PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT
GENERAL COMMITTEES

Public Bill Committee

DEFENCE REFORM BILL

First Sitting

Tuesday 3 September 2013

(Morning)

CONTENTS

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Saturday 7 September 2013

STRICT ADHERENCE TO THIS ARRANGEMENT WILL GREATLY FACILITATE THE PROMPT PUBLICATION OF THE BOUND VOLUMES OF PROCEEDINGS IN GENERAL COMMITTEES

The Committee consisted of the following Members:

Chairs: Mr Graham Brady, † Albert Owen

† Brazier, Mr Julian *(Canterbury)* (Con)
† Brown, Mr Russell *(Dumfries and Galloway)* (Lab)
† Colvile, Oliver *(Plymouth, Sutton and Devonport)* (Con)
Docherty, Thomas *(Dunfermline and West Fife)* (Lab)
† Donaldson, Mr Jeffrey M. *(Lagan Valley)* (DUP)
† Dunne, Mr Philip *(Parliamentary Under-Secretary of State for Defence)*
† Ellwood, Mr Tobias *(Bournemouth East)* (Con)
† Gilbert, Stephen *(St Austell and Newquay)* (LD)
† Hamilton, Mr David *(Midlothian)* (Lab)
Harvey, Sir Nick *(North Devon)* (LD)
† Hinds, Damian *(East Hampshire)* (Con)
† Jones, Mr Kevan *(North Durham)* (Lab)
† Lancaster, Mark *(Lord Commissioner of Her Majesty's Treasury)*
† Mordaunt, Penny *(Portsmouth North)* (Con)
† Pawsey, Mark *(Rugby)* (Con)
† Phillipson, Bridget *(Houghton and Sunderland South)* (Lab)
† Seabeck, Alison *(Plymouth, Moor View)* (Lab)
† Wheeler, Heather *(South Derbyshire)* (Con)
† Woodcock, John *(Barrow and Furness)* (Lab/Co-op)

Georgina Holmes-Skelton, *Committee Clerk*

† attended the Committee

Witnesses

Paul Everitt, Chief Executive, ADS

Professor Trevor Taylor, professorial fellow, Royal United Services Institute

Dr John Louth, senior research fellow, RUSI

Public Bill Committee

Tuesday 3 September 2013

(Morning)

[Albert Owen *in the Chair*]

Defence Reform Bill

9.55 am

The Chair: Good morning. Before we begin, I have a few preliminary announcements. Will members of the Committee please ensure that all electronic devices are turned off or switched to silent mode during sittings? As a general rule, I and my fellow Chair do not intend to call starred amendments that have not been tabled with adequate notice. The required notice period for Public Bill Committees is three working days. Amendments should therefore be tabled by the rise of the House on Monday for consideration on Thursday, and by the rise of the House on Thursday for consideration on the following Tuesday.

I know that a few Members are not familiar with the process of taking oral evidence, so I will briefly explain the procedure. The Committee will be asked to consider the programme motion on the amendment paper—which is in today's bundle and was agreed yesterday—for which debate is limited to half an hour. We will then proceed to a motion to report written evidence and a motion to permit the Committee to deliberate in private in advance of the oral evidence session, which I hope we can take formally. Assuming the second of those motions has been agreed to, the Committee will then move into private session. Once the Committee has deliberated, the witnesses and members of the public will be invited back into the room for oral evidence to begin.

The Parliamentary Under-Secretary of State for Defence (Mr Philip Dunne): I beg to move,

That—

(1) the Committee shall (in addition to its first meeting at 9.55 am on Tuesday 3 September) meet—

(a) at 2.00 pm on Tuesday 3 September;

(b) at 11.30 am and 2.00 pm on Thursday 5 September;

(c) at 10.30 am and 4.00 pm on Tuesday 8 October;

(d) at 11.30 am and 2.00 pm on Thursday 10 October;

(e) at 8.55 am and 2.00 pm on Tuesday 15 October;

(f) at 11.30 am and 2.00 pm on Thursday 17 October;

(g) at 8.55 am and 2.00 pm on Tuesday 22 October;

(h) at 11.30 am and 2.00 pm on Thursday 24 October;

(2) the Committee shall hear oral evidence in accordance with the following Table:

TABLE

Date	*Time*	*Witness*
Tuesday 3 September	Until no later than 11.00 am	Paul Everitt on behalf of Defence Industries Council and ADS Group; Royal United Services Institute
Tuesday 3 September	Until no later than 2.45 pm	Lord West of Spithead
Tuesday 3 September	Until no later than 3.30 pm	Federation of Small Businesses
Thursday 5 September	Until no later than 12.15 pm	Lord Hamilton of Epsom
Thursday 5 September	Until no later than 1.00 pm	Major General John Crackett, Assistant Chief of the Defence Staff (Reserves and Cadets); Air Chief Marshal Sir Stuart Peach, Vice Chief of the Defence Staff; Lieutenant General Andrew Gregory, Chief Defence Personnel
Thursday 5 September	Until no later than 2.45 pm	Public and Commercial Services Union; Prospect
Thursday 5 September	Until no later than 3.45 pm	Bernard Gray, Chief of Defence Materiel, Ministry of Defence; Barry Burton, Director of Materiel Strategy, Ministry of Defence; Susanna Mason, Director General, Export and Commercial Strategy, Ministry of Defence
Thursday 5 September	Until no later than 4.30 pm	Philip Dunne MP, Minister for Defence Equipment Support and Technology

(3) proceedings on consideration of the Bill in Committee shall be taken in the following order: Clauses 1 to 4; Schedule 1; Clauses 5 to 7; Schedule 2; Clauses 8 to 10; Schedule 3; Clauses 11 to 13; Schedule 4; Clauses 14 to 37; Schedule 5; Clause 38 to 43; Schedule 6; Clause 44; Schedule 7; Clauses 45 to 48; new Clauses; new Schedules; remaining proceedings on the Bill;

(4) the proceedings shall (so far as not previously concluded) be brought to a conclusion at 5.00 pm on Thursday 24 October.

I welcome you to the Chair, Mr Owen. It is a privilege to serve on this Committee under your chairmanship. I welcome other Members. I think we are going to have an interesting two days of oral evidence. I am grateful to those from outside the House who will be giving evidence, and to those from the other House who will be joining us later today. I look forward to detailed line-by-line scrutiny in due course when we come back in October.

The programme motion, which I think is uncontroversial, was agreed at our Programming Sub-Committee meeting yesterday.

Question put and agreed to.

Resolved,

That, subject to the discretion of the Chair, any written evidence received by the Committee shall be reported to the House for publication.—*(Mr Dunne.)*

The Chair: Copies of written evidence received by the Committee will be made available in the Committee Room.

Resolved,

That, at this and any subsequent meeting at which oral evidence is to be heard, the Committee shall sit in private until the witnesses are admitted.—*(Mr Dunne.)*

9.58 am

The Committee deliberated in private.

Examination of Witnesses

Professor Trevor Taylor, Dr John Louth and Paul Everitt gave evidence.

10.7 am

The Chair: Good morning. We will now hear oral evidence from the Defence Industries Council, ADS and the Royal United Services Institute. Before calling the first Member to ask a question, I would like to remind all Members that questions should be limited to matters within the scope of the Bill, and that we must stick to the timings in the programme motion the Committee has just agreed. This morning, we are scheduled to finish at 11am. I hope we do not need to interrupt people, because we will finish at 11 o'clock on the dot. It might be appropriate if Members who wish to declare an interest do so now, before we proceed.

Mark Lancaster (Milton Keynes North) (Con): I would like to declare an interest as a member of the Reserve forces.

Penny Mordaunt (Portsmouth North) (Con): I would also like to declare my interest as a member of the Reserve forces.

Mr Tobias Ellwood (Bournemouth East) (Con): Likewise, I would like to declare an interest as a member of the Reserve forces.

Alison Seabeck (Plymouth, Moor View) (Lab): I would like to draw attention to my entry in the Register of Members' Financial Interests.

Mr Kevan Jones (North Durham) (Lab): I draw the Committee's attention to my entry in the Register of Members' Financial Interests: I am on the advisory board of Northern Defence Industries, and it is a non-remunerated position.

The Chair: Thank you. Before I call Alison to ask the first question, I ask the witnesses to introduce themselves for the record.

Paul Everitt: My name is Paul Everitt and I am the chief executive of ADS, which is the national trade association for aerospace, defence, space and security.

Professor Taylor: I am Trevor Taylor. I am a professorial fellow at the Royal United Services Institute.

Dr Louth: Good morning. I am John Louth, a senior research fellow at RUSI. I am director of the defence industries and society programme there.

The Chair: Thank you. Alison.

Q1 Alison Seabeck: I look forward to serving under your chairmanship, Mr Owen, and that of Mr Brady as the Committee progresses. I also thank the witnesses for attending today.

You have all expressed concerns about the proposals in the Bill, while equally accepting the underlying assumptions of the need for reform of defence procurement. Could you initially set out for the Committee the evidence you see for a GoCo being an effective option—if you can?

Dr Louth: Well, I think the option has its birth in the 2009 Gray report, of course, which to my mind was an evidence-led, well researched piece of work, nuanced and sensible in its conclusions. But those conclusions effectively can be brigaded under three headings, it seems to me: that we have problems, because the programme is perceived as significantly overheated, in that we have more commercial commitments than we have moneys available to pay for those commitments; the analysis also suggested that the relationships between the constituent parts of defence and provision were broken, so the relationship between main building, DE&S and the front-line command was fractured, which was causing, in part, that programme to be overheated; and the third critique was that the skills within DE&S especially were inadequate to manage such a complex portfolio.

