passports and identity cards.¹⁶⁹ The Federation of Small Businesses also thought that SME participation in procurement contracts would be improved if the UK government imitated the practice of 93% of German and 98% of French public authorities by breaking down contracts into smaller parcels.¹⁷⁰

66. The National Federation of Builders has recently completed research which measures the impact of the efficiency agenda on SMEs in the construction industry.¹⁷¹ 460 companies responded, representing 27% of the Federation's membership. About two-thirds of these companies undertook work within the private sector, and a total of 205 companies reported that public sector work represented more than half their turnover.¹⁷² For our purposes, the most significant findings were that while 32% of companies overall reported that there had been a decrease in the volume of public sector work they had undertaken over the last five years, SMEs¹⁷³ were more likely to have experienced stagnation or a decrease, while larger companies were more likely to report an increase. All 19 companies that reported they had ceased to work for the public sector in the previous five years had turnovers of less than £10 million a year.¹⁷⁴ For all companies, the most frequently cited cause of a decline in public sector work was "changes in public procurement practices" and the second most frequent was "changes in the volume of public sector work". However, companies with a turnover of less than £500,000 were more likely to think that a decrease in the volume of public sector work was the main reason for the decline.¹⁷⁵ The Federation concluded: "This suggests that relatively smaller enterprises are disproportionately experiencing a decrease in the availability of public sector work, a situation that may have arisen as a result of the drive towards efficiency gains in public sector work (Gershon, 2004), the establishment of frameworks or a re-prioritisation of maintenance and/or small scale projects."¹⁷⁶ Also, despite the belief that frameworks would provide better opportunities for SMEs through sub-contracting, the Federation's findings were that such opportunities "have either not materialised or are not being pursued." Only 59 companies reported that they had worked as sub-contractors within a framework contract. Although 34 of the 59 were companies with a turnover of under £2 million, these were a minority (23%) of all companies with a turnover of less than £2 million that had worked for the public sector.¹⁷⁷

¹⁶⁸ Qq 439–440

¹⁶⁹ Appendix 25

¹⁷⁰ Appendix 24

¹⁷¹ *The impact of public sector procurement on SME construction companies*, September 2007 (hereafter 'NFB Report')

¹⁷² *Ibid.*, Executive Summary

¹⁷³ Defined for the purposes of the National Federation of Builders's report as companies with a turnover of less than £25 million a year

¹⁷⁴ NFB Report, pp 25–26

¹⁷⁵ *Ibid.*, p 27

¹⁷⁶ *Ibid.*, pp 46–47

¹⁷⁷ *Ibid.*, p35

67. The British Printing Industries Federation was of the view that some approaches designed to speed up procedures hindered rather than helped competition. It said the OGC had established that tenders for print services above the EU threshold typically took 12 months to complete and had developed a different system in which such contracts were broken down into lots below the threshold, and those lots were then subject to competition among companies on a list. The problem from the point of view of the British Printing Industries Federation was that the list comprised only 200 out of the 12,000 print companies and was valid for about four years.¹⁷⁸

68. Centralising procurement, bundling tenders and seeking economies of scale appear to conflict with the Government’s aim of increasing SMEs’ access to public procurement contracts. The findings of the National Federation of Builders about the overall decline in SME participation in construction work and the failure of frameworks to provide the sub-contracting opportunities hoped for indicate that it will be difficult to avoid disadvantaging SMEs (and therefore, in the medium term, reducing competition and innovation) as the efficiency drive in procurement goes ahead.

69. The FPB argued: “By far the greatest economic folly committed by government is single-sourcing. It is simply not economic not to seek as many tenders as possible for each and every contract, and yet, in many cases, preferred suppliers are used without the necessary competitive tendering process. Firstly, this discriminates against smaller businesses, and causes misallocation of resources in the economy. Secondly, a lack of or limited competition in the tendering process causes prices to be inefficiently high and wastes taxpayers’ money.” It added that the Small Business Administration in the USA had advocates working with government departments to ensure that tenders were put out to competition rather than being allocated to a preferred supplier.¹⁷⁹ In contrast, British Expertise thought that other government departments could become much more efficient in procurement if, like the Department for International Development, they allowed desk officers to purchase straightforward items of below a certain value without any form of tendering.¹⁸⁰

70. Much that the Government has been doing — improving the availability of information about contracts, encouraging local authorities to sign up to the Concordat, training both purchasers and sellers — was considered by our witnesses to be helpful to SMEs, even though in some cases they felt the Government should do more in these respects. There was far less agreement on other avenues that the Government should pursue. In almost every case, any recommendation for changes to procurement practice made by one of our witnesses was opposed by another. Procedures designed to increase efficiency were seen as harming SMEs; attempts to make contracts more accessible to SMEs as slowing down procurement or increasing costs; social clauses and environmental aims as adding bureaucracy; attempts to promote innovation as increasing complexity for the officials who make procurement decisions, or giving ‘insider’ companies advantages over their competitors. There is clearly a limit to what

¹⁷⁸ Appendix 8

¹⁷⁹ Appendix 25

¹⁸⁰ Q365

can be achieved through across-the-board changes to procedures. The focus must be on the way individual decisions are taken. There is no shortage of OGC-sponsored advice and best practice guidance on these issues. Better performance against the Government's objective of increasing SME participation in public procurement therefore depends on two things that we strongly support: better trained and more experienced personnel in charge of procurement, and a change in the emphasis of the OGC from advice to enforcement.

5 Consistency and the role of the OGC

71. The problem of inadequate expertise and experience among individual officials has been compounded by the lack of clear responsibility for ensuring that best practice is followed by the various procuring agencies.¹⁸¹ Despite the intention to strengthen the role of the OGC in public procurement as evidenced in the January 2007 paper, *Transforming government procurement*, responsibility for developing various areas of procurement practice is still diffuse. Government officials told us: “The responsibility of the policy lies clearly with the Treasury, ... but the implementation of value for money policy lies with the departments who are actually deploying the public funds”; and “Where public procurement issues are related to competitiveness or productivity in business, DTI took an interest”; while the OGC’s job is to ensure the spread of best practice; and the Small Business Service has had responsibility for increasing access by small businesses to a fair share of public contracts.¹⁸² Recently, the situation has, if anything, become more complicated. As a result of the machinery of government changes in the summer of 2007, the newly-created DIUS took over the DTI’s role in relation to the encouragement of innovation through procurement; while in April 2007 the Small Business Service ceased to be an executive agency and was absorbed back into the DTI as a policy unit (later renamed the Enterprise Directorate). It is not clear whether, and if so to whom, the agency’s specific PSA target to “improve small business access to public sector procurement” has been transferred.

72. SMEs face even greater difficulties in securing public contracts than larger businesses and, as we noted earlier, these difficulties may increase as a result of the Government’s efficiency agenda — implementation of which is no longer the responsibility of the OGC. SMEs need an obvious champion within government. At present, it is not clear which department has responsibility for protecting their interests in relation to public procurement, or whether the responsible body has the necessary influence over the many central government procurement authorities to bring about a real improvement in practice.

73. Mr Fanning was convinced that *Transforming government procurement* symbolised and continued a change in the role of the OGC that he had noticed during his three years working for it.¹⁸³ He noted that, when he had joined the OGC, the agency did not even know how much departments spent on common goods and services. The figures were now known, expenditure had been broken down into 54 categories, and the OGC was able to begin making proposals about how to improve value for money. The first areas to be tackled were energy, office supplies, travel and the vehicle fleet. Moreover, the OGC proposed to collect that information periodically to discover any changes over time.¹⁸⁴ He attributed the change to a willingness in the OGC to adopt approaches from the private sector and the commitment of all Permanent Secretaries who were keen to have OGC’s help in improving their departments’ performance. He was blunt about earlier failings:

¹⁸¹ See, for example, Appendix 2, para 2.1 (Amicus) and Q 163 in ‘Europe moves East’ (Intellect)

¹⁸² Qq 680–683

¹⁸³ A view echoed by Intellect: Qq 14–176 and 178 in ‘Europe moves East’

¹⁸⁴ Qq 715, 695 and 724

“the idea of working out where you are, working out where you want to be and charting a route from A to B and measuring movement along that route is something that you do in business every day. ... we’ve not done it in [public] procurement hitherto.”¹⁸⁵

74. Another area on which he placed particular emphasis was the decision to undertake Procurement Capability Reviews of all departments.¹⁸⁶ These were conducted by a team of independent experts who examined three main elements: leadership; skills development and deployment; and systems and processes. The team then produced a report of findings together with a list of recommendations for each department. In response, departments were required to formulate an Improvement Plan, whose implementation would be continuously and robustly monitored by the OGC.¹⁸⁷ Mr Fanning said that the first review had been of the Department for Education and Skills which, though it spent £20 billion pa, devolved this expenditure and decisions on procurement to many different bodies. The OGC could not review every contract made by each school, for example, so its focus would be on the “quality of overall procurement activity within the Department”.¹⁸⁸ Two other departments (Communities and Local Government and Work and Pensions) have also been reviewed and, as of the end of September 2007, were preparing their Improvement Plans. The reports on all three and their Improvement Plans were scheduled to be published by the end of 2007. The OGC said that the next two reviews were under preparation, with all the main departments being scheduled to undergo reviews by December 2008.¹⁸⁹

75. A further source of information was provided by the OGC’s function as an informal independent complaints authority: aggrieved suppliers could go to the OGC with complaints about purchasing departments, and the OGC now (under *Transforming government procurement*) had powers to investigate individual complaints if it felt that was warranted.¹⁹⁰ Mr Fanning summarised the situation as follows: “We have not had the tools, the instruments [to ensure that departments followed best practice] before. We are building those instruments and we intend to use them.”¹⁹¹

76. *Transforming government procurement* specifies that the OGC will have “tough powers derived from the Treasury” to:

- Set procurement policy and best practice, including performance measures;
- Audit those standards through procurement capability reviews;
- Ensure that the right incentives are in place to attract and retain those with relevant procurement skills in the public sector
- Set standard terms and conditions for procurement wherever possible;

¹⁸⁵ Qq 697–698

¹⁸⁶ Q 711

¹⁸⁷ Appendix 54

¹⁸⁸ Q 722

¹⁸⁹ Appendix 54

¹⁹⁰ Qq 720–721

¹⁹¹ Q 724

- Require departments to take up centrally-negotiated deals for certain goods and services;
- Require departments to collaborate in procurement in the “most critical markets”.¹⁹²

77. As a result of these priorities, HM Treasury placed emphasis on the development of OGCbuying.solutions, the trading arm of OGC and an executive agency which is in charge of establishing government-wide procurement contracts.¹⁹³ At the same time, responsibility for the Government’s efficiency programme has been transferred from the OGC itself to HM Treasury and “In line with this sharper focus, the OGC will be a much smaller, higher-calibre organisation” concentrating on procurement in central government, “where its levers to effect change are greatest” but continuing to make its services available to the wider public sector where this does not harm its core work on central government.¹⁹⁴

78. The OGC has been given a clearer role in leading policy on government procurement, auditing departments’ performance and improving the calibre of the procurement service. All of these are welcome. However, the main thrust of the Transforming Government Procurement agenda is to increase centralisation and impose uniformity on government departments. As we have seen, that will not necessarily deal with the problems raised by our witnesses, many of which boiled down to the need for intelligent decisions to be made on individual contracts. Moreover, the majority of public agencies — local authorities — procuring goods and services remain peripheral to the OGC’s remit and, as the OGC’s description of the procurement capability review of the DfES indicated, even the reviews of the main government departments will not really touch on the expenditure devolved to organisations like schools and hospitals. Nor could the leaner and more focussed OGC cope with a wider remit. We therefore fear that Transforming Government Procurement does not represent such a leap forward as its supporters suggest.

79. Mr Fanning of the OGC summed up the challenge: “Procurement is quite a difficult thing to do, and it is quite a difficult thing to do well. The easiest thing is always to be very rigid in the application of the rules and to always go for the lowest price. That is not where the Government wishes to be. It wishes to make full use of the flexibilities within the rules and to make full use of the general statement on value for money which is the whole life-cost that brings into balance the user requirement.”¹⁹⁵ **Thus we return yet again to the quality of the officials procuring the goods and services. Until there are enough high quality people spread throughout the public sector, in local as well as national government, the problems set out in this Report will persist.**

¹⁹² Para 2.16

¹⁹³ This agency operates mainly in two areas: framework agreements (umbrella contracts arranged by the agency with a number of suppliers under which public sector bodies can buy goods and services) and managed services (where public sector customers in effect depute specific procurement projects or areas to the agency to purchase on their behalf). The agency charges a small commission or percentage of cost to its clients.

