DFID’s use of private sector contractors

Eighth Report of Session 2016–17

Report, together with formal minutes relating to the Report

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International Development Committee

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DFID’s use of private sector contractors

Summary

The Department for International Development (DFID) is a commissioning agency that partners with various types of organisations to implement programmes that facilitate poverty reduction around the world. As DFID’s budget has increased in recent years, so too have the funds channelled through these partners—a fact that has been noted in recent media reports and has raised some concerns, particularly with respect to private sector contractors. For the purpose of this report, the term ‘contractors’ refers to private sector organisations, many of which operate on a for-profit basis. Contractors can act as an effective channel for aid delivery, and one that we support where it is proven to be most effective and offer the best value for money. However, it is not evident that DFID has an effective process for assessing this at the programme level, nor whether it undertakes a sufficiently robust appraisal of all available options. We also have concerns that the contractors strategy is being driven by a lack of administrative capacity in the Department. Evidence suggests that DFID does not have a sufficient understanding of the way its procurement processes are shaping the market, particularly with respect to its procurement through framework agreements. While DFID has been explicit about its wish to expand the market and facilitate entry to smaller organisations, many of the procurement processes it uses work against this stated aim. DFID relies on the pressures of competition in its supplier market and assumes that the levels of competition assure it value for money. While we recognise that it is ahead of other donors in creating a competitive supplier market, there are aspects of its procurement, such as framework agreements and other barriers to entry, which are undermining this. The way the market is set up also means that the rewards for contractors lie in winning contracts, not in delivering on them. DFID should strengthen its approach to following up on implementation, particularly through greater use of independent evaluations. We also note concerns about DFID’s oversight of the supply chain, from lead contractors down to smaller, local organisations. Serious examples of sub-contractors being mistreated by lead contractors point towards an insufficient level of oversight that DFID should take concrete steps to improve. We are also greatly concerned about the appalling conduct of some contractors who have behaved in a way that is entirely misaligned with the Department’s purpose. We recognise that not all contractors have behaved poorly, though we also stress that recent examples highlighted in the media should not be viewed as isolated cases. We have heard that there are fundamental flaws in the working practices of some organisations. While DFID requires contractors to sign up to its Statement of Priorities and Expectations, there is a worrying over reliance on self-regulation and a complete lack of enforcement. We urge DFID to ensure that a key focus of its forthcoming Supplier Review is on ensuring greater compliance and a more robust system of incentives and consequences to shape the behaviour of contractors to the highest ethical standards.
1 Introduction

1. In recent years, as the UK scaled up its international development budget to 0.7% of gross national income (GNI), the size and number of aid programmes has increased. As a result, the various types of organisations that implement Department for International Development (DFID) programmes have received larger sums—a fact that has been noted in recent media reports and has raised some concerns, particularly with respect to private sector contractors.\(^1\) As Figure 1 indicates, the amount spent through contractors has surged in recent years, both in cash terms and as a share of total bilateral expenditure. In 2010/11 contracts represented 12% (£540 million) of bilateral spend and five years later had increased to 22% (£1.34 billion). This reflects a substantial increase and demonstrates the growing use of contractors as a channel for aid delivery over other approaches such as through multilateral organisations, NGOs and CSOs.

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\text{Figure 1: DFID spending through contractors by financial year of contract issue (Figures in parentheses reflect DFID spend through contractors as a share of total bilateral spend that year)}
\]

\[
\begin{array}{ccccccc}
\text{Year} & 2010/11 & 2011/12 & 2012/13 & 2013/14 & 2014/15 & 2015/16 \\
\hline
\text{£ billions} & (12%) & (16%) & (17%) & (19%) & (22%) & (22%) \\
\end{array}
\]

Source: DFID Annual Report and Accounts (various) and PQ 65689

2. In the course of our inquiry into UK aid: allocation of resources, we took evidence relating to the way in which the Department for International Development (DFID) uses private sector contractors to implement its programmes. Questions were raised about the Department’s strategy, whether it was achieving value for money and to what extent procurement processes were operating effectively.\(^2\) This coincided with a series of investigations by the media, particularly the Daily Mail, Mail on Sunday and the Times, which raised similar questions and also highlighted concerns regarding the pay practices and conduct of certain contractors. Particularly serious allegations concerning the conduct of one contractor, Adam Smith International (ASI), were in part dealt with in a recent Special Report by the Committee.\(^3\)

3. In addition to the investigation of ASI, we also considered that the broader issues regarding DFID’s use of contractors warranted further investigation. We had been

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\(^1\) We use ‘contractors’ to refer to private sector organisations that play a role in advising on and/or implementing DFID programmes

\(^2\) Bond (ACH0006) para 42

\(^3\) International Development Committee, Seventh Special Report of Session 2016–17, Conduct of Adam Smith International, HC 939
considering the subject as part of our inquiry into how DFID allocates its resources, but the number of media reports and the scale of the issue led us to separate out use of contractors from the existing inquiry. We launched a separate inquiry on 20 December 2016 and invited written submissions into all aspects of DFID’s work through contractors, but particularly into the following questions:

- Does DFID have an effective strategy for how it works with and through private sector contractors? Does its use of contractors provide good value for money?
- Are current levels of salaries, profits and dividends in the sector appropriate for an international development context? Does the sector conform to the same standards of transparency as the rest of the development community?
- Is there sufficient competition in the sector, and when bidding for individual programmes, to ensure that costs are kept as low as possible? How are the costs of a programme broken down?
- Do DFID’s procurement processes prejudice against smaller contractors (those not in the top ten recipients of UK aid contracts)? Does DFID have sufficient protections against anti-competitive practices and conflicts of interest in the sector?
- What is the shape and make-up of DFID’s supply chains? How well does DFID understand its own supply chains and the business environment of the sector?
- How well do DFID and its partners learn from its contractors? How compatible are learning and knowledge sharing with commercial confidentiality and competitive tendering?

4. Over the two phases of our inquiry we received 32 pieces of written evidence, with five of these received in confidence at the request of those submitting them. The Committee agreed to accept confidential evidence because it appreciated that those who often know most about the detail of DFID’s use of contractors work in the sector. They may have otherwise had reservations in being frank with the Committee for fear of jeopardising working relationships. We held two oral evidence sessions, hearing from:

- **Session 1**

  - Two experienced contractors who will hereafter be known as Contractor A and Contractor B for the purpose of confidentiality.

- **Session 2**

  - Joy Hutcheon, Director General, Finance and Corporate Performance, and Nick Ford, Head of Procurement and Commercial Department (PCD), Department for International Development.

We also sent a set of questions seeking further information from those contractors who submitted written evidence. We are grateful to all those who gave written and oral evidence to us in this inquiry.
5. It should also be noted that both DFID and the Independent Commission for Aid Impact (ICAI) are undertaking their own investigations in this area. ICAI’s work will build upon its 2013 review of DFID’s use of contractors,4 with the initial phase focusing on “reviewing DFID’s approach to ensuring value for money in the management of its supplier pool”.5 In addition to its own forensic investigation into the ASI allegations, DFID has also recently launched a broader Supplier Review. In January 2017, Secretary of State, Rt Hon Priti Patel MP, wrote a letter to the Chair of the Committee regarding the priorities of this review. She wrote:

“[ … ] there should be no room for excessive profiteering or unethical practices. All of DFID’s contractors and partners need to be fully open and transparent with UK taxpayers about where their money is going and how it is being spent to meet development outcomes. They need to uphold the highest standards and be held to account for those standards. DFID needs to reduce its reliance on a limited number of suppliers, and encourage healthy competition in what is often a challenging development sector.”6

The Secretary of State issued a letter to all DFID contractors in December 2016 noting efforts towards greater assurance on contractor delivery, but also stating that “far more needs to be done” and that a “step change” is required.7

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4 ICAI, DFID’s Use of Contractors to Deliver Aid Programmes (May 2013)
5 ICAI, Upcoming reviews: Achieving value for money through procurement (accessed 9 March 2017)
6 International Development Committee, Letter from Rt Hon Priti Patel MP, Secretary of State for International Development, concerning DFID’s relationship with its suppliers (9 January 2017)
7 DFID, Secretary of State letter to DFID suppliers (December 2016)
2 DFID’s strategy

DFID’s delivery model

6. As with any government department, the Department for International Development (DFID) has to make choices about how to spend its budget. DFID has a broad set of goals outlined in the UK Aid Strategy (and underpinned by the Sustainable Development Goals (SDGs)) that collectively contribute towards its overall objective of reducing global poverty.\(^8\) However, DFID is not a direct implementer of the development programmes that it funds to achieve these goals. As the Department stated in written evidence “as a government department DFID is structured as a commissioning organisation.”\(^9\) DFID thus has to work through partners to achieve its objectives.

7. With regards to DFID partnerships, Dr James Morton, an experienced development practitioner, wrote in evidence:

“The ideal would be for DFID to work directly with the governments and civil society of the countries it is trying to help. However, capacity constraints and fiduciary concerns mean the Department must normally depend on an external agency of some kind to manage its programmes.”\(^{10}\)

Poverty is driven by a complex set of challenges. Limited specialist skills to tackle these challenges coupled with the risk of corruption in many developing country governments means that DFID’s delivery model involves operating in partnerships with a variety of external actors.

8. There are three main channels through which the department delivers its bilateral programmes:

- **Multilateral agencies**—International organisations formed between a number of countries to work on issues that relate to members’ common priorities. The UK works alongside other donors within these organisations and they include UN agencies—such as the World Food Programme (WFP)—and the World Bank Group, which offers financial and technical assistance to developing countries around the world.

- **Civil Society Organisations (CSOs)**—The term CSO is broad and includes non-governmental organisations (NGOs), charities, trusts, foundations and advocacy groups. They typically aim to address social or political issues such as human rights, the environment or health. Some well-known examples that DFID partners with are Oxfam, CARE and Save the Children.

- **Contractors**—For the purpose of our investigation, ‘contractors’ refers to private sector organisations that play a role in advising on and/or implementing DFID programmes. DFID uses many agents and intermediaries (who themselves use

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\(^8\) UK Government, *UK aid: tackling global challenges in the national interest* (November 2015)
\(^9\) DFID (*CON0039*) p6
\(^{10}\) Dr James Morton (*DUC0003*) p1
agents and intermediaries), thus the World Bank, WFP and Oxfam may all be considered DFID contractors. However, for the purpose of this report it is private sector organisations that the term refers to.

It should also be noted that there is considerable diversity within this classification of ‘contractors’. For example, “Options”, one of DFID’s ‘Key Suppliers’, is a subsidiary of a charity (Marie Stopes International (MSI)). Therefore, unlike other contractors, it pays no dividends to shareholders and all surplus funds are given to MSI as Gift Aid.\(^{11}\)

Box 1: Bilateral, multilateral and bilateral through multilateral aid delivery

UK official development assistance (ODA) spending (by DFID and other government departments) is split into two core streams: bilateral (all aid provided by donor countries when the recipient country, sector or project is known) and multilateral (delivered in the form of core contributions to multilateral organisations, including the European Union). These streams were valued at £7.7 billion and £4.5 billion respectively in 2015. However, these figures do not reflect the full amount channelled through multilaterals, as sometimes multilateral organisations are selected as the delivery partner for bilateral programmes. £2.2 billion of UK bilateral ODA was spent in this way in 2015.

Figure 2: DFID spending through various channels

Note: Total DFID spending corresponds to 2015/16 but due to availability of statistics, the bilateral breakdown is drawn from figures from 2014/15, 2015 and 2015/16

Source: DFID, Statistics on International Development 2016 (Table 10), written evidence (CON0039) and Annual Report and Accounts 2015–16

9. DFID spent £1.24 billion through contractors in 2015/16, which comprises 20% of bilateral spend and 13% of DFID total spend in that year. While this represents an increase in recent years (see figure 1 on page 4), it is low relative to other donors. 29% of funds awarded by the US in 2016 were through contractors (US$4.7 billion),\(^{12}\) while the share of ‘official support’ from Australia’s Department of Foreign Affairs and Trade (DFAT) delivered through the private sector in 2014/15 was 24% of total spend (AUS$1.4 billion).\(^{13}\) Within the UK Government, DFID’s use of contractors is also relatively low. In a 2013

11 Options Consultancy Services Ltd (CON0006) para 7
report, the National Audit Office (NAO) stated that central government departments spent £40 billion through third parties in 2012–13. The NAO estimates that DFID accounted for less than 2% of this (making it the eleventh largest department in contractor spending) while the Ministry of Defence accounted for around half of all government spending via contractors.\textsuperscript{14}

Selecting a delivery channel

10. DFID’s Smart Rules, the operating framework for DFID’s programmes, set out the key role of the business case in determining the channel through which a given programme is to be delivered. The business case describes the need for a programme, what it will do and in what timeframe, sets out expected achievements and serves as a report to the public on how taxpayers’ funds are being used. It includes an appraisal case, which should explore the variety of options for how DFID will address the strategic need for the programme in a way that optimises value for money.\textsuperscript{15} ICAI raised concerns about the way in which business cases are used for appraisal in its 2015 report ‘DFID’s approach to delivering impact’. It wrote “They appear to set out a justification for design choices that have already been made, rather than offer a robust appraisal of options.”\textsuperscript{16} This was supported by oral evidence from Joy Hutcheon, DFID Director General, Finance and Corporate Performance, who told us:

“We would like to see a strengthening of the appraisal case. We think sometimes teams rush a bit to the option. [ … ] It is a robust process, but there are improvements we can make to it.”\textsuperscript{17}

11. With respect to appraising delivery options, Dr James Morton also felt that: “It is not clear that DFID has a clear framework to guide this central strategic choice.”\textsuperscript{18} This reaffirms past ICAI findings. In its 2013 report on DFID’s use of contractors, ICAI stated that DFID “lacks strategic guidance [ … ] on how to use contractors to best effect, including the circumstances in which contractors should be used and which contractor skills are most valuable.”\textsuperscript{19} While DFID responded referring to a Departmental review of strategic choices in 2013, evidence suggests that concerns remain. As ICAI reported, DFID does not have “an overall process for assessing how the use of contractors compares with other channels for delivering aid.”\textsuperscript{20}

DFID staffing

12. One of the stated advantages of DFID’s use of contractors is that it allows the Department to engage in a wide range of contexts and types of intervention that it would not have the capacity to deliver through in-house staff. In written evidence, ASI cited a report that estimates that if DFID were directly to implement its programmes, it would have to recruit an additional 25,000 to 30,000 personnel.\textsuperscript{21} According to Crown Agents, outsourcing services to contractors “allows DFID to have flexibility and speed to its

\textsuperscript{14} National Audit Office, Managing government suppliers (November 2013)
\textsuperscript{15} DFID, DFID Smart Rules: Version VI (last updated 3 October 2016) p57
\textsuperscript{16} ICAI, DFID's approach to delivering impact (June 2015) para 2.47
\textsuperscript{17} Q47
\textsuperscript{18} Dr James Morton (DUC0003) p1
\textsuperscript{19} ICAI, DFID’s Use of Contractors to Deliver Aid Programmes (May 2013) para 2.13
\textsuperscript{20} ICAI, DFID’s Use of Contractors to Deliver Aid Programmes (May 2013) para 2.147
\textsuperscript{21} Adam Smith International (CON0003) para 2.4.5
response, access to wide reaching technical experts, drive more targeted VFM [value for money] and support services tailored directly to the local context and DFID strategic objectives than compared to other programme delivery channels.”