There are other arguments as well, but to my sense, the main thrust of the Gray report can be categorised under those three areas. Most analysts would say that was a reasonably sound judgment on defence acquisition circa 2009.

This is perhaps where, to my mind at least, the problems start to occur, in that, if we believe MOD and the Government—no reason not to—the overheated programme is now balanced and we have a 10-year programme that has been published. Perhaps we could all benefit from a greater level of granularity and exposure to what is in the programme, but it is a balanced programme, so the programme, in logic, is no longer overheated.

The significant effort to reform MOD from the Levene reforms and recommendations post-2010 are addressing the dysfunctional relationships between the front-line commands, head office and DE&S, and I think most fair-minded people would suggest that the jury is out on those reforms at the moment, but they have potentially been effective. That only really leaves skills as the main driver for this sort of change, if the other two headlines have been addressed, so I am really interested in the case around DE&S skills, and at the moment I have not really seen a robust skills audit within the public domain on what is going on in terms of competencies within DE&S. I do not know who the private sector benchmark is to compare public sector skills to private sector skills,

so I am really interested in understanding the argument around the lack of public sector skills that is causing the private sector to be considered as part of the acquisition process.

Q2 Alison Seabeck: So you feel that we need a competency audit?

Dr Louth: Absolutely right.

The Chair: Would anybody else like to comment on this?

Paul Everitt: From an industry perspective, I think we broadly buy into the fact that there have been problems, the situation is not perfect and reform of some kind is appropriate. The focus for us is really to understand more clearly what the criteria are that will be used to judge whether it should be a GoCo or some other changes within the existing regime so that it is a clear and transparent process, but also that, longer term, we have something both to be judged by and to judge what the outcomes are. We buy into the idea that if we do this better, there are gains both for the taxpayer and for industry, but I think our concerns are really that that will not be realised unless there are some clear criteria and clear metrics against which this process will be judged.

Q3 Mr Jones: To what extent have some of those delays and cost overruns been a result not of skills, but political decisions in taking into account budgets, moving main-gate rightwards and also military demands in changing the specification of projects?

Professor Taylor: A personal view would be that the cost increases and delays that we have seen with a number of projects obviously have complex causes, but I think that most of us see that the origins of most of those causes have not actually been in DE&S. I recognise that DE&S has some real human resource problems. I would very much support the upgrading of the technical civil service in terms of standing and preparation and so on, so that their capabilities can be as strong as possible. But I do not think that many of us looking at the problems of defence acquisition over the years have seen that DE&S, or its predecessors, have been a significant cause of those challenges.

Q4 Oliver Colvile (Plymouth, Sutton and Devonport) (Con): First, I think you should be aware that I represent Plymouth, Sutton and Devonport. That includes Babcock, which runs the dockyard as well. There is one thing I am quite interested in. I was part of an all-party group inquiry into the procurement of public buildings. Although that has no relevance as far as this is concerned, one of the things that came out of that inquiry was the necessity to make sure that potential contractors educated the client as to what they were going to be producing and doing. To what extent do you find that that actually happens? From your perspective, do you need to make sure that the Ministry of Defence understands what it is actually buying? Has it thought it through, or does it simply issue a contract and you find it quite easy to run with that?

Dr Louth: As a Plymouth boy and ex-dockyardee, perhaps I should answer that. There is a good tradition of partnering between the MOD and private sector businesses—Babcock is one—that I think has been on a significant improvement curve in recent years. Part of that tradition is cross-fertilisation between the specific demands of working within the public sector: the governance and assurance demands, the value for money demands, and the demands of private sector investors for companies such as Babcock and BAE Systems. As an ex-programme director from QinetiQ, I think that that has improved dramatically in recent years. On the basis of that, the MOD has committed to a number of long-term contracts and partnering agreements: with QinetiQ for the ranges and with BAE Systems for the small arms and ammunition and so on. There is a strong sense that the private sector, in part, has been educating the public sector through the dynamics of acquisition, but the public sector has also been positioning and educating the private sector. I think the partnering mechanism is incredibly significant.

Q5 John Woodcock (Barrow and Furness) (Lab/Co-op): May I develop Kevan Jones's question on the two strands of problems in the budget? One is the lack of technological skills, but I want to focus further on the over-commitment of the budgets and decisions that are made at a political, Government level, resulting in that over-commitment. If a GoCo existed broadly on the terms set out in the Bill, what improvements, if any, could it make to that decision-making process in Whitehall?

The Chair: I will ask the Minister to ask his question, because we really need to move on.

Q6 Mr Dunne: My question is to Paul Everitt, who talked about the evaluation criteria. As you know, ultimately this will be a choice between the best GoCo proposal and the DE&S-plus proposal. You wanted us to be clear about the evaluation metrics. What, in your view, would ensure that a robust, transparent and fair choice is made? What do you want to see in that decision making?