¹⁹⁴ Transforming government procurement., paras 2.18–2.20

¹⁹⁵ Q 708

Conclusions and recommendations

1. We believe that many of those involved in public procurement are too timid, and that taxpayers may often fail to receive best value for money. This is because those buying goods and services are either insufficiently well-acquainted with the sector concerned to know or understand what options are, or could become, available, or are too afraid of failure to try anything new even if it would provide better lifetime costs or additional benefits. We were particularly struck by the evidence that, by concentrating on specifying means rather than ends, purchasers were both reducing competition among tenderers and failing to promote innovation and sustainability. We recommend the OGC to use its powers to promote best practice in this area in the course of its procurement capability reviews. (Paragraph 40)

Personnel

2. Even a quick glance at the OGC's website reveals a number of guidance and help notes for both buyers in and sellers to the public sector. However, no matter how good the guidance, implementation depends on both whether the people involved are able and willing to follow it and whether the authority issuing the guidance has power to review what is happening in practice and enforce compliance where necessary. On the first of these, the sheer number and variety of people involved in public procurement poses a huge challenge, and the target which we endorse — that the majority of public sector purchasers be professionally qualified is unlikely to be fulfilled for a very long time, until there are enough high quality people spread throughout the public sector, in local as well as national government, the problems set out in this Report will persist. (Paragraphs 28 and 79)
3. The OGC has recently been given a clearer role in leading policy on government procurement, auditing departments' performance and improving the calibre of the procurement service. All of these are welcome. However, the main thrust of the Transforming Government Procurement agenda is to increase centralisation and impose uniformity on government departments. That will not necessarily deal with the problems raised by our witnesses, many of which boiled down to the need for intelligent decisions to be made on individual contracts. Moreover, the majority of public agencies — local authorities — procuring goods and services remain peripheral to the OGC's remit and even the reviews of the main government departments will not really touch on the expenditure devolved to organisations like schools and hospitals. Nor could the leaner and more focussed OGC cope with a wider remit. We therefore fear that Transforming Government Procurement does not represent such a leap forward as its supporters suggest. (Paragraph 78)
4. SMEs face even greater difficulties in securing public contracts than larger businesses and these difficulties may increase as a result of the Government's efficiency agenda — implementation of which is no longer the responsibility of the OGC. SMEs need an obvious champion within government. At present, it is not clear which department has responsibility for protecting their interests in relation to public procurement, or whether the responsible body has the necessary influence over the

many central government procurement authorities to bring about a real improvement in practice. (Paragraph 72)

Working with the supply chain

5. The unpredictability of order flows from the public sector creates problems for suppliers. We endorse the efforts to provide more information about likely future demand. Although it is useful for purchasing authorities to deepen their understanding of the markets in which they are buying and, in some cases, to develop their contract specifications after engagement with potential suppliers, they should be aware of the danger of ‘capture’ by suppliers, with possible deleterious effects on competition in future. (Paragraph 32)

Encouraging innovation through procurement

6. There will always be tension between encouraging innovation and risk and trying to ensure efficient use of taxpayers’ money. There is not, nor should there be, as much appetite for taking risks in the public sector as in the more high-tech parts of the private sector. In the latter, it is generally accepted that a certain percentage of projects may fail, and there are usually competitors who can supply alternative goods or services if one company experiences difficulties with an innovative product. In the public sector, there is much greater emphasis on public accountability for money spent, and often there are no generally-available alternatives to the goods and services being provided by public authorities. As a result any failure has a direct effect on the public, and often a disproportionate effect on the most vulnerable sectors of society. This underlines the need for those procuring innovative goods and services to work very closely with their colleagues who will use them and to have a deep understanding of the market so that they can assess risk properly. As it is impossible for all purchasers to be knowledgeable in all procurement areas, there is a need for teams of experts who could be called in to assist with specific procurement decisions. We understand that this is being developed within the Transforming Government Procurement process. (Paragraph 41)
7. There can be tension between achieving environmental goals and procuring goods and services at low initial cost. The OGC has produced guidance on sustainable procurement, and government departments have initiated a number of projects designed to promote innovation, environmental objectives and sustainability. Again, the problem appears to be disseminating best practice more widely. The OGC’s determined response to the NAO report on the government estate is to be commended. It will take longer to engage departments fully in the task of preventing, rather than curing, such failures. However, we believe the OGC’s approach of involving the heads of department to be the right strategy (Paragraph 46)

Using procurement to promote social policies

8. There is clearly scope for greater use of public procurement to promote social policies such as vocational training and the public duty to promote equality. However, there are awkward legal requirements and the best practice guidance just

highlights the complexity of the area and the difficulty of complying with the rules. We recommend that the Government look again at its best practice guidance to see if more helpful advice can be given as to how public authorities could pursue social policy and the promotion of equality through procurement. (Paragraph 51)

SMEs

9. While there is no doubt considerable room for improvement in the UK's record for the award of government contracts to SMEs, evidence of how it compares with similar countries is mixed. We believe that serious efforts should be made to improve the situation in order to capture the benefits identified by the Small Business Service of greater innovation and competition. (Paragraph 55)
10. Much that the Government has been doing — improving the availability of information about contracts, encouraging local authorities to sign up to the Concordat, training both purchasers and sellers — was considered by our witnesses to be helpful to SMEs, even though in some cases they felt the Government should do more in these respects. There was far less agreement on other avenues that the Government should pursue. In almost every case, any recommendation for changes to procurement practice made by one of our witnesses was opposed by another. There is clearly a limit to what can be achieved through across-the-board changes to procedures. The focus must be on the way individual decisions are taken. There is no shortage of OGC-sponsored advice and best practice guidance on these issues. Better performance against the Government's objective of increasing SME participation in public procurement therefore depends on two things that we strongly support: better trained and more experienced personnel in charge of procurement, and a change in the emphasis of the OGC from advice to enforcement. (Paragraph 70)
11. Centralising procurement, bundling tenders and seeking economies of scale appear to conflict with the Government's aim of increasing SMEs' access to public procurement contracts. The findings of the National Federation of Builders about the overall decline in SME participation in construction work and the failure of frameworks to provide the sub-contracting opportunities hoped for indicate that it will be difficult to avoid disadvantaging SMEs (and therefore, in the medium term, reducing competition and innovation) as the efficiency drive in procurement goes ahead. (Paragraph 68)
12. We doubt whether the establishment of a target in relation to general procurement would greatly assist small businesses. (Paragraph 64)

Payment practices and SMEs

13. Government policy has long been that public authorities should set a good example by paying bills promptly — a policy underlined by actions such as the Late Payment of Commercial Debts (Interest) Act 1998. Statistics compiled by the Government show that government departments consistently fail to meet the required standard. There is no excuse for this: apart from questions of justice, such exercise of power by purchasers is likely to deter potential suppliers and diminish competition. It is not clear whether departments' poor performance is attributable to inefficiency on the

part of their finance departments or the perverse incentive to retain money owed in order to make their financial position appear better than it is. Whichever is true, HM Treasury has a responsibility for implementing government policy in this area; it needs to adopt a more vigorous approach and it could start by giving a better example itself. (Paragraph 57)

14. The Government should commission research to determine whether, if practices were changed so that payment could be made incrementally for work in progress, more small businesses would be able to compete for long-term contracts. (Paragraph 58)
15. We shall return to the issue of the failure prime contractors to pass on payments to sub contractors in connection with our parallel inquiry into the construction industry. (Paragraph 59)

Competing for contracts abroad

16. There is a good case for updating the Wood Review on procurement in other EU Member States. We also accept that there may be more that companies could do to fit themselves for competing for overseas public procurement tenders, such as ensuring that their agents have appropriate language skills and seeking advice from bodies such as UK Trade and Investment. The UK Government must continue to encourage the spread of best practice in procurement by public authorities throughout Europe. There is also a role for Chambers of Commerce or trade associations in helping to identify potential mentors for smaller or new-to-export companies. (Paragraph 16)

Formal minutes

Tuesday 30 October 2007

Members present:

Mr Peter Luff, in the Chair

Roger Berry	Miss Julie Kirkbride
Mr Brian Binley	Judy Mallaber
Mr Peter Bone	Mr Mike Weir
Mrs Claire Curtis-Thomas	Mr Anthony Wright
Mr Mark Hunter	

The Committee considered this matter.

Draft Report The future of UK manufacturing: public procurement, proposed by the Chairman, brought up and read.

Ordered, That the Chairman's draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 79 read and agreed to.

Summary agreed to.

Resolved, That the Report be the Thirteenth Report of the Committee to the House.

Ordered, That the Chairman make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[The Committee adjourned.]

Witnesses

Tuesday 24 July 2007

Page

David Evans, Director of Innovation, Department for Innovation, Universities and Skills, and **Peter Fanning**, Acting Chief Executive, Office of Government Commerce

Ev 1

List of written evidence

54 Office of Government Commerce

Ev 12

List of Reports from the Committee during the current Parliament

The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

Session 2006–07

First Report	Local energy—turning consumers into producers	HC 257 (HC 494)
Second Report	Work of the Committee in 2005-06	HC 332
Third Report	Stamp of Approval? Restructuring the Post Office Network	HC 276 (HC 593)
Fourth Report	Success and failure in the UK car manufacturing industry	HC 399 (HC 598)
Fifth Report	Better Skills for Manufacturing	HC 493 (HC 845)
Sixth Report	Marketing UK plc—UKTI's five-year strategy	HC 557 (HC 981)
Seventh Report	Trade with Brazil and Mercosur	HC 208 (HC 982)
Eighth Report	Restructuring the Post Office Network	HC 593 (HC 1083)
Ninth Report	Recent developments with Airbus	HC 427 (HC 1084)
Tenth Report	Strategic Export Controls: 2007 Review	HC 117
Eleventh Report	Europe Moves East: The impact of 'new' EU Member States	HC 592
Twelfth Report	The work of the Office of Fair Trading	HC 591

Tuesday 24 July 2007

Members present

Peter Luff, in the Chair

Roger Berry
Mr Brian Binley
Mr Peter Bone

Mr Lindsay Hoyle
Judy Mallaber
Anne Moffat

Witnesses: **Mr David Evans**, Director of Innovation, Department for Innovation, Universities and Skills, and **Mr Peter Fanning**, Acting Chief Executive, Office of Government Commerce, gave evidence.

Q680 Chairman: Mr Evans, Mr Fanning, welcome. Mr Evans, it is nice to see you again; Mr Fanning we are seeing you for the first time. Can I, as I always do, ask you, for the record, to begin by introducing yourselves?

Mr Evans: David Evans, I am Director of Technology and Innovation in the Department for Innovation, Universities and Skills, which, as you will know, is the descendant, the successor to DTI. I am actually speaking on behalf of that department but also on behalf of the Department for Business Enterprise and Regulatory Reform because today we felt it was more efficient if you had one spokesperson rather than two.

Q681 Chairman: Excellent. A wise decision.

Mr Fanning: I am Peter Fanning, the Acting Chief Executive of the Office of Government Commerce. We are part of the Treasury, and the OGC was set up to promote good procurement across government and to deliver value for money and, thereby, to improve quality of public services.

Q682 Chairman: Thank you very much. You know this is the last evidence session on this inquiry into public procurement, and one of the things I am still puzzling a bit about is where the ministerial buck stops. Who is ultimately responsible politically for ensuring that we get good value for money for our public procurement and effective public procurement which delivers all the other objectives of government policy we will be exploring during this session.

Mr Fanning: I shall answer that, if I may. The responsibility of the policy lies clearly with the Treasury and, therefore, with the Chancellor, but the implementation of value for money policy lies with the departments who are actually deploying the public funds. So, like many things in the public sector, there is a joint responsibility.

Q683 Chairman: The DTI used to have a very modest department that looked at these issues and the impact on business.

Mr Evans: I think our responsibility, plainly, as the Department of Trade and Industry, was government policy in relation to business, to industry and business. In that respect it is another example of this shared responsibility. Where public procurement issues are related to competitiveness or productivity in business, DTI took an interest and, perhaps in some further questioning which you will give us this

morning, I think we will be able to give you some examples of where we have been working with the Office of Government Commerce, either on the framework or on specific examples, to achieve joint objectives, both effective procurement, effective use of public money, delivering whatever the goals of the public money were and trying to support the purposes of better business and industry in the UK.

Q684 Chairman: I appreciate you are officials. I think it is a question we may well return to with the Secretary of State for the new department in due course, because we heard a lot of evidence. The industry and the trades unions all said that this was one of the most important issues for them in the future of British manufacturing, and we found it rather difficult to pin down within the old DTI exactly what was being done to ensure it was being done effectively. I think we had some concerns.

Mr Evans: I suspect that is more the responsibility of the Secretary of State for Business Enterprise and Regulatory Reform than my Secretary of State, but I am sure that John Hutton will respond positively to any request to give you more information.