13. However, there are also concerns that DFID’s approach to using contractors to deliver aid programmes is a necessity owing to the growing aid budget rather than a strategic choice. As Bond stated in written evidence:

“The decisions about when and where DFID uses contractors are internally driven, and not much is known about the decision-making process. It is widely recognised that because the increased aid budgets—which have, overall, enabled DFID to increase its impact in tackling global poverty and inequality—have not been matched by increased staffing levels with DFID, a greater use of contractors has become inevitable. It has also resulted in more ‘light touch’ management, with little time for field visits, etc.”

14. The decision processes that determine DFID’s use of contractors are a long-standing concern. In a 2011 report, our predecessor Committee considered DFID staffing and use of contractors and concluded “the use of external suppliers should be determined by assessing the best way to achieve outcomes, not by external constraints on administrative costs or staffing levels.” In our recent report ‘UK aid: allocation of resources’ we note that “DFID’s administrative capacity appears to have fallen below what is required to spend its increasing budget effectively.”

15. Figure 3 below shows the growth in the aid budget in proportion to the growth in DFID staff numbers since 1998, the year after the Department was founded. The pressures on the Department underlying this trend were clearly stated in written evidence from Crown Agents “DFID is expected to achieve more, despite having less staff.”

22 Crown Agents (CON0031) para 3.1
23 Bond (CON0040) para 6
26 Crown Agents (CON0031) para 3.1
16. In oral evidence, Joy Hutcheon reiterated DFID’s role as a commissioning organisation in the context of staffing, saying “we are not equipped, in terms of staff members, to be a delivery organisation; we are a commissioning organisation [ … ]”. However, even in taking such a role, there is a requisite level of resources and technical expertise to effectively oversee delivery. As Palladium wrote in evidence “for partnership to be successful, DFID staff must retain both the capacity and the ability to oversee the delivery of these programmes and to work in partnership with their supply base across a range of technical and operational issues.” International development company and contractor DAI added to this, stating:

“DAI would welcome greater investment by DFID in its technical depth. It is important for DFID’s implementing partners to have a technically capable partner in the field. A “hollowed out” DFID would be a less effective department: less able to achieve its development mission, less able to design, award, and monitor development programming.”

17. We recognise that in DFID’s role as a commissioning organisation, there are numerous advantages associated with contracting outside expertise. However, despite the value that contractors can bring, there are certain functions that in-house staff must serve and which cannot be outsourced. With both the size and number of contracts growing, there are increasing pressures on staff who, even with the assistance of commercial advisers, may not be equipped with the necessary skills and expertise to manage the technical, operational and commercial aspects of such large and complex programmes. Replacing development expertise with commercial expertise or overburdening staff is likely to have implications for the effectiveness and impact of programming. Evidence suggests that the decision-making process at the core of programme design—which channel to use—needs to be strengthened.
18. We urge the Department to ensure that the choice of implementing a given programme through contractors is always driven by the strategic value of that delivery channel. DFID Smart Rules should include more detailed guidance on the appraisal portion of the business case, and business cases should clearly justify why the particular channel was chosen, with reference to the relative benefits over other types of delivery. DFID should ensure that the emphasis on commercial expertise associated with the increasing use of contractors does not make generalists of DFID staff at the expense of technical knowledge and depth.

19. Questions were raised about DFID’s use of contractors by our predecessor Committee in an inquiry into Recovery and Development in Sierra Leone and Liberia. In its 2014 report, the Committee recommended that DFID “investigates the potential to set up an arm’s-length wholly or partially-owned consultancy that can either challenge these other providers and help to drive down costs or provide a greater pool of expertise.” Evidence to that inquiry suggested that some contractors have “limited experience and understanding of social programming.” The idea of an arms-length body was also raised by Contractor B in evidence to this inquiry. In its response to the 2014 report, DFID ‘partially agreed’ with this recommendation, and added that it has “established a commercial capability reform programme, building commercial capability within DFID.” However, there was no clear indication in the Government response that an arms-length body was being investigated. Joy Hutcheon said that:

“In a world where we were able to have a discussion with [the] Treasury about the implications of that for our running costs, that would be a very interesting proposition. I know you have discussed that with the Permanent Secretary on a number of occasions but that, at this stage, is not the world we are in.”

20. Evidence to this inquiry and past IDC inquiries has suggested that an arms-length body to assume some project management responsibilities could be beneficial in both strengthening the expert oversight in DFID projects and deepening competition in the market. It is our view that such a body could contribute towards a suitable balance between in-house and outsourced expertise. It would also afford DFID greater direct scrutiny of contract-based delivery, a notable advantage given recent questions surrounding contractor conduct. We repeat earlier calls for DFID to investigate the idea of an arms-length body to assume programme management responsibilities. This should be done as part of its Supplier Review and the outcome reported to us. If DFID disagrees with this or believes it is not feasible, it should set out why in its response to this Report.

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29 International Development Committee, Sixth Report of Session 2014–15, Recovery and Development in Sierra Leone and Liberia (October 2014) para 50
30 Plan UK (SLL14) p2
31 Q40 (See Annex 1)
33 Q69
DFID’s use of private sector contractors

Contractors and fragile states

21. In its Aid Strategy, the Government committed to allocating 50% of all DFID’s spending to fragile states and regions, up from a previous target of 30%. In certain fragile and conflict-affected states (FCAS), the majority of DFID programming is delivered through contractors. A 2014 report from the Organisation for Economic Cooperation and Development (OECD) found that 75% of DFID’s bilateral programme in Nigeria (DFID’s third largest in 2016/17), which is designated by the Department as a fragile state, was spent through contractors.

22. In response to questions on the impact of the fragile states agenda on DFID’s use of contractors, Nick Ford, Head of DFID’s Procurement and Commercial Department, said: “It is not necessarily right to say that, because we work in FCAS, we are going to do more through contractors. It would depend on the nature of the programme.”

However, DFID’s written evidence stated that growth in the number and total value of supplier contracts awarded “is driven by the shift towards fragile and conflict-affected states where financial aid and delivery route options are limited [...].” Comparative advantages of contractors in FCAS were highlighted in written evidence and include flexibility and adaptability in rapidly changing environments, access to relatively dangerous locations and the ability to maintain a low profile to keep security costs down (relative to multilaterals). It is thus feasible that, even on a case-by-case basis, increased spending in FCAS may be associated with an increased dependence on contractors. While contractors may represent a useful tool for DFID in delivering on its FCAS commitment, there are some key considerations that go with this.

23. Firstly, the Stabilisation Unit, a cross-government unit supporting UK government efforts to tackle instability overseas, identified certain challenges associated with partnering with for-profit organisations in FCAS. In its guidance note on outsourcing conflict, justice, security and stabilisation work, it wrote: “[…] profit motives of implementing partners can at times be in tension with other objectives, and tensions between private companies and other state and non-state actors can affect overall impact, coordination the quality of partnerships. Unless HMG commits sufficient time to programme management, delivery can get divorced from HMG’s political strategy.”

While robust programme management is particularly important in FCAS, it is in such environments that this is most challenging to deliver. As Joy Hutcheon noted “there are security and duty of care implications, and the access for monitoring is restricted.”

24. Secondly, the Government’s November 2015 Aid Strategy also committed to an expansion of payment by results (PbR). This Committee has previously expressed...

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34 UK Government, UK aid: tackling global challenges in the national interest (November 2015) p4  
35 OECD, OECD Development Co-operation Peer Reviews: United Kingdom (November 2014)  
36 Q64  
37 Coffey International Development Ltd (CON0029) para 17  
38 Stabilisation Unit, Outsourcing conflict, justice, security and stabilisation interventions (March 2016) p17  
39 Q62
reservations about whether there is sufficient evidence to support increased use of PbR, though there are particular issues with its use for contracts in FCAS. In ICAI’s 2014 report on delivering impact, it referred to PbR as a way of shifting risk from DFID to the implementer. However, in FCAS “many of the risks are beyond the control either of DFID or the supplier. In such cases, shifting the risk to the supplier may simply drive up costs for the aid programme as a whole.”

25. In its 2015 Aid Strategy, the Government committed to allocating 50% of all DFID’s spending to fragile states and regions, up from a previous target of 30%. While DFID decides on the delivery channel for its programmes on a case by case basis, any perceived comparative advantage held by contractors is likely to result in their increased use. We share the Stabilisation Unit’s concerns about possible tensions between profit motives and programme objectives in fragile states. We also question whether the shifting of risk to contractors through Payment by Results (PbR) is likely to lead to substantially higher risk premiums which are then reflected in the cost of contracts. We note that with fewer contractors operating in such difficult environments this may have implications for market competition and value for money.

26. DFID should ensure the use of contractors in fragile states is carefully managed and that output targets are designed to align profit incentives and development objectives whilst still taking account of drivers of conflict. DFID should be particularly cautious about shifting risks onto contractors in fragile states through PbR. It should also ensure that all overheads and profits are benchmarked against other donors and recipient countries to ascertain whether DFID is achieving value for money.

Learning through contractors

27. In ICAI’s 2013 review, one of the major issues raised was concerned with how DFID learns from programmes implemented by contractors—an area which ICAI gave an Amber-Red assessment. ICAI found:

“Interviews with DFID staff show a low level of learning being disseminated from the contractors to the local DFID programme teams and, in turn, to headquarters. […] There is no process which draws all the learning together and no process for setting strategic guidelines about the future circumstances in which using contractors would be advantageous.”

28. DFID accepted the ICAI recommendation in this area, and said that it would take steps including asking contractors to “propose practical ways to bring their insights and learning from programmes back into DFID and to share these across programmes.” In oral evidence, Nick Ford referred to a number of practical measures implemented to improve learning, including: DFID’s annual supplier conference; specific and targeted forums throughout the year; DFID’s supplier relationship management programme; and early

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41 ICAI, DFID’s approach to delivering impact (June 2015) para 4.41  
42 An Amber-Red assessment means: The programme performs relatively poorly overall against ICAI’s criteria for effectiveness and value for money. Significant improvements should be made.  
43 ICAI, DFID’s Use of Contractors to Deliver Aid Programmes (May 2013) para 2.140 and 2.147  
44 DFID, Management Response to the ICAI recommendations on: DFID’s Use of Contractors for Aid Delivery, May 2013 (June 2013) p3
market engagement programmes used to scope the market and better inform programme design.\textsuperscript{45} However, evidence to this inquiry suggests that further improvements still need to be made.

29. Joy Hutcheon and Nick Ford made it clear in oral evidence that DFID believes that suppliers are forthcoming in sharing their learning, with the shared incentive of the “greater good” meaning that there is “a general ethos in the sector that people want to share learning”.\textsuperscript{46} However, evidence from Bond challenges this view:

“[… ] private contractor legal departments are attempting to impose increasingly heavy intellectual property clauses on sub-contractors working on programmes with them. These try to establish ownership on approaches and materials coming out of programmes and to require sub-contractors, who are often responsible for developing these, to seek permission for their use. Bond members feel this is inappropriate for publicly funded programmes and is detrimental to learning and sharing about what works and does not work.”\textsuperscript{47}

It is certainly true that many staff operating in difficult circumstances on the ground are motivated by the development cause and will therefore share all their learning. However, recent reports on the conduct of certain contractors have raised questions over whether this can be considered a reliable assumption, particularly given the commercial advantage that learning gives to an organisation over its rivals.