Professor Taylor: I find it difficult to answer that, except by going to the political level. The over-commitment in the defence programme, incidentally, long predates 1997. It used to be called the bow wave and then it became the black hole, but it was the same phenomenon. That has never been invisible to politicians and Ministers, who have opted to leave it in place. One of the reasons for leaving it in place was that they did not want to have the difficulties of cancelling projects that did not seem affordable.

That takes us to the heart of some of the issues associated with the GoCo. The GoCo proposal assumes, to my mind, that defence acquisition is a rather technical business where there is a simple concept of value, but in fact that is not the case. Defence acquisition, for all the time that I have been dealing with it, is a highly political business where very difficult choices are made. People are concerned with different aspects of the economy; with foreign relations with Europe and the US; with defence capability, and the difference between up-front capability and whether that capability is really controlled from outside by somebody else who controls the technology; and with how much relative weight you give to purchase price, which you are relatively confident about, and through-life prices, which are much more uncertain. All that stuff is the reality of defence acquisition.

The notion that someone else can go and buy something for you that you will not change your mind about is simplistic. To answer your question, if politicians continue not to want to make difficult decisions about cancelling projects, if the UK continues to be ambitious and if the budget does not change accordingly, I do not see how this proposal will make a difference.

Paul Everitt: The difference is that there will be greater transparency in the process. The GoCo will make it much clearer that there is either a clear cost to a change of mind, or a clear delay. That, presumably, will be a benefit. In terms of the comparison, we would like to see a clear, public statement about the outcomes that we seek to achieve through this process, the evidence that supports the two different options, and how the outcomes will be achieved, so that the public are confident that the right choice has been made. Our goal is that at the end of the process there should be a strong cross-party consensus about what the right options are, and strong engagement and buy-in from industry that this is the right way to go about the process. To do that, we need to be explicit about what the changes will achieve and which of the options will deliver them in the best way.

Q7 Mr Ellwood: May I welcome the panel to this Bill Committee sitting? There has been considerable debate about the concept of putting defence acquisition and support into the private sector. You spoke about the black hole or the bow wave—however you want to justify it. One benefit seems to be transparency, which is very much welcome. May I ask whether you have done or intend to do any analysis of the concept of GoCo, what its impact will be, and whether it will be a positive move forward?

Dr Louth: We're working up a number of papers that pursue a partnering theme, specifically through the lens of GoCo. One of the issues that we seem to be encountering is that the merits of private sector success for these sorts of complex activity are normally perceived at the portfolio level—at the top level of management. The question we are asking is, how do they manage an investment portfolio?

Of course, we contract through programmes and projects. The commercial tension that that gives means that management at the portfolio level—at the strategic level—becomes incredibly complex and difficult. The private sector has not always done that well. There is significant research evidence that shows that management at the portfolio level is remarkably problematic, whether your investors come from the private sector or whether they are citizens. It is not simply a binary choice: "private good, public bad" or "public good, private bad". The complexities of portfolio management make this extremely difficult.

The transparency argument is important. The merits of GoCo as a concept are increasingly being articulated through the argument that it is remarkably transparent. That might be so, but we will not know until we see the details and the commercial wrap around the GoCo solution. That is remarkably important; how that commercial wrap interfaces with oversight from Parliament and elsewhere becomes really important, to my mind. One of the questions for me throughout the past six months has been: why are we not including the "as is" within the investment appraisal? In many ways, the public sector comparator should be what we do now, rather than an additional reform, albeit a public, in-house reform. I would really like to see three options rather than two, and I think that the "as is" should be considered.

Q8 Mr Ellwood: The status quo.

Dr Louth: Yes. Even if it is to discount it, we should include the "as is" within the investment appraisal and treat it as a public sector comparator.

Q9 Mr Ellwood: Very quickly, you mentioned that you have some analysis under way—some papers are being produced. When might we expect them to be published?

Dr Louth: We are looking to publish in line with some of the decision milestones, so if a decision is due on which solution is to down-selected at the end of the year, we will publish in line with that.

Mr Ellwood: I was just giving you a free advertising slot.

Dr Louth: To pursue that, the book will be published in November; that might be helpful.

Professor Taylor: One of my issues is the questions that need to be asked, rather than the answers that we could give. Among those questions is whether transparency is a matter of Government choice and whether we could have significantly more transparency than we have without a GoCo.

Q10 Damian Hinds (East Hampshire) (Con): Dr Louth, can you explain why you believe that a third comparison is needed? If, by definition, DE&S-plus is better than DE&S, where does your third comparator fit into the analysis?