Q685 Chairman: Thank you. Can I return to some of the details and begin with one of the most often heard criticisms of public procurement in the UK, which is that we interpret EU legislation more rigorously than other Member States and do not make use of the exemptions and provisions as intelligently as other countries. You have heard that said very often. What is your answer to that point?

Mr Fanning: I can reply on that. There are lots of assertions but the only piece of well-established and auditable research that we are aware of is the *Wood Report*, which I commend to you, which was published by the Office of Government Commerce and the Treasury in November 2004. It was undertaken by Alan Wood, the Chief Executive of Siemens and a leading businessman in his own right, and that reached the conclusion, which I think is very eloquently summarised in one of the quotes in the foreword of the document, in the summary of the document, which says that it is not about the rules, it is behavioural issues. So, there was a conclusion that maybe at the margin there is some difference across the European Community in the way in which the rules are applied, but there is no systematic abuse, there is no systematic under-use of the rules, and by and large the single market does work consistently across the whole of the EU.

Chairman: Most unusually, Mr Bone wants to ask something about the European Union.

Q686 Mr Bone: I was not really coming in on this one, but that response is incredible. I sit on the Joint Committee on Statutory Instruments and each week we have a pile of EU Directives that have come through that have been gold-plated. There is no question that the Government adds, rightly or wrongly, new regulations to EU Directives. Is that not the case?

Mr Fanning: We believe it is not the case, no.

Q687 Chairman: Specifically in procurement.

Mr Fanning: Specifically in procurement.

Q688 Chairman: More generally, I think it is unarguable.

Mr Fanning: Specifically in procurement, we translated, or transposed the EU Procurement Directive, the Articles in the Directive which constitute the legally enforced provisions, into UK law in a very flexible and permissive way, in a way that we understand and certainly were advised by Cabinet Office colleagues does not impose a burden, or imposes the least possible burden on industry and those who have to work within the rules. We took a choice, and I am sure you are aware of some of the discussions that have been had with stakeholders around the market, about whether the recitals, which are the non-legally enforceable parts of the EU Directive, should be included in UK regulation and therefore have the force of law; and not entirely but almost entirely, for the reasons of reducing the burden on both buyers and sellers, the recitals have not been included in the legally enforceable regulations but are interpreted through policy and guidance which enables us to respond flexibly as the world changes, as new information comes along, as technology changes and so on. We believe that we have a track record in interpreting the Procurement Directive in a way that puts the least burden on those people who have to use it.

Chairman: We could pursue this for a very long time, but I think we probably had better move on. I think some of our witnesses would be surprised by some of that. Lindsay Hoyle.

Q689 Mr Hoyle: I am also shocked, Chairman, like your good self. One cannot believe it. If you go round any European country, all ministerial cars will be a car that is produced in their own country. You want to try here. They are shipped round the world from Japan; so the procurement hardly applies in those rules. I think we can drive a coach and horses through what you have said, whether it is police cars, ambulances, you name it, I could go on forever, but let us get on. Somehow, as we have said, the playing field that we play on is completely different to everybody else in Europe, so we all have an opinion and we will have to be in some disagreement on that. Allowing for that, what are the main barriers for the Government using public procurement to promote innovation?

Mr Fanning: Perhaps I can pass that to my policy colleague here.

Mr Evans: Let me start by picking up the question of the regulatory framework, the framework of EU law. We do not believe that that is one of the barriers, we believe there is lots of scope within the legal framework for the intelligent use of the requirement for best value for competitions to promote innovation; but I would have to say also that we do not believe that there is enough innovative procurement going on, that innovation is supported enough within government procurement, but that is not the fault of the rules. For that reason what we have been trying to do is improve the guidance, improve the information that is available to procurers to allow procurers to help them approach their procurement exercise, the task of specifying goods and services, in a way which will help bring forward more innovative solutions, and we have been working closely with OGC on some guidance which is at an advanced stage but is not yet public—we expect to be able to publish it in the autumn—which will set out the ways in which we think that can be done.

Q690 Mr Hoyle: So the reality is there are no real barriers, it is just that the Government is not using or asking or requiring innovation?

Mr Evans: There are no legal barriers, the legal framework is not the key barrier. There are some barriers, I think, but they go back to some of the core barriers about improving practice in procurement, which I think comes back to the core functions of OGC—things like improving the capability of procurers, enabling a more risk-oriented approach to procurement, a willingness to take more risk. I have to say, there is an element in our political discourse which might be regarded as a barrier, in the sense that when things go wrong political inquiries often point fingers at individual officials or ministers. The political environment is not one which, I would have to say, speaking as an official, encourages risk-taking in procurement for fear that you might be pilloried for something that went wrong rather than saying that a corollary of a more innovative approach to procurement is that a proportion of your projects will not deliver fully on all their projects but the totality of the outcome will produce a better result for business overall. I do not have any answer to that and I do not point the finger, I just say that as a working official I have to recognise that is part of the world which I inhabit.

Q691 Mr Hoyle: Is it the officials that put the ministers in the deep freeze so they do not think anything other than what they are advised? Is it the ministers that we have got to take out of the deep freeze or is it the officials who are just too nervous about their own careers?

Mr Evans: I do not want to personalise this between ministers and officials, because both have interests in successful careers and look to their futures. I think some of the guidance material, some of the work OGC has done on professionalising procurement helps officials get out of that and I hope, in providing

24 July 2007 DIUS, OGC

better guidance to officials about whole lifetime costing, all of that kind of thing, this will then help ministers because if officials have got a soundly based case to present before a minister, a minister will feel comfortable accepting that case.

Mr Fanning: Perhaps I may add to that reply. The bulk of my career so far has been in the commercial world and it does feel very different if you are making a decision. In the commercial world you balance the upside and the downside. In the public world there is no upside, there is only downside—that is the way it feels—and, therefore, there is a predisposition to take, if you like, the least risk option as opposed to the option that gives you the greatest upside but actually, correspondingly, has a significant downside. This is particularly the case when you are making investment in new technologies or new processes and so on. Certainly talking to my Permanent Secretary colleagues, one of the observations that they make is that if they are presented with two options, one that is very attractive but risky against one that is tried and tested but may be less attractive, the tried and tested is the one that they would personally tend to prefer.

Q692 Mr Hoyle: No risk departments. That is what you are saying.

Mr Fanning: Pardon.

Q693 Mr Hoyle: They are called no-risk departments?

Mr Fanning: Well, life is full of risk. I am merely making the observation that if you are given two options, the tendency will be to go for the lower-risk option, simply because of the consequences to you as a department, and so on, whereas in the commercial environment, I believe in my experience it feels as if you can take a much more, dare I say, calculated risk, in the sense if there is a potential for upside you will be rewarded for delivering that.

Mr Evans: Might I add, I certainly do not think there is any difference between the character of people who work in the Civil Service or in the public sector and the people who work in business, because we have examples of people who move both ways; neither do I think it is in any way a positive intention of the political process to create that; but I think it may be simply a consequence of public life. If you are doing things in the public service, you are rightly subject to more scrutiny than if you are operating within a company because you are using tax-payers money to spend on these things. So, in some ways it is a corollary, it is one of the crosses in some sense we have to bear, but it is right that we should be subject to more scrutiny than private business.

Q694 Mr Hoyle: My worry is that people coming in from the commercial world get sucked into the system and do not change it, because nothing changes?

Mr Fanning: We try to.

Mr Hoyle: But, obviously, it is not happening. I leave it there.

Chairman: It reminds me of those terrifying words from Yes Minister, “That would be a courageous decision.” The ultimate warning!

Q695 Roger Berry: One area where there is less uncertainty in relation to outcomes is that of energy efficiency and sustainability, where Government has clear policy objectives and yet many organisations, not least the National Audit Office, have pointed out that Government is failing to use the public sector to make progress in those areas. How does Government use public procurement to promote energy efficiency and sustainability?

Mr Fanning: Perhaps I can make a stab at that one. I am trying to find the appropriate word, but you can perhaps help me. I was a witness at the PAC recently on sustainable buildings and I had the opportunity at that hearing to say on this very day we made an announcement of an extremely large—I cannot remember the exact figure—energy deal that gave government departments an opportunity to buy green energy at no premium, and it was an example of collaborative procurement at its best. That is an example of the sort of transaction that OGC is increasingly leading and sponsoring. Perhaps I can use this opportunity to remind you that *Transforming Government Procurement* was published in January of this year, and that marks a watershed in the Government’s approach to managing public procurement. Prior to that date OGC acted as a body at the centre which led and advised. It was not a body that directed and held to account. Following the publication of *Transforming Government Procurement* we will have new powers to set standards and require departments to adhere to those standards. One of the first areas of work where we are investigating where that might be possible is in the area of energy, looking to how we can marshal the Government’s energy demand in a way that generates good value in a sustainable way.

Q696 Roger Berry: You mentioned buildings but, as you know, the National Audit Office recently produced the report *Building for the Future*. They said the Government has set sustainability standards for construction, refurbishment of buildings on the Government Estate, and they looked at some of the projects and found that in 80% of the cases the Government was not meeting its own standards.

Mr Fanning: Yes. Partly in response to that, using the new powers available to me under this document, this policy statement, I wrote to all departmental heads, all Permanent Secretaries and Accounting Officers, requiring them to participate in the OGC’s property benchmarking scheme, which will enable us to measure the performance of all 9,000 holdings on the Government’s Estate, and one of the dimensions we will be measuring is the building’s sustainability, its performance against sustainability measures, water recycling, energy efficiency, waste recycling, and so on. So we will have the information to enable us, firstly, to work out where we are and then to map a journey from where we are to a better place, and you will have the opportunity to use that information in holding

departments to account because the information will be made available to the Sustainable Development Commission.

Mr Evans: Might I add something about the slightly more forward-looking take on exactly the same question? The same document about public procurement policy talked about the role of the Technology Strategy Board, working with the OGC in looking at developing new technologies which will be able to meet the challenges of the future so as to allow business to supply into more demanding targets, and energy efficiency is one of those areas where the Government has set, as you will know, very challenging targets for housing for 2016, zero-energy housing. As part of the work of my department, we have actually been developing a research and development programme on low environmental impact buildings with the Department for Communities, which will help underpin the creation and delivery of technologies both in the public sector and the private sector (because these issues span both) over the coming ten years where we are working with the procurers as well to make sure that the way we specify an R&D programme—this is R&D activity so it is looking to the creation of new technologies—feeds more easily into the procurement activity, whether it is public procurement or private procurement for the future. So, that is in some sense a different dimension to the way in which we can tackle the problem, because we can help create new technologies which, over the next ten years, will provide the answers.

Q697 Roger Berry: Would it be fair to summarise Mr Fanning's view as being, "Well, it has been a bit chaotic in the past, but we now have a framework that will hopefully address this so that the NAO will not produce any more reports like that", or am I putting words in your mouth?

Mr Fanning: You are not putting words into my mouth. It is a way, I think, of summarising eloquently what I was trying to get across. I think it is right that people are held to account, that is what I am used to in a commercial environment. Indeed, in response to the question earlier on, people who move from the commercial environment into public service do bring techniques, ideas and principles with them, and the idea of working out where you are, working out where you want to be and charting a route from A to B and measuring movement along that route is something that you do in business every day.

Q698 Roger Berry: It is the sort of issue we do in the public sector as well, but—

Mr Fanning: Well, we have not done it in procurement hitherto.

Q699 Judy Mallaber: I have got two DTI memoranda to this Committee for our inquiry on the future of the manufacturing industry, one on public procurement, one on skills shortages. I may have missed it, but I cannot see any reference at all within those to the issue of equalities, even though a huge area of the potential skills that we are not using

relate to the fact that women do not get the place that they should do in relation to industry, in relation to the occupations they are in, and similarly other disadvantaged groups. Does the Government use public procurement at all to promote its equality agenda?

Mr Evans: Do you want to talk about the social clauses first of all and I will see if there is anything to be said about—

Mr Fanning: Yes, the first thing is that there is no prohibition to using public procurement equality provided it is consistent with value for money and other components of policy. Indeed, again, if you will forgive me, in answer to that question OGC, working with colleagues across government, produced this *Social Issues in Purchasing*, which I do believe covers how you can use—

Q700 Chairman: I do not think we have seen that document.

Mr Fanning: I can ensure you get a copy. It has been in circulation for a time, I think, but I would be delighted to circulate it to the Committee, and that deals in some detail with what can be done. Perhaps if I can just try and dispel one of the myths, and that is that the rules are constricting. In fact our judgment is that the rules are, in fact, permissive and flexible and there is a lot you can do within the rules provided you are imaginative, and one of the challenges I would offer to public bodies is to work with us and with other colleagues on individual transactions to see what can be done to promote policy, but I stress again, consistent with value for money and the other components of the regime.