30. Palladium wrote that: “We see the main opportunity for improvement being for DFID to specify and prescribe learning objectives for all contracted programmes, and to formalise the need for collaboration and sharing across the portfolio.”\textsuperscript{48} In line with Palladium’s written evidence, it does not appear that DFID includes concrete expectations on sharing learning in its delivery contracts with suppliers. An example is one contract with Maxwell Stamp PLC for a social protection programme in Bangladesh which makes no reference to “learning” or “knowledge-sharing”.\textsuperscript{49} “This is a poorly performing project that received a ‘B’ rating in its most recent annual review.\textsuperscript{50} While many of the project performance issues are not the fault of the contractor (terror incidents made international staff recruitment and retention more difficult), it is concerning that there is no contractual obligation for the supplier to give feedback to DFID on what it has learned.\textsuperscript{51}

31. Bond raised concerns that DFID annual reviews—a vital tool for learning and improving future programming—are “increasingly becoming box-ticking exercises rather than real opportunities for DFID’s own learning.” Bond again links this back to staffing constraints as DFID staff may lack the “necessary time or indeed skills to engage with the realities of these quite complex programmes.”\textsuperscript{52} A related concern was highlighted by an experienced contractor in confidential evidence:

\textsuperscript{45} Q51  
\textsuperscript{46} Q57  
\textsuperscript{47} Bond (CON0040) para 22  
\textsuperscript{48} Palladium (DUC0008) p7  
\textsuperscript{49} DFID 6600 Service Provider for Strengthening Government Social Protection Systems for the Poor (SGSP) in Bangladesh  
\textsuperscript{50} By DFID’s rating system, a ‘B’ rating means that ‘Outputs moderately did not meet expectations’  
\textsuperscript{51} DFID, Strengthening Government Social Protection Systems for the Poor (SGSP) in Bangladesh: Annual Review (November 2016)  
\textsuperscript{52} Bond (CON0040) para 6
“The biggest single structural weakness in the international development consultancy market is the apparent conflict of interest in the role of many of the firms that DFID employs to undertake reviews of its projects. [ … ] This can and does 1) lead to misleading results claims, and 2) undermine effective learning from experience.”

The OECD Development Assistance Committee (DAC) guidelines state that evaluations should be “independent from the development intervention, including its policy, operations and management functions, as well as intended beneficiaries.” DFID stated that the independence of a review “will vary depending on the particular circumstances of the programme.” There is no clear guidance in DFID’s Smart Rules as to when evaluations should be conducted independently.

32. While DFID is a key purchaser of development contractor services, it is not the only donor in the international market. DFID contributed 13% of all ODA flows from DAC donors (through all channels) in 2015, and there is undoubtedly much to learn from the other 87%. Other major donors use very different contracting models, such as USAID’s “cost-plus” contracts where there is a fixed management fee at the inception of the contract, and the remuneration framework used by Australia’s DFAT in determining consultant fees. Nick Ford told us of some work he had recently done with UNOPS in Jordan which he said was “really insightful, and it made me think about how we could use our commercial advisers more in country to do similar events.”

33. DFID has taken some key steps towards improving the way it learns through contractors, though concerns remain about whether this knowledge is effectively extracted and internalised. The assumption that contractors are keen to share learning for the greater good overlooks the fact that, as for-profit companies, there is a strong commercial incentive to withhold information from DFID and potential competitors. We stress the importance of independent evaluations, and note that there appears to be little clear strategy to determine the degree of independence in evaluations across various programmes. A number of other donors use very different contracting models which are likely to have their own advantages and disadvantages.

34. As part of DFID’s Key Supplier Management (KSM) system, it should apply a metric on the contractor’s contribution to DFID learning, including how cooperative they are with other contractors. Other innovative approaches should also be explored in the Supplier Review. DFID should use guidelines on best practice to set out clear regulations in its updated Smart Rules on when programme evaluations should be done completely independently of both DFID and contractor staff. It should also foster closer relationships with the procurement departments of other donors as well as multilateral agencies to try to learn about what works in different procurement models.
3 Procurement processes

35. A key part of ensuring effective delivery through contractors lies in the procurement processes that DFID employs to secure the best supplier for the job. OECD DAC guidelines stress the need for effective procurement systems among donors, stating that “good public procurement systems are central to the effectiveness of development expenditure”.\(^5^6\) In recent years, the Department has introduced several innovations that have influenced the shape and behaviour of the supplier market in an attempt to ensure better management. One example is the increased use of framework agreements between DFID and a number of contractors, pre-qualifying those contractors against its criteria in a number of implementation areas. DFID’s Procurement and Commercial Department (PCD) was also one of the first teams in UK Government to adopt the new ‘Competition with Negotiation’ EU procurement process in 2015, ensuring that incumbency does not guarantee the winning of future contracts. This is intended to allow for “the maximum opportunity for DFID to negotiate with suppliers” affording the Department a stronger negotiating position.\(^5^7\) The value of effective, responsive procurement systems has been recently demonstrated in the case of DFID’s response to the Ebola crisis (see Box 2).

Box 2: Procurement and rapid responses: the Ebola crisis

In our January 2016 report ‘Ebola: Responses to a public health emergency’, the Committee found that, after a Public Health Emergency of International Concern (PHEIC) was eventually announced, DFID responded swiftly to address the outbreak.\(^5^8\) This was due, in part, to PCD’s ability to quickly launch a procurement exercise to secure the necessary skills/materials through its rapid response procurement process, which DFID stated in written evidence “is fully compliant with the regulations but enables DFID to source rapidly in cases of extreme urgency”.\(^5^9\) This was vital given the need to quickly stop the spread of the disease. DFID was able to source six treatment centres in eleven days through this process, as well as providing Personal Protective Equipment and vital medicines, medevac services, three Ebola Laboratories, Facilities Management for the Treatment Centres and placing team members in-country to manage the daily supply chain logistics.

36. PCD has been recognised for its procurement practices, winning a number of awards from the Chartered Institute of Purchasing and Supply (CIPS) in recent years. These awards were for work in sourcing contraceptive implants for 27 million women across the developing world and the purchase of long lasting insecticide treated bed nets, anti-HIV drugs and other products.\(^6^0\) We commend PCD for its efforts in driving down costs and delivering value for money for the taxpayer. We also note that in delivering on DFID’s objective of poverty reduction, DFID needs to do more than procure products and so much of its procurement activity is of a fundamentally different nature. Procuring goods is a key element of DFID’s work, but a significant share of programming focuses on goals related to institutional change—such as delivering better healthcare and education systems or stronger governance and rule of law. Through procuring services to support

\(^{56}\) OECD DAC, Harmonising Donor Practices for Effective Aid Delivery (2005)
\(^{57}\) DFID (CON0039) p8
\(^{59}\) DFID (CON0039) p7
\(^{60}\) DFID Annex (CON0039) p217
these objectives DFID has created a very different type of market. Evidence to this inquiry has suggested that DFID does not understand this market sufficiently well. In the process of this inquiry we took oral evidence from two contractors in confidence, who will hereafter be known as Contractor A and Contractor B. Contractor B raised concerns in oral evidence that “they [DFID] make a market and that market does not work well, because they do not understand it sufficiently well.”

**Procurement issues**

37. An issue affecting the competitiveness of the DFID supplier market is the different information that each potential contractor has, with some contractors having more information than others. This can give some suppliers an unfair advantage and undermine market competition. One example is instances where procurement-sensitive information has been poorly handled by DFID. DAI Europe highlighted two cases in written evidence where information was found online containing detail beyond that included in the invitation to tender. While we commend DAI Europe for reporting this information to DFID, we are concerned that there may be more unreported instances where contractors may have gained an advantage by using such information to strengthen their bids, distorting competition in the market.

38. Other concerns were raised in evidence about contractors’ ability to bid for the research work that feeds into programme design. Contractor B gave an example of where a major contractor won a DFID research contract by undercutting a more qualified organisation. The contractor then was able to conduct this research and feed into the design of future programming, with the intention of using the insight it had gathered to ensure it was “ahead of the game” in any future tenders. Nick Ford told us that in such a case, the organisation might be excluded from bidding for related future work:

> “If it had given them any perceived unfair advantage, then absolutely they would not be allowed to bid. If it was purely level and all the information was in the public domain, then potentially they could.”

However, Nick Ford added that this power to exclude bidders “is not a carte blanche, because you need to be reasonable and proportionate under the regulations.” Procurement regulations can place a bind on DFID in this respect, as they restrict its ability to exclude bidders. In cases where bidders are not excluded it is not clear that DFID actually has the capacity to guarantee a genuinely level playing field. Contractor B told us that sharing information with potential suppliers at the bidding stage is not enough, as the organisation who took part in the research “will have already tied up the best consultants, talked to the local partners, got better information, got their consortium together, etc.” Similar concerns about the input of firms in project design were raised by ICAI in its recent report on the cross-Government Prosperity Fund.

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61 Q2 (See Annex 1)
62 DAI Europe (DUC0002) para 4
63 Q40 (See Annex 1)
64 Q40 (See Annex 1)
65 Q101
66 Q101
67 Q40 (See Annex 1)
68 ICAI, The cross-government Prosperity Fund: A rapid review (February 2017) para 3.37
39. We have also heard a number of complaints about delays and cancellations in DFID procurement. In written evidence, Mott MacDonald stated “we note that the time between issuing a tender and contract starting has considerably lengthened in recent years due to increased procurement scrutiny.” DAI Europe wrote “when contracts are delayed for longer, it can become difficult and costly to retain a proposed team and the assumptions underpinning a project design begin to erode, often requiring re-designs.” Coffey added that “long delays can also erode local stakeholders’ and beneficiaries’ trust in the supplier and in DFID’s commitments. This, in turn, can hinder effective delivery.” While the appropriate level of procurement scrutiny is vital, associated delays have the potential to undermine the benefits of contractors as an effective channel for aid delivery.

40. Coffey International Development Ltd also noted an increase in the number of procurement cancellations and retenders, specifically citing five cancellations in the last eight weeks (at the time of writing). DFID did not acknowledge that there had been a recent increase. Such cancellations have serious implications for suppliers due to the high costs associated with bidding for DFID work—contractors told us that the costs of preparing a bid can be as high as £120,000 in the case of a large project due to the research, information and time required in preparing a bid. A cancelled tender is a lost investment to the contractor, and the costs of this are ultimately borne by the UK taxpayer as this loss is then recovered through the overheads charged for the next project. While we recognise that there may be instances where cancellation is necessary and desirable in some cases—it is better to cancel a tender at a relatively small loss than to misallocate millions in taxpayers money—we stress that DFID should ensure that such cancellations are minimised.

41. A related issue is that the cost of bidding is prohibitive for many smaller suppliers. As one contractor wrote:

“The cost of bidding for DFID contracts has increased significantly in recent years. In our experience, DFID tenders are more expensive to submit than those of other donors, and certainly of our private sector clients. This is due to both the competitive nature of the market and also the depth of content that DFID requires. We believe this represents a significant barrier to entry for both new and small firms.”

42. We commend the ability of DFID’s procurement processes to source development interventions quickly when needed, particularly in the case of the Ebola crisis. While DFID should be recognised for using effective procurement to drive down the costs of goods such as bed nets and vaccines, we believe that the majority of DFID programming—such as improving governance—involves a very different approach than that of commercial procurement of goods. We are concerned about instances where procurement-sensitive information has been available to some bidders and not others, and also about the limitations on excluding bidders (imposed by procurement

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69 Mott MacDonald (See Annex 2)
70 DAI Europe (See Annex 2)
71 Coffey International Development Ltd (See Annex 2)
72 Coffey International Development Ltd (See Annex 2)
73 Q128
74 Coffey International Development Ltd (See Annex 2)
75 Confidential (See Annex 2)
DFID’s use of private sector contractors

regulations) who have had a role in the programme formulation. Delays and cancellations are also a concern, and high (and rising) bidding costs are likely to work against DFID’s stated desire of expanding the supplier base.

43. **DFID must make every effort to level the playing field in terms of information available.** While we recognise that mistakes can be made in the way procurement-sensitive information is handled by staff, this can be overcome through greater transparency from the outset—publishing all information so that no single or group of bidders is at an advantage. Where a procurement is delayed or cancelled, DFID should take lessons away from this so similar events can be avoided in the future. Additional bidding requirements that come out of the Supplier Review should not impose significant additional costs on contractors, as these may drive those least placed to bear them (i.e. smaller organisations) out of the market thus reducing competition.

Framework agreements

44. Framework agreements are used by DFID as a means to streamline the procurement process. They enable PCD to simplify a two-step process—pre-qualification followed by tendering—to focus efforts on the tendering stage. By establishing a pre-qualified set of potential bidders through the framework, it allows DFID to tender in a single stage where only firms (or consortia of firms) appointed to the framework can bid. DFID currently has five active frameworks, containing 63 lead suppliers, and suppliers awarded frameworks undergo due diligence, technical assessment and benchmarking of fee rates to ensure value for money. In written evidence, DFID stated that:

> “DFID uses frameworks as they are fast, efficient and easy to use. Internal reviews of current frameworks have shown that their use reduces the procurement timescale by 30% on average. A single supplier framework was recently re-tendered and is now delivering fee rates 15% lower on average than the original framework.”

While the streamlining logic behind framework agreements is apparent, concerns have arisen about the way that they operate.

45. The main problem with framework agreements expressed in evidence is that they can have the effect of “locking out” organisations from bidding—particularly smaller ones. Contractor B told us that:

> “Where increasing amounts of DFID work are let through framework contracts, if you are not on the right framework, you are simply locked out. […] Frameworks have been useful in terms of streamlining procurement, but they have been quite rigid and restrictive in terms of market access, particularly for smaller players.”

Public Administration International, a micro contractor itself, wrote that “DFID is making too little use of small, expert, technical suppliers and pays too little attention to how its commissioning affects small suppliers.” Another small contractor with professional experience in fragile states told us that they were ineligible to bid for work because they

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76 DFID Annex A (DUC0018) p11-12
77 Q5 (See Annex 1)
78 Public Administration International (CON0016) p1
were not on the FCAS framework. They reported that when they asked DFID how they could become part of the framework, they were told they could not apply to join until the framework was retendered.\footnote{Confidential written evidence (DUC0001) p1} They were completely locked out.