Dr Louth: At the moment, we have an acquisition process, and that process has generated the artefacts of acquisition—programmes, projects, contracts, and physical things that people sail on and fire. That has generated an effect and desirable outcomes. Quite often, those outcomes actually match the requirement, albeit that a number of issues have occurred, in terms of requirement setting. It seems that that should be tested to see whether or not it is properly broken. To my mind, the process is clear: an investment appraisal in the private sector will look at what you do today against what you think you can do better. If this was a private sector investment appraisal, it is almost inconceivable that the "as is" would be glibly discounted.

Q11 Mr Ellwood: In a way, that was my question. From the perspective of cost and financial benefits, surely that will be done using as a yardstick current performance and how we do things now?

Dr Louth: But it is not though, is it? The two options are DE&S-plus and GoCo. Those are the two options in the investment appraisal. The "as is" has been edited and filleted out; we are not concerned with the "as is," in terms of the investment appraisal.

Mr Ellwood: I think that that might be for the Minister to determine later on. I presume that a benchmark will be taken from where we are today.

Q12 Mr Russell Brown (Dumfries and Galloway) (Lab): Good morning, gentlemen. Industry has said that a key concern with defence contracts currently is certainty. To what extent do you think a GoCo would provide greater certainty to companies bidding for contracts?

Paul Everitt: For us, it is about predictability and stability. Part of the rationale for the changes is that we would expect there to be fewer changes in a contractual arrangement, so we would therefore have greater predictability on what we are being asked to do. Similarly, part of the change is to address the overheated project portfolio, so that a more stable level of funding is available and we know what that is likely to be over time. Against that background, we would be better able to manage our businesses. If you like, the rationale for the change is to deliver those conditions. I guess that we are asking for it to be more explicit that predictability and stability of funding are goals that the change is aiming to achieve. There should be some rationale as to which of the two options being assessed is better able to deliver that.

Q13 Mr Jones: That is a perfect world, but you know that we do not live in a perfect world. How would a GoCo deal with the problem that we faced during the previous Government as regards urgent operational requirements, which meant very quick decisions were taken on the kit that was needed and, inevitably, budgets were diverted from other programmes, which were reprioritised? How would that fit into a GoCo?

Paul Everitt: My proposition is that I am not here to say that a GoCo is the right option. I am suggesting that we need clarity on how the two options will be assessed. Clearly, one part of that would be how the GoCo responds to those types of challenges, and another would be ensuring that they are able to do that. From an industry perspective, with both options, we would look at things that we know are important. The sustainability of capability over the long term is important, in terms of the defence capability aspect and from an industrial point of view. We have questions about how that would be embedded into a GoCo-type situation, much as we would around the focus on exports and exportability. Those things have not been made explicit in the information that has so far been made available.

Q14 Mr Jones: No, but we were sat here in 1997 considering the defence procurement budget, and we would not have predicted—very few people would have—that we would be in Afghanistan, or that we would need a whole fleet of mine-protected vehicles and improvised explosive device technologies. How quickly do you think a GoCo could react to that, in terms of skewing budgets, which is a political decision and not for the GoCo? Would that lead to difficulties with the idea that the GoCo will deliver everything?

The Chair: A brief response to that, please.

Paul Everitt: From an industry point of view, we have demonstrated that we can respond quickly to urgent operational requirements and deliver as well as we can. I am sure that industry would be seeking to do that under any circumstances.

The Chair: I need to move forward, because we need to speed up a little. We have a very condensed session.

Q15 Alison Seabeck: You have talked about security and continuity of the GoCo. We know that the contracts will initially be let for nine years. Do you have a view on whether those contracts can be successfully evaluated after nine years, given that the length of Ministry of Defence programmes is often much longer than nine years? Do you also have a view on whether an incumbent GoCo will be in an almost unassailable position, with its internal knowledge? It will be quite difficult for the Government to replace it after nine years. Do you think that the GoCo will be in too strong a position at the end of those nine years to be replaced?

Professor Taylor: I think that above that question is the issue of whether there is a market to provide the kinds of services that we are interested in, as far as GoCos are concerned. Currently, there appear to be just two companies in the western world—neither of them British—that are able to compete. There is a whole question about what the form of competition is when you are beginning with an oligopoly. My view is that if this organisation did any kind of job over a nine-year period, it would be extremely difficult to recompete the contract in any meaningful way, because of the knowledge that the organisation would have acquired. As for whether its performance could be assessed over that period, because of the number of projects, that is a large question. If we are dealing with this agenda in 55 minutes, we cannot expect meaningful answers to the question, but there is a lot of doubt about it.

The Chair: To respond to that point, you can give us written answers later if you wish, and we will use those in our deliberations.

Professor Taylor: Okay.

Q16 Mr Julian Brazier (Canterbury) (Con): Mr Everitt, in ADS's submission, you say that in clauses 7 and 8, which give the new entity the same access to information as the existing entity,

"There is inadequate protection for suppliers' IP and commercially sensitive information".