Mr Evans: I apologise for appearing a bit bureaucratic, but I am afraid I think the equality agenda is no longer a responsibility of DTI and was not a responsibility of DTI for the last six months—I think it went to the Department of Communities—and so I simply have not briefed myself on that issue. I can procure an answer for you subsequently, but I am afraid that on the specific question of what has or has not been done on the equality agenda I have not covered.

Q701 Judy Mallaber: But there is now a duty on public authorities to promote equality in relation to gender?

Mr Evans: Yes.

Q702 Judy Mallaber: So although we are saying it may not be a specific DTI responsibility, that is a responsibility on all government departments. Mr Fanning, you said that there was no prohibition, which is helpful because we got rather bureaucratic answers when we were at the EU in relation to some of those issues, but are you saying that, as far as you are concerned, there are up to now no positive steps that have been taken to positively promote equalities, because, clearly, in relation to asking questions of those people that are putting bids in on what their equalities policy is and then expecting them to promote those objectives is something that we should be able to do. Does that not happen at all at the moment?

24 July 2007 **DIUS, OGC**

Mr Fanning: I believe it does. I think, for example, the ODA, which is the non-departmental public body which is delivering the Olympic programme, the infrastructure—

Mr Evans: The Olympic Development Authority.

Mr Fanning: The Olympic Development Authority, it will be essentially using public money to buy the infrastructure that is necessary to deliver the Olympics. From memory, they have set out a statement of the principles underlying their procurement policy and I do believe that it does say that they intend to promote equality, both race and gender, as working with their suppliers, but, again, they do add a caveat inconsistent with the general value for money and compliance regime within which they have to work. So my short answer is, yes, people are buying using tax payers' money and when they buy they are having regard to these other objectives.

Q703 Judy Mallaber: But at the moment that is not within the guidance that is given to procuring sections of departments that they should take that into account?

Mr Fanning: I am trying to find examples in this document here, and, again, I apologise, I should have briefed myself on that particular question a bit more thoroughly, but it does say, "The main social issues covered in this note are", and I go through them, and it does say "gender equality and race equality" and, indeed, it does give an example here. It is an issue of race equality and it says, "In an ethnically diverse area, a local authority would want to ensure that information about its services was accessible to all racial groups", and to answer the authority might choose to outsource a help desk and it might specify that in that help desk people need to be able to speak the languages that are used by the community in that area, and that would be an example of how you can achieve your race equality objective through public procurement.

Q704 Judy Mallaber: Finally, at the moment is there any prohibition to requiring the make up of the workforce?

Mr Fanning: Yes, there is. I am sorry to interrupt you, but we are getting into fine points of rules as they apply to individual contracts and, when you are buying anything, you put in the specification, which is the device you usually use to achieve, if you like, non-value for money outcomes, by thinking through very carefully your specification and setting out what you are trying to buy, and there is great flexibility in the specification. However, it has to be relevant to the contract and providing benefit to the authority, and that is where, for example, local labour clauses are usually not relevant to the contract and do not provide a benefit to the authority. However, with imagination, and there are examples in this document, you may have the effect of being able to achieve non-value for money objectives. Most of your work force could, in fact, be locally based, but you cannot actually put that as a requirement in the specification.

Q705 Chairman: I suspect you are pushing too hard on this. As you have frankly and honestly admitted, you have not briefed yourself thoroughly in this area. I think I am going to ask you to send us the document you are referring to; also to give us a clearer written statement of what the issues are around this. I think that would help us to make progress.

Mr Fanning: I would be delighted to.

Q706 Chairman: And clarify in our minds exactly what you are saying, because I am a little more confused than I was when you began.

Mr Fanning: I do apologise.

Q707 Roger Berry: Would it be helpful also if you could give some examples of where the equality agenda has actually made a difference?

Mr Fanning: There are some in this document.

Roger Berry: In passing, since last December there has, of course, been a public sector duty to promote equality for disabled people, which has applied, of course, to DTI as well as everybody else, although on the DTI website, I have to say, I would not have noticed, but it is not your fault.

Q708 Judy Mallaber: The question of whether it is a disadvantage to the authority not to promote those duties might also be one that you could comment on in your submission.

Mr Fanning: I would be delighted to do so, yes. Perhaps I can make a general statement, which might help navigate a way through this. Procurement is quite a difficult thing to do, and it is quite a difficult thing to do well. The easiest thing is always to be very rigid in the application of the rules and to always go for the lowest price. That is not where the Government wishes to be. It wishes to make full use of the flexibilities within the rules and to make full use of the general statement on value for money which is the whole life-cost that brings into balance the user requirement.

Q709 Chairman: We are going to go through that in more detail. Let me finish this session by saying it may be helpful if, before you write your note, you discuss with the clerk some of the issues and evidence about this particular issue to make sure that you are addressing fully the issues that have been raised with us as a committee in the policy inquiry.

Mr Fanning: I would be delighted to do so.

Q710 Mr Binley: Can I touch on the whole question of procurement and SMEs?

Mr Fanning: Yes, of course.

Q711 Mr Binley: Because I think about 22% of contract value in 2004-05, which are the last figures we have got, went to SMEs, although that represented 58% of total numbers of contracts, and I understand that. The other point I would make is that overall the UK gave 15% fewer government contracts to SMEs. We have got a problem that the Government wishes to solve but that we are not solving very successfully at all, quite frankly. I want

24 July 2007 DIUS, OGC

to touch on three areas. The first is cultural. It does seem to me that you made the statement that there was no difference in terms of the upside of risk between the private and the public sectors and that there had been change-overs that made you believe that to be the case. Can I first ask you whether the truth of the matter is that most of the people you deal with are from UK Plc, who become more and more bureaucratic by the year, and that is why you think there is no difference, when in truth there is a massive difference in the SME sector, which is the most creative sector of British industry where most of the new innovations come from and where all the job growth is coming from?

Mr Fanning: There are a number of items in that. My first point is that OGC works very closely with the former DTI to try and increase the participation or remove barriers to participation of SMEs within public contracts. We did some research—it is a little old now, it is about four or five years old, but it is quite intensive research—in the West Midlands and also in East London, in Haringey, and based on that evidence we came to the conclusion that the barriers faced by SMEs are largely to do with the capability on the buying side and on the selling side and also on information. We responded to that. There was a training programme that was enacted in the West Midlands for training both buyers and sellers in public bodies there. In *Transforming Government Procurement* there is a programme of improving the performance of buyers right across government. We have relaunched the Government Procurement service. We have got Procurement Capability Reviews of all departments. We have done two, there is a third one that will be completed soon and that will drive performance on buying across government, and also we have, with our colleagues in DTI, launched a website *Supply2.gov*, which will enable smaller contracts to be advertised.

Mr Evans: Shall I give you a little more information on that. The *Supply2.gov* website was launched in March 2006 to allow both public sector organisations (i.e. the procurers, and the people wanting to supply small businesses) to get better access to one another, and it is predominantly targeted on the lower value and the smaller procurement opportunities less than £100,000 specifically with the objective of making it easier for small businesses to do that. Since that launch over 50,000 buyers have registered—that is predominantly small businesses who are potentially trying to get business—and over 3,500 public sector contracting authorities have registered and since the overall launch nearly 50,000 opportunities have been published. We continue to want to grow this as an opportunity, but it is an example of the joint activity between OGC and DTI to try and help small businesses get access to government procurement.

Q712 Mr Binley: Gentlemen, I have to tell you that the question I asked you has not been answered at all, and it was a question of cultural barriers. You maintained that you felt that there was no difference in cultural terms, particularly with upside of risk, between private and public sectors. I asked you

whether that was because you mostly deal with UK Plc, which are quite bureaucratic organisations, and I talked specifically about SMEs which tend to be much less bureaucratic. Will you please answer that question?

Mr Fanning: I shall. I must have been unclear. There is a difference between the culture of the public sector and the private sector in my experience. In the private sector you are certainly rewarded for upside very, very significantly.

Chairman: I think Brian is asking about the difference between big businesses and smaller businesses.

Q713 Mr Binley: Exactly that.

Mr Fanning: I have worked in leadership positions in both large organisations and small organisations and my judgment is that there are many myths about smaller organisations. My main observations about small organisations is that they are small and that, therefore, it is very difficult to get anything done because the management there is very thin, the management band-width is very narrow, the experience of people at the top of the organisation is usually very constrained. They are desperately anxious about where the next deal is coming from. They have, for example, less fixed costs available to win bids as a proportion of total sales that would be the case in a larger organisation, and what they really want from government, certainly what I wanted from government when I was a managing director of a firm selling right across the public sector, both in this country and abroad, was stability of demand. We can cope with competition, but what we found very, very difficult was stop and go, and that is one of the issues that we as OGC are trying to address in marshalling public sector demand, putting greater visibility to the market so that they can deliver to the public sector in the most advantageous way possible.

Q714 Mr Binley: Let me move on. You have talked about assessment of progress and I have heard a little of that. Clearly, much more assessment needs to be done to understand whether you are on the right track or not, because I have not really heard very much that convinces me that you do know whether you are on the right track in regard to the Government's targets to involve many more SMEs and sell much more ability to SMEs to take part in procurement than you are doing at the moment: because it does seem to me the Government does want you to go out and sell to Outreach and to get people involved. I am not sure how you are doing that. You say you have got a website. What else are you doing?

Mr Evans: Can I take half a step back just before I answer the specifics and give some more examples of what we are doing. What the Government is completely clear about is that it wants small businesses to be able to compete better for business. So it wants to be able to improve the ability of small business to engage in public programmes to meet the needs, for exactly the reasons you have said: the fact that small businesses can be more innovative. You

24 July 2007 DIUS, OGC

can find good and bad small businesses in the same way you can find good and bad big businesses, but you can find a lot of innovation, a lot of flexibility, a lot of benefit with small businesses, and if our systems of procurement are in some way biased against small businesses, we will be losing out as well as the small businesses. That is the fundamental point on which we agree with you, but I do not think we have actually said that we know that the level of participation that we have currently got in terms of the current participation of small businesses in public procurement is too small or too big, because I do not know how we would decide whether or not what in absolute terms the right level is, but what we certainly want to do is to make the market more competitive, actually help small businesses participate. What else have we done? The Regional Development Agencies have helped train more businesses; I have talked about the website; the local authorities have been encouraged to sign up to a concordat to make their own procurement more small business friendly; there has been a range of guidance improvement, process improvement activity which we have done with a range of different public authorities coming from the DTI side, working with our colleagues, to help small businesses get business off government—

Q715 Mr Binley: Would it be very unfair if I said that the impression I am getting is that whilst you are in line with government thinking, you wish to improve, your assessment of where your systems actually are is pretty poor?

Mr Evans: I am afraid I do not have the data. I do not know whether Peter has the data.

Mr Fanning: I think that we are in a much better place now than we were when I first joined OGC, to be blunt about it. I now, for example, know that we spend about £75 billion a year on common goods and services. We can analyse that into 54 different categories of spend. We are going to develop plans for driving value out of those categories, category by category, in a systematic manner. The first four pilots are in energy, office supplies, travel and fleet, and we will do our best make sure that we have a level playing field for SMEs and increase to make sure that there are as few barriers to SME participation in those contracts as we possibly can. However, my job is to drive out value for the tax payer, and that is what I shall do. I will give you an example perhaps of where, using the specification, you can achieve, if you like, a social outcome by using the principles underlying the EU procurement rules, and that is, for example, in the area of food. You can specify, for example, if you are a hospital or a prison or whatever, that you want food to be of a certain freshness. It needs to be available, very, very fresh, and the effect of that is that it means that local suppliers have an advantage over those who have to take their food over longer distances, using refrigeration and chemicals to keep it fresh. That is an example where you can level the market. If a large supplier, of course, chooses to set up a big farm beside a prison, that is the way the markets operates.

Chairman: Can I just say, we are making rather painfully slow progress, so if I can make the usual plea from the Chair of the speaker: short questions and answers as far as we can.

Q716 Mr Binley: Can I ask you to us send us some real examples of assessment and monitoring, because I have still yet to hear what you are doing in that respect. Can I ask a final question? I have made the point about the Europeans being more successful in this respect than we are and, indeed, there are suggestions that the approach taken there is the reason why they are being more successful. That is not very difficult. The systems they use to get to SMEs and to offer them the opportunity is a more successful system. Have you looked at that and are you thinking about tweaking our own processes to improve in that way?

Mr Fanning: I can reply on that. We have looked at it. We have produced the Wood Report.

Q717 Mr Binley: That is five years ago?