46. DFID told us both in written and oral evidence that current frameworks and opportunities are widely advertised; on the Gov.uk website, in the European Journal, on DFID’s supplier portal and through the DFID Procurement Twitter account.\footnote{DFID Annex D (DUC0017) p2} However, it cannot be assumed that advertising frameworks alone makes them accessible, particularly to smaller contractors. Nathan Associates wrote that:

“There has at the time of developing these frameworks been very limited clarity as to how they will actually work and what will be tendered through them. This made it difficult for smaller firms to ‘lead’ in lots and most were pushed towards a ‘tier 2’ role in which they participate as sub-contractors to the ‘lot leaders’. DFID is now moving towards new frameworks for private suppliers to participate in, with new rules once more and again, at this time it is very unclear how they will emerge. Each of DFID’s procurement routes needs clearer rules and guidance. When questions are asked to seek clarity, the responses often fail to give a definitive answer. The complexities, uncertainties and lack of clarity of DFID procurement systems also act as an unintended barrier to entry for new firms, particularly smaller firms.”\footnote{Nathan Associates (DUC0005) p3}

47. We are concerned about the rigidity of frameworks that apply over such a long time period, as several of DFID’s frameworks have a life of four years which means suppliers—particularly smaller ones who are less aware of the processes involved in gaining access—can be locked out for lengthy periods.\footnote{DFID, \textit{Procurement at DFID} (accessed 13 March 2017)} In guidance on ‘How to Prepare and Evaluate Tenders’, the CIPS states that the procurement organisation “should have some idea as to which organisations are likely to be potentially suitable supply sources”. However, it also notes “the disadvantage of this approach is that the systems need to be kept continuously up-to-date.”\footnote{Chartered Institute of Procurement and Supply, \textit{How to Prepare and Evaluate Tenders} (2013) p1} A review of DFID Frameworks by ADS Group, a trade organisation for UK companies UK aerospace, defence, security and space sectors, found that “Framework Agreements quickly became out of date; they did not reflect rapid changes in the nature of the supplier base.”\footnote{ADS Group, \textit{Review of DFID Framework Agreements} (accessed 13 March 2017)} Framework agreements need to be updated more regularly in order to be effective.
48. The disadvantage for smaller contractors caused by framework agreements was also supported by evidence from larger firms. The Centre for Development Results, wrote of changes to the Economic Development Framework and stated that:

“[ … ] smaller companies may struggle to demonstrate track record and ability to absorb the risk associated with programmes in such narrowly defined terms. [ … ] While frameworks have the ability to help make and shape markets, DFID has demonstrated a lack of technical understanding of the impact of these changes on the supply chain.”

49. Smaller organisations do have the opportunity to participate in work procured through frameworks by forming consortia to offer specialist skills under the leadership of the prime contractor, though the way this operates in practice can also be problematic. Public Administration International wrote that, from a smaller organisation’s perspective “the system seems to have the effect of excluding them from bidding and from being included as genuine partners in work programmes, as opposed to having their names included to add superficial credibility to proposals.”

Another small contractor stated in confidential written evidence:

“If you didn’t sign up to one of the big contractor consortia at the time, you’d be out in the cold ever since. If you did sign up, then you’re “locked in” to that lead firm and that consortia. There’s no freedom of association. This restricts access and choice to DFID, and reduces the power and influence of smaller firms within any consortia [ … ]”

DFID was very clear in evidence that it does not condone these kinds of exclusivity agreements where smaller contractors are bound to larger firms, though in practice this appears to be a feature of the market.

50. These concerns are not new. In evidence to our predecessor Committee’s inquiry into DFID’s Annual Report and Accounts 2013–14 submitted in December 2014, The Springfield Centre wrote:

“DFID has historically benefited from the technical expertise of smaller, specialist organisations which are able to be more agile and innovative. However, now these organisations are beholden to large contractors, their ability to shape the work they do is limited and they become task-based consultants with less control of technical delivery. They are obliged to comply with the demands of larger contractors, having been unable to meet compliance requirements to be eligible for the framework agreements.”

In its report, the Committee asked the question “does DFID understand how its way of commissioning is affecting suppliers as a sector, and not just in terms of the effectiveness of individual procurement decisions?” Evidence to this inquiry over two years later suggests that the answer to this question remains unclear.

85 Centre for Development Results (DUC0007) para 6.3
86 Public Administration International (CON0016) para 4.4
87 Confidential written evidence (DUC0015) p3
88 Q83
89 Springfield Centre (DAR0003) para 21
51. DFID informed us that steps are being taken towards improving frameworks. In oral evidence, Nick Ford told us:

“DFID has put in place a number of frameworks since 2011–12, when we did our first wave of frameworks. We are now on to our second wave. We have taken on board quite a lot of learning from the first wave in the new set that we are running. [ … ] we are taking on board a lot feedback about what has worked well and what has not.”

However, it appears that the wider trend across government is moving away from frameworks. In her former role as Chief Executive of the Crown Commercial Service (CCS), Sally Collier was reported as saying there had been a 40 per cent cut in the number of framework agreements as the CCS moved to “new contracting models”. Why DFID has moved into a new phase of framework agreements while the rest of government moves away from them is unclear.

52. We recognise that there are benefits to framework agreements, including the time and cost savings generated through greater administrative efficiency. However, there is a strong suggestion from evidence to this inquiry that they lock out organisations—particularly smaller ones with technical expertise—from bidding for DFID work. They can force smaller contractors into ‘second tier’ roles where their power and influence is reduced. In order for frameworks to work as intended and avoid narrowing the supplier base, they need to be updated regularly which is not current DFID practice.

53. DFID should undertake a review of framework agreements and justify how their benefits outweigh the costs reported in evidence to this inquiry. Where framework agreements are used, DFID should commit to regular reviews and updates, allowing new market entrants access to bid for existing frameworks at more regular intervals. DFID should also consult with smaller organisations on how to make bidding for frameworks more accessible, offering tailored guidance to ensure that its procurement processes are not a barrier to entry. DFID should also justify why it continues to use framework agreements when the trend across government is moving away from them.
4 DFID suppliers and the supply chain

Market competition

54. In oral evidence, Nick Ford, Head of Procurement and Commercial Department (PCD), DFID, explained the principle that underscores the Department’s approach to the contractor market:

“If we go down a procurement or contracted route, as opposed to a multilateral or NGO route, it is around cost, transparency and competition. […] We obviously follow public procurement regulations, which are all about open and fair competition and trying to create more competitive markets, using market forces.”

Box 3: What is market competition and why is it important?

55. In the context of DFID’s supplier market, competition is where the suppliers (contractors) compete with each other to satisfy the wants and needs of the consumer (DFID). If the market is competitive, suppliers will attempt to outdo each other by pushing prices down or increasing quality, which can lead to better value for money through greater development impact at lower costs. In a competitive market, businesses will also try to make their services different to distinguish themselves from competitors, driving innovation and offering a wider choice of suppliers that can specialise in different areas across the range of DFID programming. DAI Europe stated in written evidence “for our client, for the taxpayer, and for development as a whole, competition yields lower costs, better value, superior technical innovation, and more diverse technical choices.” This view was also summarised more broadly by Michael Grenfell, Competition and Markets Authority (CMA) Executive Director for Enforcement, in a recent speech:

“Competition harnesses that desire of businesses to make money, and directs it to the public good. And that’s why competition is so valuable.”

Therefore, the assumption that it procures from a competitive supplier market is key to DFID’s strategy in its use of contractors.

56. Some of DFID’s major suppliers stated in evidence that there are signs of healthy competition in its supplier market. Palladium wrote that:

“Over 200 companies attended DFID’s last supplier conference, and the number increases each year. No single company accounts for a market share of greater than 10% of the UK aid expenditure delivered through contractors. DFID performs better than other donors. In Australia, three firms win 69% of contracts, in the US more than 50% of contracts are won by five companies.”

However, much of the confirmation of market competitiveness has been from contractors themselves as well as DFID, while other sources have been less convinced.

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93 Q65
94 Michael Grenfell, What has competition ever done for us? (Speech at the Institute of Customer Service annual conference, 7 March 2017)
95 Palladium (DU/C0008) p4
57. One experienced development professional wrote in confidential evidence that while: “competition at the point of tendering is intense […] at the same time there are structural features of the way that the market is organised that undermine competitive pressures.”

One of these features that has been frequently raised in evidence is the access—both formal and informal, centrally and in country offices—that larger suppliers have to DFID staff. One example raised is through the Key Supplier Management (KSM) system that DFID uses to maintain strategic relationships with major suppliers. Information from the Chartered Institute of Purchasing and Supply (CIPS) states that such collaborative relationships can have benefits to the supplier, including:

- The supplier will be kept informed of the buyer’s forward plans;
- The supplier will gain a much better understanding of the buyer organisation and its needs; and
- The supplier is likely to get more business from the buyer, as a preferred supplier.

58. DFID insists that suppliers in the KSM do not receive any preferential treatment, however confidential written evidence stated "the key supplier group by definition provides real or perceived privileged access to DFID people and information for a small group of established suppliers." Another contractor wrote that these suppliers meet with DFID officials on a regular basis while others “not on the small elite list have no such access to DFID.”

A related concern is the in-country access to DFID staff. Major contractors are able to maintain a country presence (an overhead paid for through existing contracts) and so have much more regular professional and social contact with DFID staff. We heard in evidence that “such contacts are particularly useful to build an understanding of the emphasis required in a particular proposal, which may not be immediately apparent from the published tender documents.”

59. Concerns around the level of competition have also been raised with respect to the number of bids that DFID typically receives per contract. This may partly be related to DFID procurement reforms, with one contractor noting a significant drop in the number of bids since the implementation of the Wealth Creation Framework (WCF) (one of DFID’s key framework agreements). DFID were unable to confirm this as it told us that comprehensive data on the number of bids is only available from 2015–16—however it was able to say that it received an average of 2.5 bids per contract in that year. Figure 4 below shows the distribution of the number of bids per contract for each competitively tendered contract between the start of the 2015/16 financial year and the end of 2016. The most common number of bids was three (37 contracts), with 39% of contracts receiving two bids or less. Nick Ford told us that the 2015–16 average of 2.5 bids was “not sufficient”.

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96 Confidential written evidence (DUC0004) para 12
97 CIPS, Presentation on ‘Collaborative Relationships’ (accessed 14 March 2017)
98 Confidential written evidence (DUC0004) para 13
99 Confidential written evidence (DUC0015) p3
100 Confidential written evidence (DUC0004) para 16
101 DFID (DUC0016) p12
102 Q95
Few bids does not always mean an uncompetitive market. Nick Ford pointed out the intense competition between Boeing and Airbus in the market for aeroplanes. However, as has already been noted in this report (see para 36), the market for development services is of a different nature. Boeing and Airbus have clearly defined deliverables whereas DFID contractors often do not. DFID’s role is not to procure a particular good but to procure poverty reduction, and market structure is important when trying to ascertain whether it is purchasing the most effective way of delivering on non-tangible outcomes such as better governance. In oral evidence DFID stressed its efforts to expand the contractor market through its early market engagement efforts, providing examples of good progress in Pakistan and Mozambique. As DFID recognises, there is still some way to go in this respect.

It should be noted that a perfectly competitive market is a theoretical concept, therefore we are not attributing blame to DFID for failing to create one. However, it is clear that much of the justification underlying DFID’s use of contractors relies on the assumption that the market is competitive. DFID referred to market competition as evidence to allay a number of the Committee’s concerns, including:

- Ensuring value for money,
- Why UK companies are so dominant in the market (winning 85% of centrally issued DFID contracts),

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104 Q66
105 Q63
106 Q65
107 Q94
• How DFID ensures contractor profits are “fair but not excessive”,\textsuperscript{108} and
• Whether DFID is buying services at competitive rates.\textsuperscript{109}

Therefore, given the importance of this assumption, any factors that may undermine market competition are a concern. Guidance from the Office of Fair Trading (OFT) states that “any assessment of the working of competition in a market will begin with an analysis of market structure and the implications of this structure for the conduct of the firms engaged in the market.”\textsuperscript{110} Market features identified by the OFT that may raise concerns in such analysis include concentration (the number and size distribution of firms), barriers to entry and information asymmetries, all of which have been raised in evidence to this inquiry.

62. There is some evidence to indicate that there is healthy competition in DFID’s supplier market relative to other donors. However, there are a number of factors undermining the competitive elements of the market, including unequal access to Department officials, low numbers of bids and a range of other issues including unequal information and some organisations being locked out by framework agreements. Ensuring a competitive contractor market is a central component of DFID’s commercial strategy, and while it has the potential to lower costs and deliver greater value for money, this should be balanced with greater risk management.

63. DFID should conduct market analysis, potentially with assistance from experts at the Competition and Markets Authority (CMA), to determine any issues that may be undermining market competitiveness. It should then take necessary steps to correct for these issues in order to create an increasingly level playing field for all potential bidders.

**Expanding the supplier base**

64. As previously mentioned, a key priority identified in DFID’s Procurement and Commercial Vision is growing the supplier base.\textsuperscript{111} In written evidence, DFID stated:

> “We have taken a number of actions already to increase the number of suppliers bidding and winning DFID contracts (including for SMEs and local suppliers), through: the choice of delivery routes; improved cost transparency; and structuring programme size and design to encourage access by new entrants.”\textsuperscript{112}

While Nick Ford confirmed that there had been improvement in this respect, he added that “it is still nowhere near where I want it to be.”\textsuperscript{113} There are two elements to this: expanding the base among domestic contractors and among those in developing countries.