Would you like to say why that is?

Paul Everitt: The reason why it is a concern is that, as we already know, a number of the companies that will potentially bid to run the GoCo do in a variety of other circumstances act as competitors, collaborators and suppliers, so where any company provides absolutely everything to those companies, there must be concern that that information will leak into some of those other relationships. Our concern is that, in the second part of the Bill looking at the single source regulations office, there is a specific criminal offence of the inappropriate release of information, but similar approaches are not provided in the first part of the Bill. We would look for that to be strengthened in both areas, so that the crime is about not only deliberately handing over information, but also not having in place the kinds of processes and procedures that adequately protect that important information. Often, given the nature of the sector, both domestically and internationally, many such companies are either working together or indeed competing, so it is important that there is protection not just for hard intellectual property rights, meaning the particular technology and innovation, but also for some of the softer stuff, which are the clever and innovative ways that we are delivering a particular service.

Q17 Mr Brazier: May I pursue that a little further? Suppose for the moment that the clause in part 2 of the Bill were put into part 1, so that we really had tough

criminal sanctions enforcing the rule. There are foreign companies among the bidders in both the main consortia. Would it worry you that there might be some difficulty, particularly where individuals were concerned, in enforcing the rule? I am asking you a leading question.

Paul Everitt: I think the signal is the more important thing. If it is clear in the Bill that there are repercussions of not managing data and information appropriately, most companies would endeavour to deliver in an appropriate way. Without that signal, however, that seems to be a significant weakness.

Mr Brazier: Thank you.

Q18 Oliver Colvile: It is likely that some defence companies will form a consortium to be part of the GoCo. Do you foresee conflicts of interest arising if a company bidding for a particular contract is also a member of the winning consortium? How do you think that can be managed?

Paul Everitt: It is very clear, given the economy that exists within the defence sector, that companies that are participants in the sector and suppliers to the MOD and others will also potentially be part of this. At the moment, our assumption is that in contracting for a GoCo—if that is the route that is finally taken—there will be either contractual requirements that prevent companies from bidding for contracts within themselves, or a set of rules put in place to ensure that the relationships are not inappropriate. At the moment, there is an open question as to how the operational aspects of the GoCo will be delivered.

Dr Louth: But the MOD has done this pretty well in the past. With QinetiQ, for example, firewalls were put in place and reviewed regularly, and that has worked reasonably well over the past few years. A tradition of managing firewalls on the supply and advisory sides is in place and exists within the MOD and the industry. Lessons have been learned from that. I am reasonably sanguine that it could be managed well, but the perception is remarkably important here. The perception of doing good is remarkably significant for defence business.

The Chair: Professor Taylor, do you want to add anything?

Professor Taylor: A little account should also be taken of how non-UK businesses, particularly businesses from Europe, might feel about putting commercially and technically sensitive information into an organisation that was run by American companies. It is not just what British companies might feel; there is also a confidence factor to do with what the views are of people from the continent who we might want to bid on our contracts.

Q19 Mr Jones: You are talking about companies now. What about individuals who work for the GoCo being poached, or moving on, in later life, to defence contractors? I am talking about them not taking specific knowledge of an individual programme, but understanding how the processes work. How would you stop that?

Professor Taylor: This is a legal question to which I do not know the answer. There are restrictions on the ability of MOD people, uniformed and civil servants, to move into the private sector.

Q20 Mr Jones: It does not work very well, does it?

Professor Taylor: As I understand the law, restrictions on freedom of contract are always pretty tricky. People generally can choose their employer. That is a kind of human right. Whether it would be possible to write into the terms and conditions of people working for the GoCo that there were limitations on where they could go to work next, I do not know. You would have to get a legal opinion, but it is a valid question.

Paul Everitt: I am not a legal expert, but in other areas and in other industries, when a senior executive moves from a particular company to a competing company or somewhere that is closely related, there would normally be an agreed period of gardening leave to ensure that the person would not necessarily have current information or knowledge on market strategy. That is not an unreasonable request or requirement that could be placed in employment contracts.

Q21 Mr Brazier: Presumably that would not be enforceable in America. That presupposes that you are dealing with British employees.

Witnesses indicated assent.

Q22 Penny Mordaunt What is your assessment of the likely reaction of the UK's allies to the pursuit of the GoCo model?

Professor Taylor: The Americans are coming at this from a rather different position. They have some acquisition issues. Everybody has acquisition issues. None of the major countries—France, Germany, the US and so on—to our knowledge, are taking this route. The US is going in the opposite direction and has a long-term plan to build up the capabilities of its internal people. Part of that is that in the US there has been a significant clarification of what is meant by an inherently governmental function. The term "inherently governmental" has not been used much here, but it was in the last White Paper on security through technology. In America, there has been a thorough clarification. We are not clear what the GoCo here will do, in terms of decisions, advice and that balance.