Mr Fanning: It is five years ago, and there are no plans, but perhaps that is something which I will suggest my successor reviews.

Q718 Mr Binley: Are you leaving them?

Mr Fanning: I am the Acting Chief Executive.

Mr Binley: I understand that now. Carry on.

Q719 Chairman: That is it, is it?

Mr Fanning: I think there is a good case. We will have to discuss it with our ministers for the Wood Review to be revisited.

Chairman: Thank you. We want to make slightly faster progress. Judy Mallaber.

Q720 Judy Mallaber: Mr Fanning, you said earlier that Government did not just want to go for the lowest price, but obviously that is still the very widespread criticism we receive, that they do just go for the lowest price rather than broad value for money considerations. How are you addressing this problem, particularly in light of constraints on public spending?

Mr Fanning: The first thing is, it is a myth, and I will repeat that, it is a myth that it is government policy to go for the lowest price, the main issue is people. The reason why people go for the lowest price is because it is easy. If you want a more sophisticated approach to generating value using whole life costing, for example, which is the policy, you do need more experienced, capable, sophisticated people who are willing to make more balanced judgments. What we are doing is trying to drive up standards across government in procurement, firstly through reinvigorating the Government Procurement Service, for example, which has been re-launched recently, and we have got graduate recruitment going on with about 200 people passing through the system at the moment. Secondly, we are also holding departments to account for the quality of their procurement activity. As I said, we have had two completed reviews of government departments' capability in procurement and we will be publishing

the first three of those reviews in the autumn. Finally, we have a complaints function which is something that, again, may be unknown to you because it is fairly new and we had a soft launch, but OGC has now launched an informal independent complaints function, so should aggrieved suppliers believe they have an issue they want to take up with Government but they are uncomfortable about going directly to the purchasing department, they can come to us and we will deal with it.

Q721 Judy Mallaber: When you say you can deal with it, what authority have you got with the purchasing departments? Can you go in and do a sample of the contracts they are putting out and say, "That's not good enough, you've got to change it"? What are your powers?

Mr Fanning: Our powers are quite considerable inside *Transforming Government Procurement*. I think we would have to see what was appropriate in the circumstances of the individual complaint but, in principle, if it did require us to undertake an investigation, if the evidence merited it, then I am sure we would consider that.

Q722 Judy Mallaber: Do you just respond to complaints or do you go and look periodically at how they are doing their contracts and say, "Look, you're not doing the specifications right" or "You're not taking account of all the factors"?

Mr Fanning: That will be the subject, yes. The short answer is, yes, the Procurement Capability Reviews will do that. However, I would make the point that in the Procurement Capability Reviews we have to have regard to the scale of some of these. For example, the Department for Education and Skills, which was the subject of the first pilot, spends £20 billion a year. I do not think we will be reviewing all of the contracts they do, not least because many of them are executed inside the educational sector and, therefore, there is a very large number of them. What we will be looking at is the quality of the overall procurement activity within the Department.

Q723 Judy Mallaber: If, for example, the MoD comes back to you and says, "It's soldiers on the frontline and more equipment or getting this cheaper, but maybe cutting some of the corners on specifications, you might want to look at", how do you respond to that?

Mr Fanning: I do not want to be drawn into hypothesis but we do expect to undertake a capability review of the MoD's procurement capability next year where that issue may arise.

Q724 Roger Berry: To pick up on what Judy was saying, we have been told that some government departments are frankly better at procurement than others. The Ministry of Defence is usually held up as one department which is good at procurement, which begs the obvious question, what are you doing to ensure that the public sector is more consistently good at procurement? In fairness, to some extent you have been talking about that, but how big a

problem is this diversity of practice? Apart from reviews, what can you do? What are you doing to try to have uniform best practice?

Mr Fanning: Again, drawing on my experience from the commercial world, you have to start measuring things. You have to work out where you are, work out where you want to be and chart a course from A to B and we are doing that in a way which we have never done before. I gave examples of what we now know about common spend, that we propose to collect that information periodically and systematically so that we can build up a picture of how things are changing. This is the first time these Procurement Capability Reviews undertaken by departments have been done and over time they will drive up performance. One thing I can give you an assurance on is the Permanent Secretary community are, in the argot, up for it. They look to OGC to help them improve the performance of their own departments. We have not had the tools, the instruments before. We are building those instruments and we intend to use them.

Q725 Roger Berry: When did that process start?

Mr Fanning: I think it started initially with Sir Peter Gershon's report in 1999; he created OGC. In its early years, OGC was focused on leadership and advice and a lot of changes were made. Sir Peter Gershon, to pay him credit, generated a fantastic brand. What we have learned through the Efficiency Programme is you can drive change right across the public sector but it does require the hard grind of setting targets, agreeing plans, monitoring performance against those plans and intervening where you get an adverse variance and we are doing that now.

Q726 Mr Hoyle: Quickly on procurement. You obviously said you did not want to get into hypothetical defence issues, but there is a good case of army uniforms which were made in the UK and were put out to China to a Chinese factory, state owned, unfair competition, how do you end up in a position like that? That is not hypothetical, that is fact.

Mr Fanning: I am sure it is fact, but my job is to deliver value for money for the British taxpayer and I have no reason to believe that the MoD did anything other than seek to get value for money when they made that procurement decision. If there is any other evidence to the contrary, I would be delighted to have a look at it.

Q727 Mr Hoyle: Obviously we gave away our technology advantage on camouflage because it did have special infrared to ensure that you could pick out the camouflage of our troops and we actually gave that information away, so there is a whole issue to be taken into account. I will give you another one then. How do you end up with ministerial cars, Toyota Prius, driving around which have been shipped all the way around the world from Japan?

Mr Fanning: Firstly, I do not know that they are shipped.

24 July 2007 **DIUS, OGC**

Q728 Mr Hoyle: They are, they do not make them here in this country.

Mr Fanning: Is that right?

Q729 Mr Hoyle: Absolutely, so I cannot understand how procurement rules work and do not work.

Mr Fanning: The first point is the Prius cars were procured through a deal which OGC helped to broker. For the first time we have managed to require the whole of the government fleet is now sustainable, so what we are doing is creating demand in the UK for sustainable cars.

Q730 Mr Hoyle: Sustainable, what do you mean by sustainable?

Mr Fanning: I am not an expert on fleet, so I am advised by—

Q731 Chairman: I do not think we should get into the details of this, but I think many of us would regard the Toyota Prius as being unsustainable rather than sustainable.

Mr Evans: Can I intervene a little bit to remind you that Toyota does, indeed, have a very significant manufacturing capability in the UK in the North East albeit, you are quite right, they do not produce that particular vehicle in the UK. They have made a major investment in the UK and, therefore, like many multinational companies, they do different things in different countries.

Q732 Mr Hoyle: That is nonsense, is it not?

Mr Evans: I have to put my wider DTI hat on here and say, yes, of course we want to sustain UK technology, yes, of course we do want to support companies which manufacture in the UK and, yes, of course we do want to advance our own industries' capability, but it is not true that the only way to do that is to buy British. There are varieties of different ways in which we can sustain it. The work we will be doing, which I described in relation to the sustainable buildings, the low environmental impact buildings, we have got a similar activity which we will be launching with the Department for Transport on low emission vehicles where I am sure we will be engaging with Toyota and other car manufacturers. The programme has not been launched yet, so we have not got the specifics in place to make sure that all of those manufacturers in the UK, whether they are Toyota, Ford, GM, whoever it is, produce vehicles which will be more able to meet the demands on the world market.

Chairman: We only have another 14 minutes and we have six or seven questions to go.

Q733 Mr Hoyle: Chairman, I must say, that is absolute utter nonsense. If you had not been shipping cars from Japan all the way around making the biggest carbon footprint with ships where one pollutes more than any aircraft, the fact is they might have been now producing in the UK. It is because you are willing to accept the mean ship that they have got away with it. It is absolute nonsense, and this is at the expense of British jobs and British technology. Everything you said at the beginning

has been thrown out with the baby and the bath water. To move you on to something else, R&D. Why have previous efforts to enable smaller companies to gain access to publicly funded R&D contracts failed?

Mr Evans: I think you are talking about the Small Business Research Initiative, SBRI. The original proposal was to ensure that of the totality of government procurement for R&D—this is very specific, this is procurement of R&D—a significant proportion would be done with small businesses. The figures which I have got for 2005-06 say that the total quantity of extramural R&D by central departments—this is very much Whitehall central department focused—was £2.6 billion and, of that, £225 million, that is 9%, was spent with small businesses. I have to say, that does not seem to me to be an absolute failure, notwithstanding the fact that I would like to see that small business proportion go higher. I think there is also a good case to say that not enough of that £225 million spent with small businesses is at the kind of leading edge products and leading edge services which will generate value going forward in the wider markets. That is not just my view, it is also David Sainsbury's view. Lord Sainsbury was asked last November by the Chancellor to do a review about innovation policies and he is well advanced with that review, although the report has not been published yet, it will not be published until the autumn. I know that he is very keen that we take further action to push the SBRI harder to use central Government R&D budgets to procure more of the kind of leading edge R&D which will get new products and services on the market. I am afraid, because his report has not been delivered to me or anyone else, I cannot tell you when we will get to that.

Q734 Mr Hoyle: Why has the US been more successful?

Mr Evans: The interesting thing is the US analogue of this talks about 2.5% of central Government. The figure we have got in the UK is already 9%, so there is a question about whether or not it is more or less successful. The more subtle and more difficult question is whether the right kind of small business R&D is being done under our 9%. That is the point David Sainsbury is referring to, but, I am afraid, you will have to wait a little bit before I can give you further answers to that. There is the issue of exactly what we do about it, I think we will have to wait and see and, indeed, we will have to find out exactly what David Sainsbury says.

Q735 Chairman: We will have to move on, but did you give us a date for when Lord Sainsbury is likely to report?

Mr Evans: I am speaking on behalf of another department, the Treasury, but I understand it is likely to be in the autumn, after the holiday break. You will not have to wait very long.

Q736 Mr Bone: I want to ask you a couple of questions about bureaucracy but, first, I must go back to something Mr Hoyle said. Is it not the truth

that these Toyota cars, or whatever they are, are a pure government gimmick and a stunt? Procurement had nothing to do with it and it is all to do with political stunting? As officials, should you not have been telling the Minister, "Don't do this, this is bad procurement"?"

Mr Evans: I am not going to comment, Peter can comment on that last point if he wants to, but he may well wish not to. If you go to the US and you ask the US car companies whether or not Toyota did a good thing by getting out in front with a whole new technology, the hybrid engine technology, and producing a vehicle five years ahead of GM, they will say, "Toyota did a brilliant piece of marketing because they got to a technology which will dominate cars".

Chairman: I am sorry, we are moving on from Toyota because we have not got the facts, but I think the Committee disagrees with you.

Mr Hoyle: What is not being pointed out is that those cars are being built in America.

Mr Bone: Could we have a note on how that decision was made?

Q737 Chairman: I am very happy that we should ask for a note on the Toyota Prius decision.

Mr Fanning: I would be delighted to produce that.

Q738 Mr Bone: Manufacturing companies, and I used to run a manufacturing company, certainly the vast majority believe that government procurement principles and procedures are a hindrance rather than a help. Am I right in that?

Mr Fanning: That may be their view but we do not think they are.

Q739 Mr Bone: What are you doing to remove bureaucracy from those procedures? One example will do.

Mr Fanning: Firstly, we are training our people so they can apply the rules in the most effective way possible.

Q740 Mr Bone: That has not removed anything yet because you are just training them. I want to know what you have actually removed? What is going to be better for my company if I was supplying clocks to government now? What have you reduced which I did not have to put up with before?

Mr Fanning: The reason I am hesitating is because, in my judgment, again having supplied to government, so I am in the same position that you are, the rules are not the issue, it is the cost of bidding which is the problem. That is more to do with the way the rules are applied by the people who are applying them and less to do with the rules themselves. The second point is when I was running a business the thing which I cared most about was the stability of demand. One thing we are trying to do, as I said, for the first time is trying to marshal our demands in a way which gives the suppliers much visibility on where the deal flow is coming from. The other thing we are doing is we are extending the use of frameworks. I am sure you are aware that one of the achievements of the recent EU directive

negotiations was that the previous and widespread use of frameworks within framework contracts, which are very good for business and for government, within British procurement is now brought formally within the EU regime. That will have the effect of effectively reducing burdens on business.

Q741 Mr Bone: You have obviously bid for government contracts as well and you know that you get this huge tender document and you think to yourself, "I'm a small business, that is going to cost me X thousands of pounds to do against what might be a million pound contract". One part of that tendering document, perhaps at the front, is all the pre-tendering qualifications and what amazed me was if I was selling clocks to British Rail in those days as part of a nationalised industry I could get on that list but then if I wanted to sell it to somewhere else I had to get pre-approved again.