\textsuperscript{108} Q96
\textsuperscript{109} Q104
\textsuperscript{110} Office of Fair Trading, *Market investigation references: Guidance about the making of references under Part 4 of the Enterprise Act* (March 2006) para 5.1
\textsuperscript{111} DFID, *DFID’s Procurement & Commercial Vision* (April 2016)
\textsuperscript{112} DFID (DUC0016) p6
\textsuperscript{113} Q66
Expanding the developing country supplier base

65. DFID reports that it formally untied its aid in 2002, however it also wrote in written evidence that over 85% of centrally issued DFID contracts are won by British companies which it attributes to their competitiveness. The OECD has pointed out that even among donors who have fully untied aid formally, there is still tying in practice in the sense that procurement processes can favour domestic companies. DFID performs extremely poorly on measures of the share of contracts going to companies based in developing countries—in 2013 less than 2% of the total value of DFID contracts awarded were awarded to organisations in developing countries, compared to an average across other selected DAC members of 54%. In oral evidence, Joy Hutcheon gave an example where an initiative had been undertaken in Nepal to contract through local NGOs, though such efforts appear to be on a relatively small scale.

66. Framework agreements act as a barrier to greater inclusion of overseas contractors. An independent evaluation of DAC members’ policies and practices towards untying stated that:

“Framework contracts can preclude the competition gains from untying to local and regional suppliers. Undoubtedly donors find these contracts convenient in achieving administrative efficiency savings and they may be cost effective from a perspective of managing a multi-country project portfolio. They may also be competitively tendered amongst developed country suppliers. However, at the individual project level and from the recipient perspective they appear to be a form of de facto tying that precludes local sourcing.”

67. In evidence to this inquiry, DFID spoke at length about its use of Early Market Engagement exercises to expand the supplier base, where upcoming procurements are discussed with potential bidders and market input requested. We welcome the fact that these exercises are increasingly conducted in developing countries, with DFID reporting 65 in-country exercises in the last twelve months. However, we also have concerns about the way in which they are conducted and also caution against an over reliance on these as a tool to attract new suppliers. One contractor wrote in evidence:

“Early Market Engagement (EME) meetings, while welcome in principle, can be more confusing than informative. This is because they are often held prematurely—before DFID has a clear view of how it wants to procure or implement a programme. EMEs would be more effective if managed as a genuine consultation with suppliers, encouraging constructive dialogue as a way to test market response and improve design principles—which is not possible with the format currently used by DFID.”

114 DFID defines this as “removing the legal and regulatory barriers to open competition for aid funded procurement – generally increases aid effectiveness by reducing transaction costs and improving the ability of recipient countries to set their own course. It also allows donors to take greater care in aligning their aid programmes with the objectives and financial management systems of recipient countries.”
115 DFID (CON0039) p7
117 Q91
118 OECD, Untying Aid: Is it working? (December 2009) p50
119 DFID (DUC0016) p9
120 Confidential written evidence (DUC0004) para 19
68. In the interests of the untying of aid, the OECD DAC also encourages donors to post notification of tenders on the Untied Aid Public Bulletin Board, which acts as a centralised notice board for private sector actors from anywhere in the world to compete for aid-funded contracts. This acts as a simple and transparent means for donors to advertise opportunities to developing country contractors which is undoubtedly cheaper than other means of engagement such as EMEs. Other major donors—including those with better track records of using developing country contractors—make use of this tool. It appears that the UK did post to the Bulletin Board until 2006 when it stopped doing so. When questioned as to why DFID does not make use of it Nick Ford referred to “system integration capability issues, which stop us from being able to integrate and publish to other sites.”

69. Expanding its supplier base is another key component of DFID’s procurement and commercial strategy. While the Department has taken some steps to reach out to and include developing country contractors, these have had limited effect with only a tiny proportion of contracts still awarded to companies that are based in-country. We note that the UK Government made commitments to untying aid, both formally and in practice, yet some of DFID’s procurement practices (such as the establishment of framework agreements) can work against this commitment.

70. DFID should report on how it plans to increase its efforts, beyond what has already been stated in evidence, towards helping more developing country contractors bid for DFID work. It should ensure that the format of Early Market Engagement (EME) exercises is geared towards greater inclusion, and should report to us on whether greater use of in-country EME’s has increased the number of developing country contractor bids. DFID should also make use of the Untied Aid Public Bulletin Board and, if it continues not to do so, should clearly justify why not and describe an alternative approach to advertising contract opportunities to developing country contractors.

Expanding the domestic contractor base

71. Evidence suggests that there are also barriers to the participation of smaller, UK-based organisations. Some of the challenges for such organisations have already been discussed (such as framework agreements), but more broadly, DFID’s approach to tendering and developing the market has meant that “small and micro consultancies are squeezed to the margins and do not get a fair share of project work, or often even the chance to be full participants in the tendering process.” A number of concerns from the smaller organisation perspective were raised in written evidence by Public Administration International, including:

- They can only participate as sub-contractors who “rarely get a commensurate share of the paid work in implementation.”;
- The decision to bid when tenders are issued through frameworks lies with the lead contractor, and seems to be made “primarily on the basis of the interest and potential involvement of the lead consultancy itself.”;

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121 OECD, Untying aid: Official development assistance contract opportunities (accessed 14 March 2017)
122 Q141
123 Public Administration International (CON0016) para 3.5
• They are in a “Catch 22” situation. They cannot grow and enhance capabilities until they win more work and they cannot win more work until they have stronger track records and cash flows for start-up costs.\textsuperscript{124}

Other concerns about the treatment of small organisations that access DFID work through sub-contracting are addressed in the following section on supply chains.

72. While DFID wrote that it is taking “a number of steps to stimulate and encourage competition across its supplier base”,\textsuperscript{125} including smaller organisations, it is not clear that it has a thorough enough understanding of these challenges. In written evidence, DFID mentions its strong track record of contracting through SMEs:

“The department actively contributes to the central government priority for engaging with SMEs and now has the second highest spend with SMEs across government, representing 32% of contracted spend.”\textsuperscript{126}

While this is welcome, it fails to acknowledge that the definition of SMEs (which is imposed across Government due to European Commission Public Contracts Regulations) may not be appropriate for DFID procurement.\textsuperscript{127} The chart below shows that half of DFID’s top ten contractors between 2010 and 2016—with a combined contract award value of £1.5 billion—are considered SMEs. This demonstrates that the value of contracts awarded to SMEs is heavily weighted to the ‘medium’ end, and suggests that such a focus is unlikely to be inclusive of smaller organisations and expand their opportunities for DFID work.

Figure 5: DFID’s top 10 suppliers, the value of contracts awarded and SME status, 2010–2016 (£ millions)

\begin{table}
\begin{tabular}{|c|c|c|}
\hline
Supplier & SME Status & Value Awarded (£ millions) \\
\hline
ASI & SME & 500 \\
PwC & non-SME & 400 \\
Palladium & SME & 300 \\
Mott MacDonald & non-SME & 200 \\
DAI Europe & non-SME & 150 \\
IMC Worldwide & non-SME & 100 \\
IMA World Health & SME & 50 \\
Oxford Policy Management & SME & 20 \\
Crown Agents & non-SME & 10 \\
Mannion Daniels Limited & SME & 0 \\
\hline
\end{tabular}
\end{table}

Source: DFID Annex D (\textit{DUC0017})\textsuperscript{128}

\textsuperscript{124} Public Administration International (\textit{CON0016}) para 4.3 and 4.5
\textsuperscript{125} DFID (\textit{DUC0016}) p2
\textsuperscript{126} DFID (\textit{CON0039}) p3
\textsuperscript{127} The EU defines SMEs as organisations with annual turnover of less than (or equal to) €50 million. For more information on SME definitions see ‘European Commission: What is an SME?’
\textsuperscript{128} IMA World Health is a non-profit DFID supplier
73. The movement towards Payment by Results (PbR)—a way to deliver services where all or part of the payment depends on the provider achieving specific outcomes—represents another issue for smaller organisations. In a 2015 report, the NAO suggests that Payment by Results schemes by their nature are typically let to larger contractors with the capacity to bear the financial risks and the substantial working capital required to finance large teams and operations until results can be achieved.\textsuperscript{129} DFID’s lack of understanding of the challenges faced by small organisation is demonstrated in its SME Action Plan, which refers to “output based contracts” (the principle of PbR) as “SME friendly processes”.\textsuperscript{130} Further to the findings of the NAO, one contractor wrote that such approaches “favour large and established firms, by creating pressures on cashflow which only they can withstand.”\textsuperscript{131} PbR is thus likely to further concentrate work in the hands of medium-sized contractors at the expense of small and micro enterprises.

74. Despite DFID’s stated aim to expand the supplier base and facilitate access to DFID contracts by smaller organisations, evidence suggests that it does not have sufficient understanding of the challenges faced by small organisations nor how to address these. The broad Cabinet Office definition of SME’s means that DFID’s SME Action Plan is unable to capture the needs of small and micro enterprises. However, we also recognise that the Government is bound by this definition due to European Commission regulations. We also note that the use of Payment by Results (PbR) is likely to work against the aim of DFID procurement being more inclusive.

75. \textit{DFID should be more inclusive of small and micro enterprises by disaggregating its approach to SME’s to target small and micro enterprises. This should include both collecting data on the work contracted to such enterprises and producing a strategy on how opportunities for them to bid for DFID work can be expanded. DFID should also report to the Committee on how it plans to mitigate the impacts of Payment by Results so that it does not preclude smaller organisations from bidding as evidence suggests is currently the case.}

\textbf{The DFID supply chain}

76. DFID’s delivery model means that there are various levels through which funding cascades in order to reach programme beneficiaries. As reflected in figure 6, this is not just true in its use of contractors but also through the other delivery channels. In many cases, this can mean a complex array of suppliers at various levels throughout the supply chain. We heard from DAI Europe that in December 2015 they identified more than 550 sub-contractors or local NGOs working across 27 DFID contracts, at an average of more than 20 sub-contractors used per DFID-funded programme.\textsuperscript{132} A highly simplified model of this supply chain is represented in figure 6, which shows that there are four main groups of actors in programme delivery through contractors—DFID, lead contractors, sub-contractors and beneficiaries.

\begin{itemize}
\item \textsuperscript{129} NAO, \textit{“Outcome-based payment schemes: government’s use of payment by results”} (June 2015)
\item \textsuperscript{130} DFID, \textit{SME Action Plan} (November 2016) p7
\item \textsuperscript{131} Confidential written evidence (DUC0004) para 15
\item \textsuperscript{132} DAI Europe (See Annex 2)
\end{itemize}
Some of the advantages of this contracting model were presented in evidence to this inquiry. Options wrote that, in order for DFID programming to have maximum impact, it is vital that the right kinds of organisation are deployed for the roles for which they are best suited. Mott MacDonald added that “the complexity and size of many DFID programmes requires both large contractors like ours to lead and manage them and small contractors to deliver niche inputs to achieve specific results. It is not a case of either or, but both.” Coffey wrote that lead contractors play an important role in connecting DFID with small, local organisations that have experience and knowledge on the ground. Delivery through lead contractors:

“enables these NGOs to learn about DFID’s priorities without requiring them to invest resources in building that relationship. DFID, in turn, benefits from the managing contractor providing the programmatic oversight that ensures partner NGOs’ activities on a given programme are aligned with the department’s aims.”

While there are certain benefits of the current approach for DFID programme delivery, there are also a number of risks. Saferworld focused on some of these risks in written evidence:

“This model is susceptible to creating distance between the contractor from the actors and realities on the ground. Equally, the further along the chain, the more removed the sub-contractor will be from the overall project budget, aims and structure. The contractors, in some cases, keep the subcontractors in anonymity so they do not know the identity or deliverables of the other subcontracted organisations. This can lead to the duplication of activities...
or subcontractors working in the same location without being able to create synergies to strengthen the coherence of the programme and the potential impact.”

Many of the concerns presented to the Committee focus on two core areas: DFID’s understanding of contractors’ supply chains and how DFID ensures fair treatment of subcontractors.

**DFID’s understanding of contractors’ supply chains**

78. In written evidence, Dr James Morton said “DFID does not, in my view, take sufficient interest in properly understanding this complex network and in ensuring robust financial control at the lower levels.” A recent ICAI report on DFID’s approach to managing fiduciary risk noted that DFID’s approach “[ … ] reduces DFID’s direct interaction with local civil society organisations and businesses and the possibility of increasing the capacity of these organisations to manage risk, it also distances DFID staff from some of the practical risks and challenges that emerge during programme implementation.”

A thorough understanding of supply chains is a key factor with respect to ensuring value for money—if DFID is unable to trace funds down through to beneficiaries, it is unable to say whether it is achieving value for money. When questioned on this, it was not clear whether DFID is able to do this for all its programmes.

79. A lack of understanding of its partnerships was also raised by Contractor A, who referred to a programme that experienced serious performance problems due to a lack of understanding of the intra-firm contracting relationship. While the contract was won by a UK-based firm, the delivery was sub-contracted to its affiliate in another country. There were tensions between the two entities that had a serious impact on programme performance, with the evidence stating that “the main sticking point for the separate companies was not how to deliver a DFID programme effectively, but was obsessed with how they divide up the profit in the contract.”

The fact that these issues were not anticipated in the procurement process demonstrates that DFID had an incomplete understanding of the delivery chain with implications for programme delivery.

80. However, in her December 2016 letter to suppliers, the Secretary of State made it clear that supply chain mapping will be a key focus of DFID’s future work with contractors. There will be an increased focus on due diligence throughout the supply chain and mandatory provision of a full supply chain map at the bidding stage. DFID announced a number of other welcome measures in written evidence, including the introduction of a new online tool so that supply chains can be mapped in a consistent format to facilitate aggregation and analysis of the information and a greater focus on delivery chain mapping in key training courses.