Broadly speaking—I could provide the Committee with chapter and verse—in the American concept of "inherently governmental", what we understand as defence acquisition and defence procurement is an inherently governmental activity. They are trying to claw back from their use of contractors and use more Government personnel. That is a very quick answer. France, Germany, Japan or any places like that are not moving in that direction at all.

Q23 Mr Ellwood: On the concern about employees going elsewhere, I say this without any knowledge whatever of their interest, but if companies such as G4S, Serco and RAND Corporation got the contract for this, would you be content? The fact that a foreign company had gained the contract would not make you nervous at all?

Professor Taylor: I think the question is: what are the clearance arrangements for the people working on the contract? Normally, British security clearance is just given to British personnel.

Q24 Mr Ellwood: But you would not say that it had to be a British company that ran it; you would not limit it.

Professor Taylor: I think it very much hinges on which people are going to be involved. We have very many American companies here, that have invested here and produce goods and are treated as British companies, because they add significant value here; but normally clearances are just given to British personnel, so there is a question about what would be the security clearance arrangements for the people who would have access to what, historically, has been considered to be very sensitive information.

Dr Louth: Where the head office is located is less and less an issue, to my mind.

The Chair: Moving on now to single-source contracts—John.

Q25 John Woodcock: Speaking as a Member of Parliament for the place that houses the finest, and indeed the only, source for the United Kingdom to produce our incredible submarine fleet, can I ask about single-source contracts? Generally, are the proposed changes proportionate to the identified problems? In particular, in picking up on that, Mr Everitt, can you talk about your proposal of the pharmaceutical price regulation scheme as potentially a more appropriate model to combat what you see as lack of political independence?

Paul Everitt: I think we recognise as an industry that we have been using a particular approach over a very long period of time, and some of that goes back to the late 1960s, so review—reform—is not a problem as far as we are concerned. The issue for us is very much about trust and confidence that the mechanisms that are going to be put in place will deliver the outcomes that we want, which is the right capability for our armed forces at a price that is good value for money for the taxpayer, but also be appropriate for the companies that are having to invest and deliver it. So independence for us is a key part of that. The trust and confidence that industry has in the mechanism has to be a key part of the test, as far as we are concerned.

Currently the regime, as sketched out, effectively sees all of the power and responsibility for who is part of the SSRO—who is leading it; how it is orchestrated—being determined by the MOD and, indeed, by the Secretary of State. That, to us, instinctively does not feel quite right, and we would like to see some appropriate scrutiny and industry input. So, for instance, it may well be that the chairman of the SSRO should be subject to pre-appointment scrutiny by a parliamentary Committee, to ensure that Parliament has trust and confidence that the individual chosen is robust, and is genuinely going to deliver on the remit in an independent way. Similarly, in terms of the governance structure of the SSRO—you mentioned the pharmaceutical industry approach—there are mechanisms to ensure that industry has some input into the candidates that would be reviewed: not a choice from industry, if you see what I mean, but an option for industry to ensure that some appropriate people on that governance board have the expertise, knowledge and independence that we would hope to see.

Q26 Mr Brown: Obviously, there are clauses in the Bill specifically dealing with monitoring and compliance regulations. Have any concerns been raised regarding the power to exempt contracts from the monitoring and compliance regulations, and to what extent would you expect exemption to be given more often to overseas suppliers? What would the impact be for UK businesses if that were to be the case?

Paul Everitt: We are concerned, again, about what appears quite a powerful right for the Secretary of State to waive this regime for specific contracts, but there is no information on the circumstances where that waiver would be given. For us, I think, it is about having some clarity as to why a waiver would be given, and in what circumstances it would be provided. I guess that the suspicion from industry is that we believe that some of the commercial arrangements, particularly those linked to Government-to-Government deals, would not allow such a type of scrutiny, or that companies providing that support from outside the UK would not sign up to such a type of scrutiny. That seems, potentially, an unfair set of circumstances or not a level playing field. Domestic suppliers would potentially have to meet quite onerous requirements, but those supplying from outside the UK would not have to meet those requirements.

The reverse, if you like, is that when UK businesses compete in foreign markets, we very much have to deliver against the requirements that are operating in that regime. I think we can understand that there are circumstances where a waiver would be required. We just want to ensure that it is explicit as to why it is being taken up.

Q27 Heather Wheeler (South Derbyshire) (Con): I am interested in the small and medium-sized enterprise side of the matter as well, particularly in whether you think there will be extra burdens placed on SMEs, or whether there might be a way around it, maybe with thresholds or something like that. Do you have any views on that?