Mr Fanning: It is crazy, is it not?

Q742 Mr Bone: Once you are pre-approved, why are you not on one list of pre-approved government suppliers?

Mr Fanning: A couple of things. Firstly, we have produced a standard prequalification questionnaire as part of the work we did in the West Midlands and that is on our website and is available to anybody who wants to use it. Secondly, we have got *Supply2.gov* which lists on it a large number of modestly sized government contracts, I think it is under £100,000, and as part of that process it should be easier for small businesses to bid for those contracts at lower bidding costs.

Q743 Mr Bone: Yes, but that £100,000 is really, really small, I am talking about a medium-sized company which is doing £5, £10 million of business. If you go through this wretched thing once, you have got all the equity, you are competent and all that sort of thing, once you have done that, why do you have to go through it again for a different department? Why can you not have a list saying if you are approved there is your stamp mark and somebody can look you up and say you have been approved?

Mr Fanning: It is a very good point and I would simply have to agree with you that more can be done in that. As I said, what we have done so far under the old regime is produced a standard prequalification questionnaire which is on our website and we do endorse, encourage and promote its use. What we did not have was the power to require departments to use it. I now have the power to use it and I will consider applying that power. Whether I will or not will depend on the evidence but I will consider using it.

Q744 Chairman: Can I be clear whether that power would extend to all central Government departments, non-departmental public bodies, public corporations, whatever status they have, all of central Government departments?

Mr Fanning: Yes, all of central Government.

24 July 2007 DIUS, OGC

Q745 Chairman: That is helpful. That report which I skimmed and did not form a very high impression of, more pious platitudes and aspirations, you are putting a lot of faith on that, are you not?

Mr Fanning: Yes. It is published by the Treasury but it is a government document. It was approved by a Cabinet Committee.

Chairman: I would not want to anticipate what the Committee will recommend in this respect, but I think Mr Bone made some very powerful points during his questioning.

Q746 Anne Moffat: My question is about developing good relationships with suppliers. We have been told that by the government being over-prescriptive in its specs that it is often failing to achieve the best solution. What is your view of this? Should we leave it to the suppliers to say what they need and government to be more specific?

Mr Fanning: You have a point that certainly our advice is that specification should be in output form rather than input form, so, therefore, you should say what you are trying to achieve rather than what you are trying to buy.

Mr Evans: I think that is a particular issue in relation to promoting innovation within the context of procurement, because if you specify the means by which something must be delivered, the end is going to be achieved, you are going to prevent the person who has got a different way of delivering it—a more efficient or a potentially cheaper more effective way which will achieve some wider goals as well, whatever those wider goals may be—from being eligible to bid and you will prevent innovation. This is one of the areas where we join forces and say, “If you want to promote innovative procurement, you really ought to be specifying the outcomes, or maybe some outputs, rather than the means by which it should be achieved”. For that reason, OGC and DTI as was my department, have been working on some specific guidance for procurers. You may say this is yet more guidance, but unless we provide the information to procurers we cannot expect them to behave in the way we want them to, to explain to them how that objective end way of procuring is, in our view, the right way to get more innovation in the whole procurement process.

Q747 Anne Moffat: You think that is clearly stated to the suppliers that is what the objective is?

Mr Evans: My day job, so to speak, is to promote innovation. I do not think there is as much innovation in the UK economy, full stop, as there should be, and public procurement is one of the areas where I would like some more innovation, yes.

Mr Fanning: Indeed, one of the innovations which was achieved in the recent EU directives was the competitive dialogue process which is designed to enable a dialogue to occur between the buyer and the seller so that you increase the opportunity for a conversation between the buyer and the seller, which hopefully will result in a more innovative response to the buyer’s requirements. It is very new and we are observing its application. I am pleased to say that one of the first enthusiasts using this new facility was

the ODA, the Olympic Development Authority, and we are studying how they are getting on and seeing if we can improve on it, so it will be a way of stimulating innovation.

Q748 Anne Moffat: Thank you for that. We have heard from the manufacturers that they would like better guidance from government sooner rather than later about procurement needs and they would like to be involved in the consultation with industry. Do you believe that industry should be part of the process?

Mr Fanning: Absolutely. Indeed, one of the developments which we have now established is much more effective dialogue between the supply community and the buying community. For example, what we now do is OGC collects information on the performance of suppliers right across government. Also, we are collecting from suppliers their views on the performance of departments. It is called the 360 Degree Comprehensive Assessment Framework. Hopefully what that will do is begin to identify where departments could be doing better or suppliers could be doing better. One of my colleagues is being targeted on ensuring that over a period of time we have a measurable improvement in the quality of the dialogue we have with our major suppliers. The first market we will be looking at is the IT market because of the very sizeable spend in that market and the importance of that market to delivery of a lot of the major government programmes.

Q749 Chairman: It is also where you have heard a lot of particular criticism as well?

Mr Fanning: Absolutely, yes, so we hope progress is being made on that.

Q750 Anne Moffat: A further small point. Do you think that would discriminate against SMEs in any way because of their lack of resources?

Mr Fanning: To a certain extent, there is always a risk in that and it is a risk we need to guard against. I would not want for you to take away any suggestion that there is any sort of complacency on that side. The reality is, particularly in the IT sector, very large organisations are needed to deliver very large projects. One thing we do have regard to, however, is the supply chain, and one of the things we will be launching very soon in another market is fair payment. The Government is to support the fair payment policy which will have the effect of hopefully improving the lot of small subcontractors to larger primary contractors in the construction market where the primary contractors make some of their profits out of aggressive cash flow management and denying the payment on time to the subcontractors for the work that they have done.

Mr Evans: Let me say, from the ex-DTI perspective we certainly do not believe that good procurement is in any way inimical to the interest of small businesses. We think good procurement, good procurement processes, more efficient, more professional procurement processes can help SMEs get business just as much as big business.

24 July 2007 DIUS, OGC

Q751 Chairman: We have heard quite a lot about e-auctions as a way to encourage SMEs into the market. Does that not rather go against the innovative agenda, which you were talking about, and the whole life cost, because it is always going to drive the lowest cost solution, is it not?

Mr Fanning: Perhaps I could talk a little bit about e-auctions. Firstly, the application of e-auctions is at the end of the procurement process, not the beginning. The first stage in preparation is differentiating between bids and you refine them to a point where the only thing which differentiates the proposition is the price or, in rarer cases, something which is measurable and is easily quantifiable and that is when e-auction comes into play. What I can say is the public sector is capable of getting very, very substantial savings. For example, we have done between half a dozen and a dozen e-auctions in the IT market where savings of between 20% and up to 50% have been got on a standard lot. The other final point I am making is the public sector is a very occasional user of e-auctions compared with my colleagues in the private sector. I would not want to go on record suggesting that the private sector is supplying bad services to its customers simply because they are using e-auctions, it is simply a

device and it is a device which can be used in rather narrow circumstances, but it can generate value for money for the taxpayer where those circumstances arise.

Q752 Chairman: That is helpful. Thank you. That answers my question. We have given you a slightly tough time today probably, but I think you have also been very honest about the shortcomings of the history of public procurement. Perhaps some of that toughness from our questioning reflects our frustration with the failures in the past, on which I think you have been very frank. Thank you very much indeed and good luck in whatever your future career holds. How long have you been there?

Mr Fanning: I am towards the end of my third year at OGC.

Q753 Chairman: As Acting Chief Executive?

Mr Fanning: I have been there as Deputy Chief Executive and Acting Chief Executive. I shall be handing over to Nigel Smith and I commend him to you.

Chairman: We may well see him because we will be looking at these issues in the context of construction industry as well particularly in our next inquiry. Thank you very much indeed, gentlemen.

APPENDIX 54

Memorandum submitted by the Office of Government Commerce

THE FUTURE OF THE MANUFACTURING INDUSTRY: PUBLIC PROCUREMENT

I am writing to provide the Committee with the information it requested when it took evidence from my predecessor, Peter Fanning, and David Evans of the Departments for Innovation, Universities and Skills (DIUS) and Business, Enterprise and Regulatory Reform (BERR) on 24 July 2007.

1. SOCIAL ISSUES IN PUBLIC PROCUREMENT

The Committee asked for clarification on what can be done in the procurement process to promote social issues, with particular reference to equality.

All public procurement work within the legal and policy framework as laid down by EU law and the Government's procurement policy. It is the responsibility of Departments and other public bodies to ensure compliance with this framework. The EU rules consist of the EU Treaty, that is, the Consolidated Treaties of the European Union, including the Treaty on which the public procurement rules are based, known as the "Treaty establishing the European Community" (with broad principles of equal treatment, non-discrimination and transparency) and the EU Procurement Directives (which reinforce the Treaty provisions and set out detailed requirements for contracts above certain thresholds). In conjunction with these EU requirements, the Government's procurement policy is that the purchase of all goods and services should be based on value for money, defined as: "the optimum combination of whole life cost and quality to meet the user's requirement".

Within this legal and policy framework, there is scope to consider social issues—including equality—where they are relevant to the subject of the contract and in line with value for money policy. There is most scope at the beginning of the procurement process, when defining the requirement and setting the business case. At this stage, contracting authorities should consider which social agendas or obligations—including equality legislation—are most relevant to their procurement, and where appropriate, they should also consult interested parties eg users of the goods or services, small businesses (including ethnically-owned businesses) and interest groups, who may be able to help shape the requirement more effectively. This should ensure that all relevant social issues, including equality considerations, are reflected as appropriate in the specification. Contracting authorities may also consider whether the contract is appropriate to reserve for supported factories and businesses (organisations with over 50% disabled employees).

There is also scope to take account of social and equality issues at the selection stage (where contracting authorities select candidates that they intend to invite to tender). Candidates can be asked for relevant evidence of technical capability eg language skills or cultural awareness, and contracting authorities can consider suppliers' track record on delivering the social aspects of other, similar contracts. This is also the stage at which candidates can be rejected if they have been convicted of an offence concerning professional conduct or grave professional misconduct that could include a breach of the equality laws.

At the award stage, the contract should be awarded to the tenderer offering the best value for money goods or service. Social issues can be taken into account where they are relevant to the subject of the contract, but award criteria must be relevant from the point of view of the contracting authority in that they must determine the best value for money bid for the contracting authority itself—wider benefits must be considered earlier in the procurement process. They also have to be consistent with the EU Treaty principles outlined above. In addition, where there are two or more bids precisely equal on value for money grounds, it is possible to use “additional social award criteria” to determine between the equal bids, although legal advice should be sought first.

Social and equality considerations can be included as contract conditions provided they are relevant to the subject of the contract and do not undermine the performance of the contract or the achievement of value for money for the taxpayer.

I should point out that there are wider issues around the use of social contract conditions which should also be taken into account when considering their relative merits. Public sector contracts are sometimes criticised for their length and complexity, and including numerous contract conditions related to social issues can add to this, undermining efforts to make public procurement more accessible to certain groups such as SMEs and black and minority ethnic and women owned enterprises. Contract conditions should therefore not impose requirements that do not bring a proportionate benefit and care must be taken to ensure that they are non-discriminatory, and that value for money is being maintained.

Generally, laws relating to social, environmental and employment obligations are not highlighted in contract conditions, because contractors should be acting legally regardless of a contract term specifying this. However, at ministers' behest, an exception was made when the Race Relations Act was introduced, to include a reference to the law on racial equality. This concept has more recently been extended, in the model terms & conditions that we encourage departments to use, to cover other areas of equality—gender and disability—as well as health & safety.

There are also specific equality duties in place—the Disability Equality Duty, Gender Equality and Race Equality Duty—which require public authorities to have due regard to the need to eliminate unlawful discrimination on these grounds and to promote equality of opportunity. In public procurement, these Duties require public authorities to consider whether any of these equality issues are relevant to their requirements and where they are relevant, to reflect them within their specifications in a non-discriminatory manner.

Where these duties exist, they do not apply directly to the private sector. However, where a contracting authority is contracting out a public service, and an equality duty applies to parts of that service, relevant obligations may need to be passed to the contractor. These obligations, because they relate to the performance of the contract, should be included in the contract conditions.

I believe Peter gave you a copy of our guidance to departments “*Social Issues in Purchasing*”, which has further details. OGC produced it in consultation with the European Commission and colleagues across Government. Here is the link. http://www.ogc.gov.uk/documents/Social_Issues_in_Purchasing.pdf.

I would also like to draw your attention to Annex A of this letter which includes a practical example of where equality has been considered in public procurement, which is largely in accordance with the best practice framework described above.