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136 Saferworld (CON0033) para 11
137 Dr James Morton (DUC0003) p2
138 ICAI, “DFID’s approach to managing fiduciary risk in conflict-affected environments” (August 2016) p iii
139 Q120-122
140 Confidential written evidence (CON0007) para 20
141 DFID, Secretary of State letter to DFID suppliers (December 2016)
142 DFID Annex D (DUC0017)
Treatment of sub-contractors

81. DFID’s lack of oversight of both the supply chain and delivery has also reduced its ability to ensure that sub-contractors are being treated fairly. Seriously concerning reports have emerged to suggest that sub-contractors are occasionally mistreated, which Bond attributes to “[ … ] a lack of contractual disincentives for such behaviours in DFID’s engagement of contractors.”\(^\text{143}\) We stress that these behaviours are by no means representative of all contractors, and that this issue is related to the conduct of a select few (which will be further addressed in chapter 5). Though we also note that, by DFID’s own admission, it has relied on “self-declaration” of adherence to its expectations and principles.\(^\text{144}\)

82. Bond described one way in which sub-contractors are mistreated in written evidence:

“There are repeatedly documented accounts of NGOs being included at the bid/design stage only for them to be dropped or disengaged when the prime bidder has won the contract. This practice (which has led to the emergence of the term ‘bid candy’) means that DFID does not get what it paid for.”\(^\text{145}\)

Contractor A reported that the choice of sub-contractor can be a key factor in helping the lead contractor win the contract (due to their expertise), but after it is won there is little incentive to keep them on and a great deal of incentive to drop them to increase profit margins.\(^\text{146}\) DFID stressed in written evidence that “no changes or substitutions of key supplier personnel as identified in the contract can be made without DFID’s prior written consent.”\(^\text{147}\) While DFID provided an example in Sierra Leone of where the lead supplier had lost the contract as results of this,\(^\text{148}\) the dropping of sub-contractors still appears to be a feature of lead contractors’ behaviour under DFID contracting.

83. Other concerns relate to whether sub-contractors get a fair deal even when they are kept on throughout implementation. Public Administration International wrote “while the names and capabilities of consortium members are included in tender documents as sub-contractors, sub-contractors find that they rarely get a commensurate share of the paid work in implementation. This is largely completed by staff of the lead consultancy in the bid.”\(^\text{149}\) Contractor B reported two instances where lead contractors reneged on their pre-bid agreements and unilaterally cut the sub-contractor’s share of the payment in the bid. We were told:

“In one case, there was a rate cut of 25% imposed about four days before the bid submission, on the inputs by the subcontractor. In the other case, the bid was submitted and [ … ] despite there being a pre bid agreement on consultation, saying, “We did not have time to review with you. We submitted the bid. We cut your inputs by 25%. Take it or leave it.””\(^\text{150}\)

\(^{143}\) Bond (CON0040) para 25
\(^{144}\) Q84
\(^{145}\) Bond (CON0040) para 16
\(^{146}\) Confidential written evidence (CON0007) para 20
\(^{147}\) DFID (DUC0016) p8
\(^{148}\) Q87
\(^{149}\) Public Administration International (CON0016) para 4.3
\(^{150}\) Q22 (See Annex 1)
A thorough understanding of DFID supply chains is essential to ensuring value for money and development impact in DFID programming. While we welcome DFID’s increased effort to map and better understand these supply chains, we are concerned that this is a feature of the delivery model that has been overlooked up to this point. While we recognise that DFID is not responsible for cases of mistreatment of sub-contractors, we stress that it is responsible for enforcing certain standards of conduct, and that a lack of enforcement and an over reliance on self-declaration of adherence to these standards has contributed to these behaviours.

In order to facilitate better engagement between DFID and the sub-contractors that deliver its programmes, DFID should establish a dedicated ‘sub-contractors unit’ within its Procurement and Commercial Department. Much like the Key Suppliers Management (KSM) system for larger contractors, this would act as the main access point for sub-contractors and offer them a more consistent pipeline of information on future opportunities, provide a channel for raising grievances and allow DFID to better understand the challenges they face and how it can help overcome them.
5 Conduct and performance of contractors

Compliance with priorities and expectations

86. Much of the focus of media attention on contractors has centred on examples of conduct not in keeping with DFID's objective of poverty reduction. A number of contractors referred in written evidence to the intensity of competition at the tendering stage, and it can be assumed that for-profit companies with shareholders to answer to are likely to make use of any competitive advantage they can gain. Contractor B confirmed that “contractors will play every card they have and some they should not have to win the contract.”

87. In December 2016, the Mail on Sunday published an article that used leaked emails to highlight serious concerns about ASI staff obtaining and intending to make use of internal DFID documents. The article stated that “a former government official now working for Adam Smith International obtained secret files revealing aid policies and spending plans for the next four years—then boasted this would help the firm when bidding for contracts.” DFID has been very guarded about the Business Plans in question (to the extent that they have not shared them with this Committee) as they contain substantial detail on DFID’s country-specific strategies in its bilateral programmes. The competitive advantage afforded to any contractor in possession of these documents is therefore significant, and had the Mail on Sunday not obtained the leaked emails, DFID’s procurement processes would have been severely compromised. Allegations of improper behaviour by ASI relating to submissions to our inquiry were addressed in our recent special report ‘Conduct of Adam Smith International’.

88. In response to this, DFID has launched its own forensic investigation into the allegations, and in a letter to the Committee the Secretary of State said that she is determined to “eliminate rogue practices by a few”. ASI also announced “major reforms”, including the standing down of a number of executives and the restructuring of the organisation “as an enterprise with primary focus on a social mission”. However, when asked whether such practices were a one-off case or whether there is a cultural problem among certain contractors, Contractor B told us “[…] it is absolutely embedded in the culture—absolutely.” It is also not clear in evidence from certain contractors that they have understood or internalised these concerns about the organisational culture. Written evidence from the Centre for Development Results, a group formed of contractors including ASI, makes a number of references to the media coverage of contractors being “overly negative” and “deliberately misleading”. It makes no reference to the poor conduct of some of its members. While we agree with this in some respects and call for a more

151 Q3 (See Annex 1)
152 Mail on Sunday, “Exposed, the foreign aid giant which conned MPs with fake glowing testimonials about overseas work to snaffle £329million of taxpayers’ cash” (3 December 2016)
153 International Development Committee, Seventh Special Report of Session 2016–17, Conduct of Adam Smith International, HC 939
154 International Development Committee, Letter from Rt Hon Priti Patel MP, Secretary of State for International Development, concerning DFID’s relationship with its suppliers (9 January 2017)
156 Q39 (See Annex 1)
evidence-based debate on DFID’s use of contractors in the media, it is not clear whether certain contractors genuinely see their practices as an internal problem or a media/public relations problem.

89. Recent reporting on the conduct of certain contractors shows that some have behaved in a way that is completely unacceptable, is not in line with the principles of the Department and is harmful to the public’s view of DFID’s work. While we firmly believe that this is not representative of all of DFID’s suppliers, we affirm that there is a serious problem in the practices of certain organisations and that this is unacceptable. It is not clear whether the gravity of this is appreciated by certain contractors and we are yet to be convinced that they share our view that the sector needs a genuine rethink in terms of its approach. The allegations made of ASI should not be approached as an isolated incident by DFID, but as evidence that there is something inherently wrong with the culture in certain organisations. DFID needs to take a more robust approach in creating regulations and incentives that shape the sector so that it operates to the highest ethical standards. It is clear that DFID cannot rely on its approach of self-regulation. While it is up to contractors to adjust their practices, it is the Department’s responsibility to establish a set of rules and parameters and, critically, to enforce them.

90. In her letter to DFID suppliers, the Secretary of State recognised that having contractors sign up to a set of principles is not enough. As she wrote:

“As a DFID supplier you have committed to our Statement of Priorities and Expectations for Supplier and Partner relationships. However, it’s become increasingly clear, far more needs to be done.”

While it is clear that DFID has taken action on setting the rules through its Statement of Priorities and Expectations (SoPE), it is not so clear that they are being actively enforced.

91. In order for DFID to ensure that contractors are following the rules, it needs to be in a strong position to raise concerns and investigate cases when it believes they are not. However, one of the criticisms that applies across all DFID’s channels of delivery, not just contractors, is that it lacks the ability to challenge suppliers where necessary. Dr James Morton wrote that:

“One of the Department’s biggest weaknesses is its inability to challenge suppliers effectively and robustly. Large consulting firms, international NGOs and multilateral organisations, most especially the World Bank, all have stronger institutional memories and research capabilities and it is very difficult for DFID staff, often relatively junior and limited for time, to outface them.”

With specific regard to contractors, Contractor B highlighted that this is partly a staffing issue. The two year placements that DFID staff typically rotate on do not allow them to “drill down into what is going on in its projects” in a given country. As a result, contractors get complacent and as and when they are challenged by a project officer, they can “outlast any two year posting” if necessary. This weakens the position of the Department in holding contractors to account.

157 DFID, Secretary of State letter to DFID suppliers (December 2016)
158 See Appendix
159 Dr James Morton (DUC0003) p1
160 Q28 (See Annex 1)
92. Recently the SoPE has been made increasingly stringent and, based on the Secretary of State’s letter to suppliers, indications are that it may be made more so in the future. While there is a necessary burden associated with complying with regulations, there are concerns about the impact this will have on smaller organisations. As DAI Europe wrote:

“DAI fully supports all of the principles embodied in the new requirements, but we note that the cost and complexity of compliance is growing, and in a way that will particularly disadvantage smaller suppliers for whom the fixed cost of compliance cannot be leveraged across a large volume of work.”

Another contractor expanded on this by writing that “whilst all of this might be perfectly reasonable, it does raise the bar well above smaller firms, and firms in recipient countries to ever contract directly with DFID again.”

93. Many of the key areas of concern with respect to DFID’s use of contractors, such as profits, treatment of sub-contractors, commitment to ethical codes of conduct and honesty about capacity and capability in bids, are all addressed in DFID’s Statement of Priorities and Expectations (SoPE) for Suppliers. The fact that certain contractors breach the conditions of the SoPE suggest that not enough is being done to enforce it. While the prospect of adding to the SoPE might be well-intentioned, it is also likely to have the effect of overburdening smaller organisations to the point where they can no longer bid for DFID contracts. This will work against DFID’s objective of expanding the supplier base. We also note that in particularly complex environments, staff rotations may be too short for them adequately to get to grips with the development context, and this may put them on the back foot in managing experienced contractors.

94. Rather than expand compliance regulations, DFID should do more to ensure that the regulations set out in the current SoPE are effectively enforced. In its Supplier Review, DFID should explore ways that it can track compliance, with a particular focus on the issues raised in this report. DFID should also set out a clear set of consequences for contractors if they fail to comply with the SoPE. While such consequences should be proportionate, they should also be sufficiently firm to act as an effective deterrent against poor conduct. It should also consider extended postings in challenging environments, particularly where contractors are the dominant channel for delivery. This will help ensure that DFID staff have the requisite in-country experience to effectively manage complex programmes and ensure optimal delivery.

**Ensuring high-level performance of contractors**

95. Another concern relates to whether contractors actually deliver at implementation stage what they have set out in the bid. This report has already discussed how the choice of partners may help a lead contractor win a bid, following which there are cases where that sub-contractor has subsequently been dropped (see para 82). DFID confirmed in written evidence that it does not audit firms to assess their claimed capacity. Due diligence assessments focus on the evaluation of bids stage, and are designed “to obtain a level

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161 DAI Europe (DUC0002) para 4
162 Confidential written evidence (DUC0015) p3
of assurance of a potential delivery partner’s capacity, capability, systems, policies and processes to deliver DFID programmes prior to entering into a formal agreement.”

Nick Ford told us that “Through the life of the programme is where I am a bit more concerned.”

96. DFID’s Internal Audit Department (IAD) assesses implementation of a cross-section of programmes. However, with 32 Full Time Equivalent staff who are required to cover assurance and counter fraud functions across DFID’s entire portfolio, it is undoubtedly stretched in its ability to perform in-depth follow up on all contractor-delivered programming. Contractor B noted that:

“[ … ] the point at which a procurement is finalised is an important pinch point in the market, because there is every incentive to win that contract and there is very little punishment for not delivering on the contract. You will say everything you possibly can to win that contract.”

97. In written evidence, DFID stated that it uses payment by results contracts “to ensure payment is linked explicitly to delivery.” However, in its Payment by Results (PbR) Smart Guide it also acknowledges that there are risks associated with this. If poorly designed, procured, or delivered, the impacts of PbR can include:

- perverse incentives, where the payment scheme encourages damaging behaviour by suppliers or partners;
- cherry-picking or corner cutting, where suppliers choose the easiest interventions, avoiding harder-to-reach groups or individuals (see paras 118-122);
- distorting effort away from what’s important and towards what can be measured.

Concerns about these issues were echoed in evidence to this inquiry. One contractor wrote that:

“DFID has tried to sharpen performance through introduction of modalities such as output-based-payments. In my experience, this skews incentives [ … ] and further reduces the returns for smaller and more local businesses. Incentives are all driven by ticking boxes and hitting indicators and targets. Not bad per se. But it assumes that what’s in those boxes matter for good development outcomes. Too often they simply don’t.”

98. Linking payments to delivery on certain milestones is effective in theory, though in practice there are issues. Contractor A told us that “in most development programmes it will be very hard to identify concrete milestones that DFID can reasonably expect a contractor to deliver.” This is supported by findings from ICAI that “in Pakistan, DFID staff informed us that they lacked the information and the commercial expertise to select reasonable targets for supplier performance.”