Paul Everitt: Again, at the moment, there are some references to slightly different arrangements for subcontractors, but it is not clear what those would be. In terms of volume, there are around 4,800 single-source contracts. Obviously, the majority are relatively small in value. Certainly we believe that there is an argument to say that there should be a de minimis threshold put in to ensure that we do not have the SSRO being clogged up by huge numbers of contracts where they are not a significant issue. Even if there was a problem, the problem we would be solving would be relatively small in terms of the overall quantum of expenditure. Others may have exact numbers, but there are a relatively small number of large contracts that are responsible for the overwhelming amount of expenditure. Ensuring that there is perhaps some reasonable threshold that means that time and effort can be spent on those contracts with the highest value seems to be a sensible way.

The other issue for us is, if you like, the flow-through. It may be that a prime contractor has a large contract, which is appropriate to be scrutinised. However, if they have to put in place contractual or operational arrangements that require each and every one of their suppliers to provide information that is then used in the format required by the SSRO, that could lead to unnecessary or burdensome requirements on relatively small companies. Again, I think there may be an appropriate approach that says, "For the subcontracting route, there are substantive contracts that should be part of that approach,

and there are a whole bunch of contracts for which it is not necessary to have that level of scrutiny." I think that within European regulation, it is normally accepted that for smaller companies, some kind of de minimis threshold is the right approach to deal with those things.

The Chair: Would any other witnesses like to comment before we move on?

Dr Louth: The ways of working of the SSRO are absolutely pivotal here. An understanding of how it will be established and how it will work is quite important. I think most analysts are thinking along the lines of some kind of banding on either value of contract or size of entity. I think we need more visibility of what the intent is.

Professor Taylor: I think also that there is a question about how the SSRO will work in the context of a GoCo. The value of contracts that are placed competitively is about 50%; it goes up and down, but it is about 50%. However, in terms of number of contracts, 70% of contracts are not placed on a competitive basis, for a range of reasons. The issue about how the single-source arrangements would work in conjunction with GoCo arrangements is not clear.

The Chair: Thank you. Moving on now to Reserves, Russell.

Q28 Mr Brown: The Bill's impact assessment states that the Government's intent is to ensure that the

"reserves will complement the regulars within an integrated Whole Force, providing military capability in a different way from the past to deliver the range and scale of military forces and skills required."

Do you feel that the Bill's provisions contribute to achieving the same? I appreciate we have a number of Reservists on the Government side here.

Professor Taylor: This is slightly beyond our domain. The idea of sponsored Reserves, brought in under the previous Government, raised the question to what extent people working for a civil employer could in a crisis put on a uniform and become military personnel. That has proved possible in a small range of specialist areas. It may be, as contractors become more involved in the support on a day-to-day basis of military equipment, that that needs to be expanded.

My personal view is that the whole Reserves question is very complicated, given that different sorts of people will be needed as Reservists. People who bring their civilian skills into the military and essentially use those skills obviously need less conversion. It would be easier to use them than people who might be a Member of Parliament but an infantryman, where I do not think the skills are quite comparable. I am interested in the sponsored Reserves domain and whether we could expand the number of people who bring their civil jobs into the military in an emergency.

Dr Louth: Does it depend on how you manage and measure effectiveness and when you take that judgment? Should Parliament have clarity on that simple question?

The Chair: The next couple of questions will probably be the last. Please bear that in mind.

Q29 Mr Dunne: Just picking up on Professor Taylor's comments on sponsored Reserves, I think, Mr Everitt, that many of your members will already be engaged in sponsored Reserves programmes. Do you see our proposals for Reserves in the Bill as assisting and encouraging the use of sponsored Reserves? Secondly, you have applauded some of the measures that we have taken to respond to particular challenges for SMEs. Are there are other things that you think we should have included in the Bill to help SMEs, rather than your larger membership?

Paul Everitt: As an industry, we absolutely support the Reserves, and we are happy and keen to employ them. We have experience of Regular Reserves and sponsored ones, and we think the proposals are relatively sound and we support them.

Inevitably, for SMEs—smaller companies—the challenge will be that their specialists are likely to be required. It is a matter of ensuring that there are appropriate management structures in place to give that SME the time it might need to replace those specialist skills in its business. There is a paradox that the Reserves are probably going to be most used when there are particular pressures on the Regular forces, and those may well be points at which the defence industry itself is most engaged in supplying.

We do not have any major issues with the Bill or how that element is proposed. It is about how it is implemented, ensuring that there is a sympathetic approach to SMEs that might be giving up specialist resource within their businesses. It might take them time to organise replacement of that.

The Chair: Would any of the other witnesses like to make a brief comment before we finish? Right, there is a minute left and I am going to ask the Whip to do some business. I am going to ask him formally to adjourn consideration.

I thank the witnesses for their evidence this morning. As I indicated, if there is any further information they would like to supply to the Committee, would they please do so in writing?

Ordered, That further consideration be now adjourned. *—(Mark Lancaster.)*

10.59 am

Adjourned till this day at Two o'clock.