2. PROCUREMENT CAPABILITY REVIEWS

In regard to the assessment and monitoring public procurement, OGC sets the standards against which Departments are judged. Our Procurement Capability Reviews (PCRs) identify capability gaps and examples of excellence, helping Departments to build procurement capability. PCRs look in detail at three main elements of a Department's procurement activities: leadership; skills development and deployment; and systems and processes. The PCRs represent an independent strategic view of procurement in its widest definition across the department and its wider network. The reviews are conducted by a team of high calibre independent experts. The review team produces a report of findings and prioritised recommendations for each department. To address the issues raised, Departments are required to formulate an Improvement Plan, with OGC engaged in continuous and robust follow-up, to ensure that improvement is achieved.

Three departments (Department for Education and Skills, Communities and Local Government and Department for Work and Pension) have so far had PCRs. Feedback on all three has been delivered to Permanent Secretaries. The Departments are at varying stages of preparing Improvement Plans. The reports and Improvement Plans are scheduled to be published by end-2007. We are currently preparing for the next two reviews (Department for Transport and Department for Environment, Food and Rural Affairs), with all major departments scheduled to undergo reviews before December 2008.

3. PURCHASE OF TOYOTA PRIUS

We agreed to provide you with clarification on the decision to purchase Toyota Prius. The Government Car Dispatch Agency (GCDA) in October 2005 carried out a full review of cars appropriate for Government Ministers. The objective was to provide a reasonable choice of vehicle for Ministers within the guiding principles laid down in the Prime Minister's Guidance, "Travel by Ministers". The review took into consideration fitness for purpose, whole life operating cost, compliance with EU emission requirements, country of build and conformity with end of life regulations.

The Toyota Prius was approved by the Cabinet Office as a suitable vehicle and included on the official list of cars. The whole life operating cost made the Toyota Prius very competitive with the exemption from the congestion charge, the low maintenance cost, the low fuel consumption and the high residual value. The very low exhaust CO₂ emissions made the Toyota Prius a very attractive vehicle for a high profile government fleet. In addition, the Toyota service levels were comparable to those of other major manufacturers. The Toyota Prius therefore fulfilled the requirements of fitness for purpose in the GCDA review.

I understand that the Committee were concerned about the impact on UK car manufacturing. The Government is working on a number of initiatives to help enhance the UK automotive industry. Cenex is a Public Private Partnership set up by the Department for Trade and Industry (now the Department for Business, Enterprise and Regulatory Reform) in 2005, with a mission to build a competitive advantage for automotive industries in the UK through a shift to a low carbon economy. It is working on the creation of fleet-scale demonstrators in the passenger car, public transport and commercial vehicle market sectors and on providing more certainty on future demand (Forward Commitment public procurement model) to encourage market transformation.

I hope this clarifies the issues raised during the discussion on 24 July and that this provides the Committee with the information they require.

Annex A

THE OLYMPIC DELIVERY AUTHORITY'S APPROACH TO PROMOTING EQUALITY THROUGH PROCUREMENT

1. INTRODUCTION

1.1 This paper looks at how the Olympic Delivery Authority (ODA) has integrated equality and diversity into its approach to procurement. It outlines the ODA's mission, objectives and priority themes. It demonstrates the overlap between the ODA's legal duties to promote equality and its legal duty to consider, in carrying out its functions, how it can maximise its impact on the legacy of the Games. It then goes on to show how, through its balanced approach to procurement, the ODA has been able to cascade its objectives and priority themes into its procurement process, and pay due regard to its legal duties in respect of equality and legacy.

1.2 This case study focuses on the promotion of equality through procurement. The ODA's balanced approach to procurement deals with wider issues such as sustainability, employment, skills and training as well (see Figure 3 below).

2. THE OLYMPIC DELIVERY AUTHORITY

2.1 The Olympic Delivery Authority (ODA) was established by the London Olympic Games and Paralympic Games Act 2006 (the "Act") and started business on 1 April 2006. It is an Executive Non-Departmental Public Body (NDPB) accountable to the Secretary of State for Culture, Media and Sport.

2.2 The functions of the ODA, defined by the "Act" are to do anything necessary for "the purpose of:

- preparing for the London 2012 Olympic Games and Paralympic Games,
- making arrangements in preparation for or in connection with the use or management before, during or after the Games of premises and facilities acquired, constructed or adapted in preparation for the Games, or
- ensuring that adequate arrangements are made for the provision, management and control of facilities for transport in connection with the London Olympic and Paralympic Games."

2.3 In exercising its functions, according to the "Act", the ODA must have regard to a number of things, including the "desirability, wherever relevant, of maximising the benefits that may be derived after the Games from its preparation, whilst contributing to sustainable development".

2.4 In exercising its functions the ODA, like all public bodies, is also bound by statutory duties to promote equality which require it to have due regard, in carrying out its functions, to the need to promote race equality, disability equality and gender equality. These duties are summarised in Annex A.

2.5 The overall vision for the Games, agreed by the Olympic Board¹ is “to host an inspirational, safe and inclusive Olympic and Paralympic Games and leave a sustainable legacy for London and the UK”. The four strategic objectives that underpin that vision are:

- To stage an inspirational Olympic Games and Paralympic Games for the athletes, the Olympic Family and the viewing public.
- To deliver the Olympic Park and all venues on time, within agreed budgets and to specification, minimising the call on public funds and providing for a sustainable legacy.
- To maximise the economic, social, health and environmental benefits of the Games for the UK, particularly through regeneration and sustainable development in East London.
- To achieve a sustained improvement in UK sport before, during and after the Games, in both elite performance—particularly in Olympic and Paralympic sports—and grassroots participation.

2.6 The ODA’s mission is “to deliver venues, facilities, infrastructure and transport for the London 2012 Olympic and Paralympic Games on time, to budget and to leave a lasting legacy”.

2.7 There are three overarching themes that drive and define the success of the ODA:

- Time
- Cost
- Fit for purpose

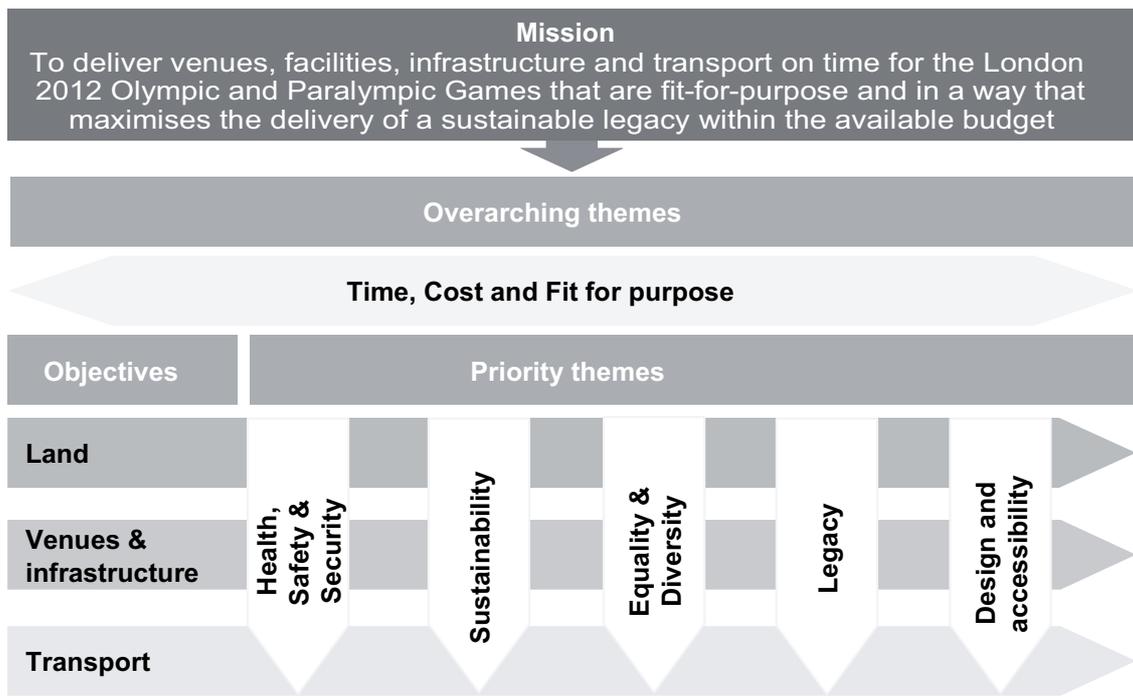
2.8 Five further priority themes underpin the ODA’s mission, existing within the constraints of the three overarching themes:

- Health, Safety & Security
- Sustainability
- Equality and Diversity
- Legacy
- Design and Accessibility

2.9 Figure 1 summarises the ODA’s mission and the themes emphasised in delivering its objectives.

Figure 1

SUMMARY OF THE ODA MISSION AND APPROACH



¹ The Olympic Board comprises representatives of the Department for Culture, Media and Sport, the Greater London Authority, the London Organising Committee for the Olympic Games and Paralympic Games and the British Olympic Association. It is jointly chaired by the Secretary of State and the Mayor of London.

2.10 The ODA has identified five pillars of legacy, which it is working with partners to achieve:

- Sporting legacy, through delivery of new sporting facilities, increased participation, health and awareness of personal responsibility for well-being in the UK.
- Physical legacy, through the regeneration of the Olympic Site, including the provision of new homes, employment space and landscaped parks and waterways.
- Economic legacy, through the creation of new jobs, a better skilled workforce and local business growth.
- Legacy for the UK, through increased tourism, enhanced image and cultural developments arising from the Games.
- Social legacy, through having a positive impact on the people in the communities affected.

3. IMPACT ON EQUALITY OF THE PROCUREMENT PROCESS

3.1 The promotion of equality is highly relevant to the economic and social legacy of the Games. The communities in the five London Boroughs surrounding the Olympic park are among the most diverse in the UK. In the UK nearly 8% of the population is from non-white ethnic groups, compared to nearly a third (29%) of London's population, and four out of 10 (42%) of the population in the five Host Boroughs. Table 1 below shows the representation of each ethnic group in the five boroughs, London and the UK.

Table 1

PERCENTAGE OF EACH ETHNIC GROUP IN TOTAL POPULATION OF UK, LONDON AND THE FIVE HOST BOROUGHES

	<i>UK</i>	<i>London</i>	<i>Five Host Boroughs</i>
White	92.1%	71.2%	58.0%
White British	*	59.8%	49.2%
White Irish	*	3.1%	2.2%
White Other	*	8.3%	6.6%
Mixed	1.2%	3.2%	3.3%
Asian or Asian British	4.0%	12.1%	20.0%
Indian	1.85%	6.1%	5.3%
Pakistani	1.3%	2.0%	4.0%
Bangladeshi	0.5%	2.2%	9.0%
Other Asian	0.4%	1.9%	1.7%
Black or Black British	2.0%	10.9%	16.1%
Black—Caribbean	1.0%	4.8%	6.4%
Black—African	0.8%	5.3%	8.4%
Other Black	0.2%	0.8%	1.3%
Chinese or other	0.8%	2.7%	2.7%
Chinese	0.4%	1.1%	1.1%
Other ethnic group	0.4%	1.6%	1.5%

(Source: ONS Census 2001)

*The sub-categories of white which were offered to people in England & Wales during the 2001 census differed from the sub-categories offered to people in Scotland. People in Northern Ireland were not offered any sub-categories of white.

3.2 Black, Asian and minority ethnic people are significantly under-represented in the construction workforce. They are only three per cent of UK construction workers, compared to 7.9% of the UK's population. The same patterns occurs in London, where BAME people are just 14% of those employed in construction (compared to 29% of the population) and in the five Host Boroughs where BAME people are just 24% of those employed in construction (compared to 42% of the overall population)².

² Source: Labour Force Survey, Spring 2004

3.3 Women are also severely under-represented in the construction workforce, constituting only 10.4% of the UK construction workforce as a whole, and only 1.2% of the manual workforce in construction³.

3.4 In accordance with its statutory duties to promote equality, the ODA assessed its potential impact on race, gender and disability equality, and found that its direct impact will be felt in four ways:

- Through what it builds, provides and leaves behind; that is, the extent to which the design of the park and venues, and the transport network provided, are truly inclusive and accessible.
- Through how it goes about building and providing; that is, the extent to which the processes used to let contracts and employ people are demonstrably transparent, open and fair.
- Through who does the work of building and providing; that is the diversity of people and businesses taking up business and employment opportunities on Games projects.
- Through whom the ODA involves; that is, the diversity of people the ODA listens to in deciding what it does, how it does it and determining the design of what it creates.

3.5 The ODA also identified two indirect impacts it can have on equality, by demonstrating to others:

- Effective practical steps which can be taken to promote equality and diversity in construction.
- The level of excellence which can be achieved through inclusive design.