Contractor A raised an example where poorly designed milestones had a significant negative impact on the delivery of the
programme. The lead contractor agreed milestones “without checking their feasibility with the technical team, and thus committed to some milestones that were either meaningless or impossible to achieve.” When these milestones were missed and funds withheld, project beneficiaries suffered as the costs were not absorbed by the lead contractors management fees but by the share of funding spent on field activities. The result in this case was that “[…] the milestone system badly misaligned incentives, failed to induce good performance, and denied the programme resources to fulfil its objectives.” 171 Given recent concerns about the conduct of contractors, it is also concerning that they can actually use the weaknesses inherent in the design of milestones to conceal poor performance. One study of incentives for contractors used by the Swedish International Development Cooperation Agency (SIDA), concluded that:

“If the project outcomes are not easy to measure and evaluate, it is easier for the consultant to hide project misperformance or failure. This condition suggests that consultants have weaker incentives to perform at a high level when project outcomes are difficult to appraise. Moreover, cunning consultants who expect to perform at a low level of competence have an incentive to prescribe difficult-to-measure project outcomes.” 172

99. DFID’s due diligence of contractors appears to focus excessively on the bidding stage and not enough on the implementation stage. There are examples to suggest this may have skewed the incentives of contractors to focus on winning contracts, not delivering them. While we recognise the logic in using Payment by Results (PbR) to incentivise effective delivery, we are concerned that DFID is not doing enough to mitigate the risks involved and this is to the detriment of quality programming and impact.

100. DFID should rebalance its due diligence efforts to focus increasingly on contract delivery. It should also increase the resources of the Internal Audit Department (IAD) if necessary. Where PbR is used, DFID should use the research it has commissioned—as well as the forthcoming work from ICAI—to create more robust guidance and training resources for staff on how to design effective programming milestones.

Performance incentives for contractors

101. One of the advantages of contracting stated in written evidence is that “when a contract is underperforming, or its activities no longer contribute to a DFID goal, DFID is at liberty to cancel that contract for convenience at any time.” 173 In evidence from DFID, we were informed that “in the last year, 9 contracts above the OJEU threshold174 have been terminated for reasons including the programme’s underperformance, poor value for money, concerns regarding supplier capability, and changes in the delivery context.”175 Evidence suggests that there may be other cases of underperformance where the contract should have been cancelled but was not. Contractor A told us of an instance where the

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171 Confidential written evidence (CON0007) para 21
173 DAI Europe (DUC0002) para 17
174 The Official Journal of the European Union (OJEU) threshold is the mandatory value (£135,000 or £106,047) above which Public Contracts Regulations apply
175 DFID (DUC0016) p8
lead contractor received less than 50% on its Key Supplier Management (KSM) review due to "serious shortcomings in the management team", but the contract was not cancelled. According to DFID’s scoring system, such a rating demonstrates "serious delivery failure and under performance. Immediate and major changes needed." However, DFID failed to follow up on this and the project actually received an extension despite the protests (and withdrawal) of the sub-contractors who were unhappy with the way the programme was being managed.176

102. DFID contractual terms and conditions include provisions for the suspension or termination of the contract with or without default of the supplier. Despite the fact that programmes have been cancelled due to ‘underperformance’ and ‘concerns regarding supplier capability’, we were informed that none of the nine contracts in the last year were cancelled for ‘default of the supplier’. All were cancelled ‘for convenience’.177 Nick Ford told us that “even if you are terminating for underperformance, you may end up not going down the fault route, because it would be quicker, easier and less costly to the taxpayer to go down a convenience route”.178 While we recognise that this may be an easier and cheaper approach to contract cancellation, we have concerns about the implications for accountability. Failure to recognise formally and record the fault of the supplier may limit opportunities to investigate and learn from underperformance for future programming.

103. There is another concern about DFID’s ability to use the past performance of contractors to inform subsequent programming decisions. Contractor B described one of the problems DFID faces as “asymmetry of information” (i.e. contractors know how good they are at delivering while this is challenging for DFID to ascertain). It seems sensible that DFID would draw lessons from where contractors have performed poorly in the past and to use this to assess their suitability at the bidding stage. Other donors appear to do this, as Crown Agents wrote “it is notable that other donors (such as USAID) take into account scores from annual reviews and project completion reports as part of their selection process.”179

104. When initially questioned on whether DFID takes account of prior performance in assessing bids, Nick Ford told us that public procurement regulations “do not allow for past performance to be brought into account in the bidding phase.”180 However, Crown Commercial Service guidance on the 2014 EU Public Procurement Directives state that “poor performance under previous contracts is explicitly permitted as grounds for exclusion.”181 When this was raised with the DFID officials, Nick Ford told us that “you need very robust systems to be able to take into account any past performance obligations, to ensure that you are assessing the tenders on a like-for-like basis.” Joy Hutcheon added that “the remedies available to suppliers under EU directives are extremely robust and we would run a risk of ending up in court very quickly.”182 We were also told that one of the goals of the supplier review is “ensuring that all our suppliers are incentivised to meet our statement of priorities and expectations.”183

176 Confidential written evidence (CON0007) para 25
177 DFID (DUC0016) p5
178 Q112
179 Crown Agents (DUC0013) para 6.3
180 Q115
181 Crown Commercial Service, A Brief Guide to the 2014 EU Public Procurement Directives (October 2016) para 5.9
182 Q116
183 Q53
105. Evidence suggests that continued poor programme delivery by contractors does not necessarily lead to the cancellation of contracts. Even in instances where it is recognised that DFID contracts are underperforming, they are cancelled ‘for convenience’ as this is an easier and cheaper route. While this may save money for the taxpayer in the short run, we are concerned about the long run value for money. Failing to recognise and record any fault of the contractor demonstrates a weakness in accountability and may result in missed opportunities for learning and strengthening for future programmes. Given the inherent difficulties faced by DFID in choosing the best organisation for the job, we are concerned by the fact that DFID, unlike other donors, appears to be unable to use past performance in assessing bids. It is unclear as to why this is the case given that the Crown Commercial Service states that this is explicitly permitted under the EU Public Procurement Directives. We are concerned about the potential effect this may have on contractors’ incentives.

106. DFID should take a more robust approach to creating performance incentives and demonstrate practical ways it is going to do this in its Supplier Review. This should include setting out clear parameters on the grounds on which a contract might be cancelled, and ensuring that there is a credible risk of cancellation by adhering to these. DFID should also ensure that where a contractor is seriously underperforming, the contract should be cancelled on the basis of default so that the failure of the contractor is recorded and that lessons can be learned. In light of the UK’s decision to leave the European Union, DFID should ensure that it has substantial input into any discussions of Government-wide public procurement regulations to be implemented after withdrawal. Such regulations should give DFID greater freedom to take into account contractors’ past performance in evaluating bids. Other donors, such as USAID, have this power and use it.
6 Value for money

Profits and fees

107. A further focus of media scrutiny on DFID in recent months has been on profits made by contractors, the fees they charge and the value for money they offer for the taxpayer. It is clear that DFID holds value for money as the prime objective in its strategic use of contractors, as it said in written evidence “the preferred delivery route is fundamentally determined by value for money considerations, for example which model delivers the maximum impact and outcome for DFID money.”

The increasing use of contractors suggests that, in DFID’s view, they offer better value for money in many cases. Mott MacDonald argued that it is the competition in the contractor market that drives this. It wrote:

“The very nature of competitive tendering requires contractors to deliver the very best value for money. If contractors cannot demonstrate in their bids that they can deliver the best results for the most competitively advantageous price then they will not win the contract.”

108. DFID’s Statement of Priorities and Expectations (SoPE) for suppliers states that contractors may incorporate “fair but not excessive” profits into their costing. In practice, fair but not excessive appears to mean different things to different contractors, as demonstrated in the different rates of net profit reported to this inquiry.

In its written evidence, Palladium summarised typical profit rates:

“Companies House data reveals that most DFID suppliers are earning an average net profit of 5.5%. Levels of net profit in the sector are typically between 3 and 7%. Comparing other industries, profit levels are 50% lower in development than in UK government consulting.”

109. When questioned about what the Department deems “fair but not excessive”, Nick Ford did not provide a definition as such, but told us that DFID uses competition and cost transparency to drive this. However, as this report has already noted in other chapters, there is a danger inherent in assuming that market forces are working sufficiently well to drive down profits to a level that is “fair but not excessive” in the views of the taxpayers footing the bill. The Centre for Development Results, a group formed of contractors, stated in written evidence that contractors “would welcome a conversation with DFID about setting industry standards on issues such as what constitutes a fair and reasonable profit.”

110. DFID also states that it uses benchmarking “across Government, across our programmes and across the international development system” as evidence that it is achieving value for money. Since 2016 it has used a fee benchmarking database to do this. The Independent Commission for Aid Impact (ICAI) has also supported this with

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184 DFID (CON0039) p5
185 Mott MacDonald (DUC0010) para 3
186 See Appendix
187 Confidential written evidence from contractors
188 Palladium (DUC0008) p3
189 Centre for Development Results (DUC0007) para 5.6
190 Q96
191 DFID (DUC0016) p9
a benchmarking exercise in 2013 which concluded that “DFID obtains highly competitive prices from its contractors.”\textsuperscript{192} However, Dr James Morton stated in written evidence that “DFID rates are now ahead of those paid by other donors.”\textsuperscript{193} It is difficult to establish the details of these rate comparisons (or indeed, if they are a valid comparison of like for like) as they are internal.

111. We agree with DFID’s position that, where contractors offer the best value for money, programmes should be tendered rather than delivered through multilaterals or civil society organisations. However, we stress that there is a critical difference between profiting and profiteering. The vague definition of “fair but not excessive” profits provides little reassurance to the public that contractors are not getting rich from UK Aid. While we recognise that being too prescriptive on what is “fair but not excessive” may distort the market, there is room for discussion on what this constitutes. Benchmarking against the rates paid by other donor agencies to contractors is key to ensuring that DFID is getting value for money. The fact that this is done internally with no reporting or details of methodology points towards a lack of transparency.

112. DFID should determine some clear parameters on what constitutes fair but not excessive profits. It should also commission an independent review which benchmarks contractor fees across DFID programmes (including in different locations and comparing fragile and non-fragile states) as well as against other donors. It should also consider whether other donors are achieving better value for money through their differing procurement processes.

113. Media reports have also focused on the daily fee rates paid to contractors—something which our predecessor Committee raised concerns over in a 2011 report.\textsuperscript{194} While we stress the importance of continuous scrutiny by DFID of the value for money in the fees it pays, we note that delivering development impact requires highly qualified staff with the specialist skills required to solve some of the world’s toughest challenges. We also recognise that comparing daily fee rates with an annual salary can be highly misleading. One consultant pointed out in written evidence that he is only paid for the days that he works (which can result in long, unpaid stretches due to procurement delays or illness), he is responsible for his own social security and pension costs and is often liable for local income tax.\textsuperscript{195} Comparative analysis suggests that, comparing on a like for like basis, DFID frontline staff cost 50% more and multilateral staff three times more.\textsuperscript{196} It should be noted that this analysis was conducted by a contractor and has not been verified by DFID.

114. However, concerns were raised to this inquiry that in past DFID programmes, the management mark-up fees were high. Staff costing breakdowns provided to us in confidence suggest that, for one project, the contractor had a margin of 141% between what staffing costs were charged to DFID and the cost at market rates.\textsuperscript{197} DFID has taken crucial steps towards eliminating this practice. It implemented open book accounting last year, so that it can see “all the way through from net costs, including all overheads and

\begin{itemize}
  \item \textsuperscript{192} ICAI, \textit{DFID’s Use of Contractors to Deliver Aid Programmes} (May 2013) para 2.71
  \item \textsuperscript{193} Dr James Morton (DUC0003) p2
  \item \textsuperscript{194} International Development Committee, Third Report of Session 2010–11, Department for International Development Annual Report & Resource Accounts 2009–10 (February 2011) para 79
  \item \textsuperscript{195} Confidential written evidence (DUC0004) p3
  \item \textsuperscript{196} ASI, \textit{Comparative Analysis: DFID Contractor Costs} (2016) p3
  \item \textsuperscript{197} Confidential written evidence (CON0007) Table 1
\end{itemize}
When contractors submit a bid, DFID can use the costing template to separate out and compare profits, overheads and pay rates at the bidding stage. This is a significant improvement on previous practice, though it is unclear why it was not adopted earlier to stamp out profiteering.

115. While open book accounting affords greater transparency and thus enhanced scrutiny of value for money, it does not control fee rates in itself. Australia’s Department for Foreign Affairs and Trade (DFAT) employs a different method in the form of its Aid Adviser Remuneration Framework (ARF) (see Box 4). We recognise that there are certain risks associated with having a prescriptive remuneration framework for consultants. Nick Ford highlighted one in oral evidence:

“If you set a rate and say you will not pay more than £1,000 a day, then over time you will see contractors typically putting people forward who may historically have only been on £800 and are moving up to the top of the different rate bands, depending on what you have for the professional roles that you are recruiting. You will find that you always pay at the top of that band.”

Contractor B highlighted risks that DFID may struggle to attract the top development consultants if it operated such a rigid pay structure, though also noted that this could be overcome with the right amount of flexibility.
Box 4: Australia’s Aid Adviser Remuneration Framework (ARF)

The ARF prescribes a set of rates, allowances and support costs which all consultants (advisers) engaged directly or indirectly under Australian Government contracts must be paid in accordance with. The Terms of Reference (TOR) for an adviser position must be classified according to a set of professional discipline categories and job levels, must be paid as per classification of their role, not according to an individual’s skills and experience. In exceptional cases higher rates may be awarded by senior DFAT officials, though this is subject to a business case. Justification should demonstrate:

- scarce skills and/or outstanding past performance;
- negotiation process undertaken; and
- how the proposed engagement represents value for money.

An example of the pay scale for Discipline Group Category C (which might include an expert in energy, urban development, mining, etc.) is shown below. All figures are in Australian Dollars.