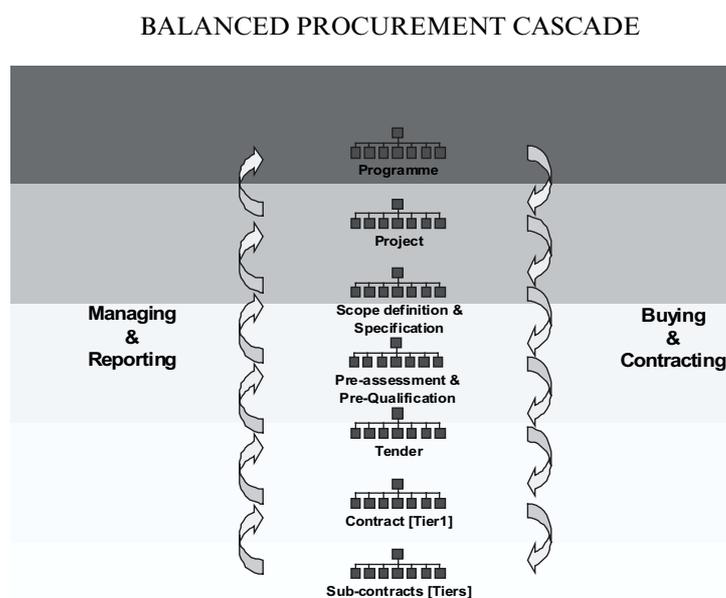
3.6 The ODA believes that the delivery of these positive impacts on equality can contribute greatly to the achievement of its duty to maximise the benefits that may be derived after the Games.

3.7 The ODA's procurement process has a critical role to play in relation to ensuring equality of opportunity in access to employment opportunities and business opportunities.

4. BALANCED PROCUREMENT

4.1 The delivery of the 2012 Games is a major undertaking, necessitating the procurement of a wide range of goods, services and works. In total the ODA will procure several billion pounds of expenditure. The ODA's procurement strategy is based upon a "Balanced Procurement" approach (see Figure 2 below) which establishes clear linkages from the Corporate Plan and Objectives down to the sub-contractor working on a site. This gives the ODA the basis for balancing differing priorities such as cost, time, safety, sustainability, equality and diversity, security, legacy etc.

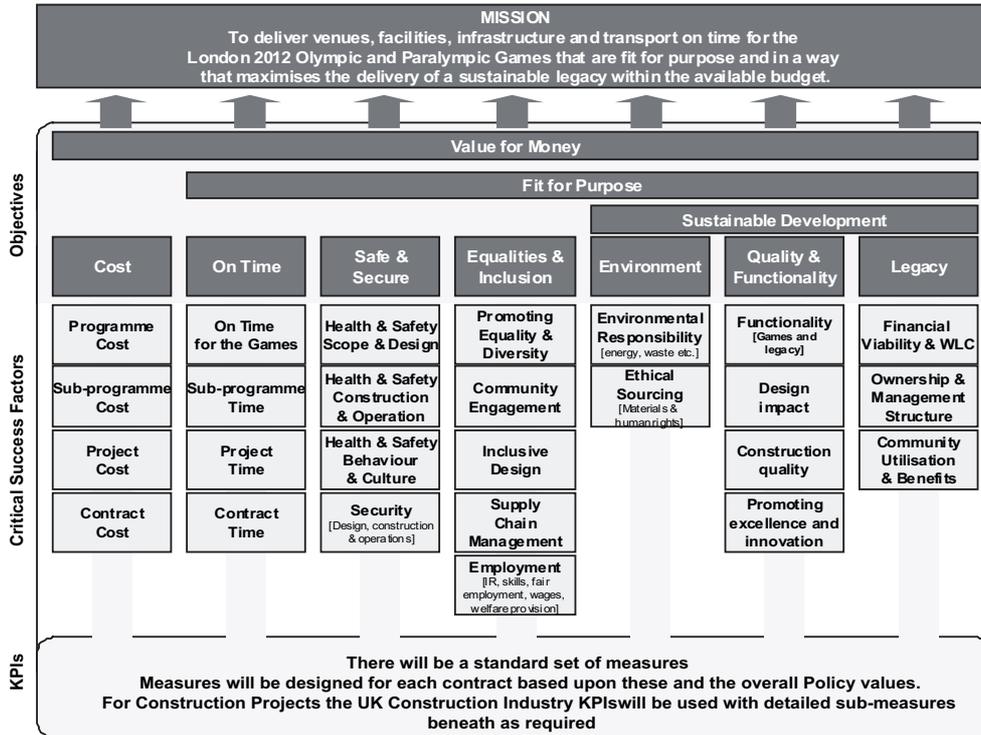
Figure 2



³ Source: Labour Force Survey, four quarter average, Summer 2005 to Spring 2006 inclusive

4.2 The balanced scorecard (Figure 3) is used as the framework through the procurement exercise, included in the Memorandum of Information, Pre-Qualification Questionnaires and tender documents. Contractual obligations are cascaded down the supply chain, whilst actual performance data is collated and clustered going up the chain.

Figure 3
PROCUREMENT BALANCED SCORECARD

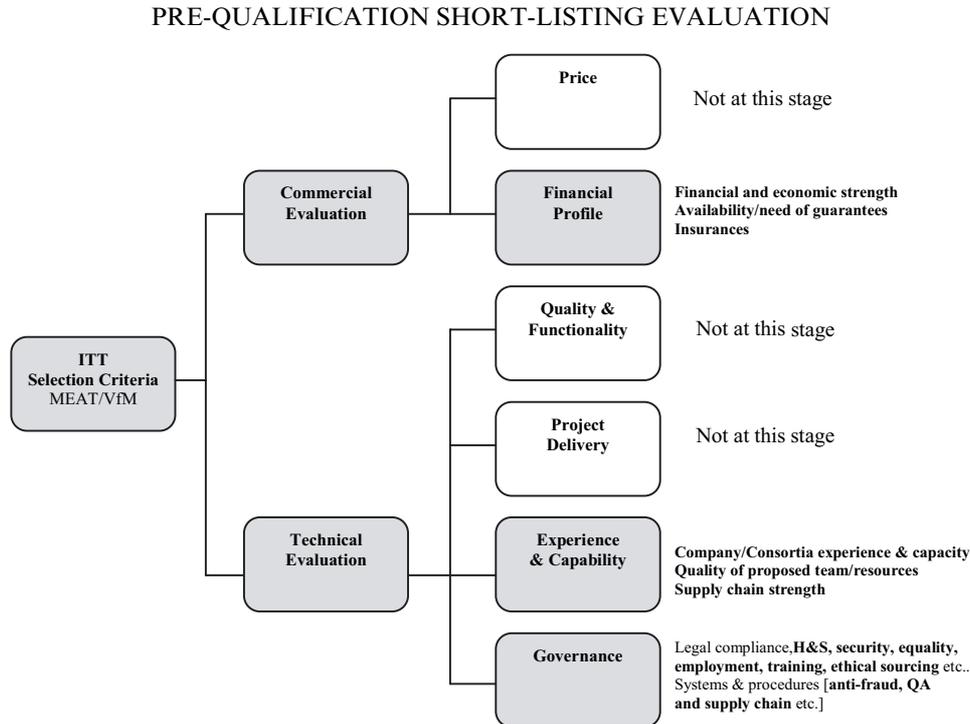


5. EVALUATION OF EQUALITY AND DIVERSITY AS PART OF SELECTION PROCESS

5.1 Equality and diversity forms one part of the technical evaluation at both PQQ and ITT stages, as part of the evaluation of governance capability of all companies bidding for contracts with the ODA.

5.2 The pre-qualification process involves openly advertising for bidders and then short-listing the applicants using a pre-determined set of criteria. These criteria are: legal compliance and governance matters, economic and financial standing, and technical or professional ability (see Figure 4) below:

Figure 4



Note: Yellow boxes are included at PQQ evaluation stage

5.3 At PQQ stage the equality and diversity evaluation focuses solely on the existing policies and procedures of the company, to ensure compliance with the statutory requirements. The evaluation looks at six areas of equality-related policy, all taken from the relevant statutory codes of practice on employment published by the Commission for Racial Equality, the Equal Opportunities Commission and the Disability Rights Commission. Companies are asked to answer simple Yes/No questions on whether they have in place policies/procedures in the following areas:

- Equal opportunities, or equality and diversity
- Recruitment
- Workplace harassment
- Reasonable adjustments
- Flexible working
- Equality monitoring

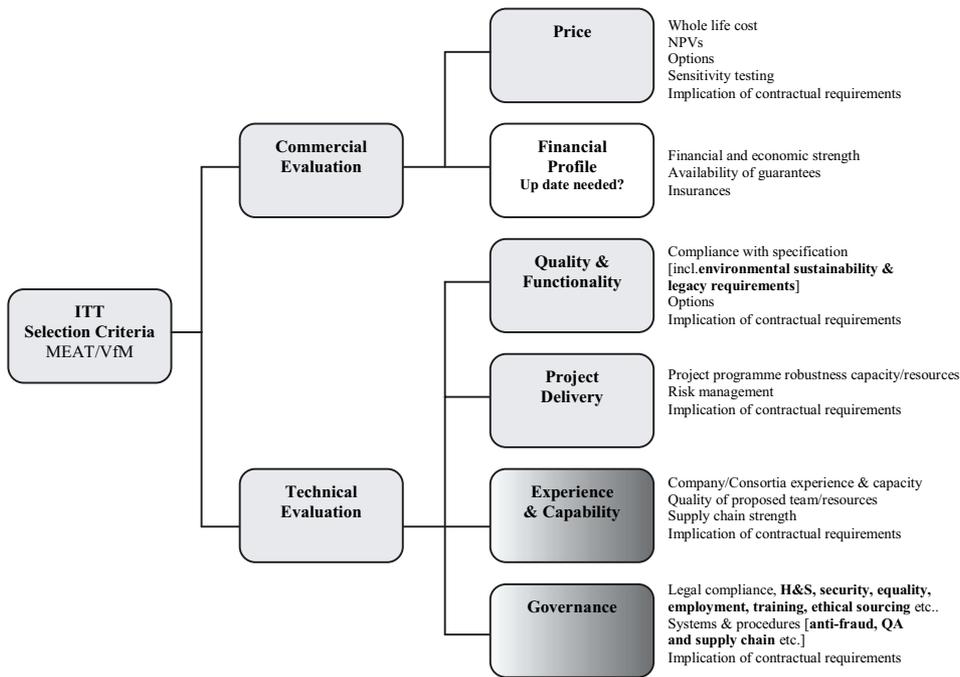
5.4 Companies are asked to submit their existing policies and procedures (or, in the case of equality monitoring, a copy of the monitoring form in use) as evidence, where they answer yes to any of the above questions.

5.5 In order to ensure that these questions do not have an adverse impact upon small companies, companies employing less than 50 people are simply asked to state if they have arrangements in place to ensure equal opportunities in relation to employment within their company, and to summarise these arrangements.

5.6 The tender evaluation process follows a similar approach. The tender documents set out the ODA's contract requirements. Included within the Governance area are those requirements related to equality and diversity in respect of successful delivery of the contract. A scoring matrix, based upon the most economically advantageous tender (MEAT) is used, and scoring is carried out by a panel. Figure 5 sets out the framework.

Figure 5

CONTRACT AWARD EVALUATION



Note: Blue boxes are tested with either new or in the cases of Experience & Capability and Governance more specific contract information.

5.7 In respect of equality and diversity, at tender stage companies are asked to describe their previous experience of promoting equality in the areas of retention and recruitment of staff, and how they might do so if successful in gaining the ODA contract. Their answers are then evaluated against a pre-determined scoring matrix.

6. OPENING OPPORTUNITIES FOR MINORITY-OWNED BUSINESSES

6.1 Early in 2007 the ODA examined all available evidence on the characteristics of businesses owned by Black, Asian and minority ethnic people, women and disabled people. This showed that businesses owned by Black, Asian and minority ethnic people and women were more likely to be micro businesses or small enterprises. The ODA has, therefore, undertaken a review of all criteria used at pre-qualification stage, with a view to reducing any unjustifiable use of criteria which would be harder for smaller businesses to fulfil.

6.2 The ODA advertises all its direct contracting opportunities on the London 2012 website. The ODA is aware that its reliance on e-procurement, and on the website for advertising may create barriers of access for some disabled people, and will be undertaking a review of accessibility of its e-procurement and e-alert systems.

6.3 In order to maximise the diversity of its supply chain the ODA is also engaging with minority-owned businesses to communicate contracting opportunities and facilitate networking opportunities between main contractors and small and medium-sized enterprises. The ODA is also working with partners to develop an electronic brokerage system which will allow tailored information to go to potential suppliers and buyers.

27 September 2007