<table>
<thead>
<tr>
<th>Discipline Group C</th>
<th>AUD - daily remuneration rates</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Entry rate</td>
</tr>
<tr>
<td>Entry (Level 1)</td>
<td>318</td>
</tr>
<tr>
<td>Middle (Level 2)</td>
<td>433</td>
</tr>
<tr>
<td>Senior (Level 3)</td>
<td>594</td>
</tr>
<tr>
<td>Senior Executive (Level 4)</td>
<td>682</td>
</tr>
</tbody>
</table>

Source: Australian Government, *Aid Adviser Remuneration Framework (ARF)* (October 2016)

116. We recognise that much of the media focus on the fees paid to consultants has been misleading, and that comparing these daily rates to the annual salaries of employees (and their benefits) is not comparing like for like. We welcome DFID’s move towards more transparent, open book contracting. However we also note concerns that this only happened last year and that, in the past, contractors may have exploited DFID’s inability to see costing breakdowns at the expense of value for money. We also note the approach of other donors towards fees, particularly Australia and its Aid Adviser Remuneration Framework (ARF). While we recognise concerns that such a prescriptive framework could distort the market, we believe that, if designed carefully, it can enhance transparency and deliver better value for money.

117. We recommend that DFID consider an Australian-style consultant remuneration framework as an output of its Supplier Review. This framework should be prepared in collaboration with contractors to take into account their views, and should be designed carefully—building in an appropriate level of flexibility—to avoid any market distortions that may emerge.
Value for money and inclusion

118. Disability inclusion is a high priority for DFID. In a recent speech, the Secretary of State said that “disability is shamefully the most under-prioritised, under-resourced area in development.”\footnote{DFID, Secretary of State speech - Bond Annual Conference 2017 (20 March 2017)} In 2014, DFID launched its Disability Framework to set out the Department’s approach on how to increase disability inclusion in programming and strengthen departmental capability on disability. Disability inclusion is a critical component of the ‘leave no one behind’ agenda of the Sustainable Development Goals, which DFID is a key supporter of.\footnote{DFID, Leaving no one behind: Our promise (January 2017)} However, in written evidence the Bond Disability and Development Group (DDG) stated that “historically, we have seen less evidence on the extent to which people with disabilities, and other marginalised groups, are included in programmes delivered by the private sector.”\footnote{Bond Disability and Development Group (CON0026) para 4.1}

119. In written evidence, DFID stated that “our Standard Contractual Terms and Conditions mandate a requirement of non-discrimination and inclusion, with specific reference to disability.”\footnote{DFID (DUC0016) p5} However, a non-discrimination clause is not the same as disability inclusion. The latest version of the disability framework states that “civil society and private sector partners should outline their approach to disability inclusion as standard in all proposals and if they need extra support, we should be asking that they engage Disabled Peoples Organisations or disability-specific NGOs.”\footnote{DFID, Disability Framework - One Year On (December 2015) p8} Herein there appears to be a mismatch between the commitments DFID made in the framework and the level of disability inclusion required in programmes delivered through contractors.

120. A narrow definition of value for money can create worrying incentives for contractors. The Disability Framework acknowledges that “unless we continually publically demonstrate that ‘VfM [value for money] doesn’t mean we only do the cheapest things, but instead is about the impact we have, we may be inadvertently incentivising partners to focus on easier to reach groups rather than on programmes that are attempting to leave no one behind.”\footnote{DFID, Disability Framework - One Year On (December 2015) p8} Given competition in the market, contractors are under high pressure to cut costs. This may result in disability inclusion being overlooked because disability inclusive programming often costs more per head.

121. Disability inclusion is a key part of DFID’s strategy, as outlined in its Disability Framework. However, there is evidence to suggest that this issue is not being addressed in programmes delivered through contractors. A narrow definition of value for money may encourage contractors to focus on the easiest and cheapest to reach. The competitive nature of the contractor market and DFID’s strong focus on value for money may therefore be creating worrying incentives for them to overlook disability inclusion.

122. DFID should ensure that the principles outlined in its Disability Framework are enforced in programming delivered through contractors and it should require that disability inclusion be written into contracts.

\footnotesize{\begin{itemize}
  \item \footnote{DFID, Secretary of State speech - Bond Annual Conference 2017 (20 March 2017)}
  \item \footnote{DFID, Leaving no one behind: Our promise (January 2017)}
  \item \footnote{Bond Disability and Development Group (CON0026) para 4.1}
  \item \footnote{DFID (DUC0016) p5}
  \item \footnote{DFID, Disability Framework - One Year On (December 2015) p8}
  \item \footnote{DFID, Disability Framework - One Year On (December 2015) p8}
\end{itemize}}
Conclusions and recommendations

DFID’s strategy

1. We recognise that in DFID’s role as a commissioning organisation, there are numerous advantages associated with contracting outside expertise. However, despite the value that contractors can bring, there are certain functions that in-house staff must serve and which cannot be outsourced. With both the size and number of contracts growing, there are increasing pressures on staff who, even with the assistance of commercial advisers, may not be equipped with the necessary skills and expertise to manage the technical, operational and commercial aspects of such large and complex programmes. Replacing development expertise with commercial expertise or overburdening staff is likely to have implications for the effectiveness and impact of programming. Evidence suggests that the decision-making process at the core of programme design—which channel to use—needs to be strengthened. (Paragraph 17)

2. We urge the Department to ensure that the choice of implementing a given programme through contractors is always driven by the strategic value of that delivery channel. DFID Smart Rules should include more detailed guidance on the appraisal portion of the business case, and business cases should clearly justify why the particular channel was chosen, with reference to the relative benefits over other types of delivery. DFID should ensure that the emphasis on commercial expertise associated with the increasing use of contractors does not make generalists of DFID staff at the expense of technical knowledge and depth. (Paragraph 18)

3. Evidence to this inquiry and past IDC inquiries has suggested that an arms-length body to assume some project management responsibilities could be beneficial in both strengthening the expert oversight in DFID projects and deepening competition in the market. It is our view that such a body could contribute towards a suitable balance between in-house and outsourced expertise. It would also afford DFID greater direct scrutiny of contract-based delivery, a notable advantage given recent questions surrounding contractor conduct. We repeat earlier calls for DFID to investigate the idea of an arms-length body to assume programme management responsibilities. This should be done as part of its Supplier Review and the outcome reported to us. If DFID disagrees with this or believes it is not feasible, it should set out why in its response to this Report. (Paragraph 20)

4. In its 2015 Aid Strategy, the Government committed to allocating 50% of all DFID’s spending to fragile states and regions, up from a previous target of 30%. While DFID decides on the delivery channel for its programmes on a case by case basis, any perceived comparative advantage held by contractors is likely to result in their increased use. We share the Stabilisation Unit’s concerns about possible tensions between profit motives and programme objectives in fragile states. We also question whether the shifting of risk to contractors through Payment by Results (PbR) is likely to lead to substantially higher risk premiums which are then reflected in the cost of contracts. We note that with fewer contractors operating in such difficult environments this may have implications for market competition and value for money. (Paragraph 25)
5. DFID should ensure the use of contractors in fragile states is carefully managed and that output targets are designed to align profit incentives and development objectives whilst still taking account of drivers of conflict. DFID should be particularly cautious about shifting risks onto contractors in fragile states through PbR. It should also ensure that all overheads and profits are benchmarked against other donors and recipient countries to ascertain whether DFID is achieving value for money. (Paragraph 26)

6. DFID has taken some key steps towards improving the way it learns through contractors, though concerns remain about whether this knowledge is effectively extracted and internalised. The assumption that contractors are keen to share learning for the greater good overlooks the fact that, as for-profit companies, there is a strong commercial incentive to withhold information from DFID and potential competitors. We stress the importance of independent evaluations, and note that there appears to be little clear strategy to determine the degree of independence in evaluations across various programmes. A number of other donors use very different contracting models which are likely to have their own advantages and disadvantages. (Paragraph 33)

7. As part of DFID’s Key Supplier Management (KSM) system, it should apply a metric on the contractor’s contribution to DFID learning, including how cooperative they are with other contractors. Other innovative approaches should also be explored in the Supplier Review. DFID should use guidelines on best practice to set out clear regulations in its updated Smart Rules on when programme evaluations should be done completely independently of both DFID and contractor staff. It should also foster closer relationships with the procurement departments of other donors as well as multilateral agencies to try to learn about what works in different procurement models. (Paragraph 34)

**Procurement processes**

8. We commend the ability of DFID’s procurement processes to source development interventions quickly when needed, particularly in the case of the Ebola crisis. While DFID should be recognised for using effective procurement to drive down the costs of goods such as bed nets and vaccines, we believe that the majority of DFID programming—such as improving governance—involves a very different approach than that of commercial procurement of goods. We are concerned about instances where procurement-sensitive information has been available to some bidders and not others, and also about the limitations on excluding bidders (imposed by procurement regulations) who have had a role in the programme formulation. Delays and cancellations are also a concern, and high (and rising) bidding costs are likely to work against DFID’s stated desire of expanding the supplier base. (Paragraph 42)

9. DFID must make every effort to level the playing field in terms of information available. While we recognise that mistakes can be made in the way procurement-sensitive information is handled by staff, this can be overcome through greater transparency from the outset—publishing all information so that no single or group of bidders is at an advantage. Where a procurement is delayed or cancelled, DFID should take lessons away from this so similar events can be avoided in the future. Additional bidding
DFID’s use of private sector contractors

requirements that come out of the Supplier Review should not impose significant additional costs on contractors, as these may drive those least placed to bear them (i.e. smaller organisations) out of the market thus reducing competition. ( Paragraph 43)

10. We recognise that there are benefits to framework agreements, including the time and cost savings generated through greater administrative efficiency. However, there is a strong suggestion from evidence to this inquiry that they lock out organisations—particularly smaller ones with technical expertise—from bidding for DFID work. They can force smaller contractors into ‘second tier’ roles where their power and influence is reduced. In order for frameworks to work as intended and avoid narrowing the supplier base, they need to be updated regularly which is not current DFID practice. (Paragraph 52)

11. DFID should undertake a review of framework agreements and justify how their benefits outweigh the costs reported in evidence to this inquiry. Where framework agreements are used, DFID should commit to regular reviews and updates, allowing new market entrants access to bid for existing frameworks at more regular intervals. DFID should also consult with smaller organisations on how to make bidding for frameworks more accessible, offering tailored guidance to ensure that its procurement processes are not a barrier to entry. DFID should also justify why it continues to use framework agreements when the trend across government is moving away from them. (Paragraph 53)

DFID supplier and the supply chain

12. There is some evidence to indicate that there is healthy competition in DFID’s supplier market relative to other donors. However, there are a number of factors undermining the competitive elements of the market, including unequal access to Department officials, low numbers of bids and a range of other issues including unequal information and some organisations being locked out by framework agreements. Ensuring a competitive contractor market is a central component of DFID’s commercial strategy, and while it has the potential to lower costs and deliver greater value for money, this should be balanced with greater risk management. (Paragraph 62)

13. DFID should conduct market analysis, potentially with assistance from experts at the Competition and Markets Authority (CMA), to determine any issues that may be undermining market competitiveness. It should then take necessary steps to correct for these issues in order to create an increasingly level playing field for all potential bidders. (Paragraph 63)

14. Expanding its supplier base is another key component of DFID’s procurement and commercial strategy. While the Department has taken some steps to reach out to and include developing country contractors, these have had limited effect with only a tiny proportion of contracts still awarded to companies that are based in-country. We note that the UK Government made commitments to untying aid, both formally and in practice, yet some of DFID’s procurement practices (such as the establishment of framework agreements) can work against this commitment. (Paragraph 69)
15. **DFID should report on how it plans to increase its efforts, beyond what has already been stated in evidence, towards helping more developing country contractors bid for DFID work. It should ensure that the format of Early Market Engagement (EME) exercises is geared towards greater inclusion, and should report to us on whether greater use of in-country EME’s has increased the number of developing country contractor bids. DFID should also make use of the Untied Aid Public Bulletin Board and, if it continues not to do so, should clearly justify why not and describe an alternative approach to advertising contract opportunities to developing country contractors.** (Paragraph 70)

16. Despite DFID’s stated aim to expand the supplier base and facilitate access to DFID contracts by smaller organisations, evidence suggests that it does not have sufficient understanding of the challenges faced by small organisations nor how to address these. The broad Cabinet Office definition of SME’s means that DFID’s SME Action Plan is unable to capture the needs of small and micro enterprises. However, we also recognise that the Government is bound by this definition due to European Commission regulations. We also note that the use of Payment by Results (PbR) is likely to work against the aim of DFID procurement being more inclusive. (Paragraph 74)

17. **DFID should be more inclusive of small and micro enterprises by disaggregating its approach to SME’s to target small and micro enterprises. This should include both collecting data on the work contracted to such enterprises and producing a strategy on how opportunities for them to bid for DFID work can be expanded. DFID should also report to the Committee on how it plans to mitigate the impacts of Payment by Results so that it does not preclude smaller organisations from bidding as evidence suggests is currently the case.** (Paragraph 75)

18. A thorough understanding of DFID supply chains is essential to ensuring value for money and development impact in DFID programming. While we welcome DFID’s increased effort to map and better understand these supply chains, we are concerned that this is a feature of the delivery model that has been overlooked up to this point. While we recognise that DFID is not responsible for cases of mistreatment of sub-contractors, we stress that it is responsible for enforcing certain standards of conduct, and that a lack of enforcement and an over reliance on self-declaration of adherence to these standards has contributed to these behaviours. (Paragraph 84)

19. **In order to facilitate better engagement between DFID and the sub-contractors that deliver its programmes, DFID should establish a dedicated ‘sub-contractors unit’ within its Procurement and Commercial Department. Much like the Key Suppliers Management (KSM) system for larger contractors, this would act as the main access point for sub-contractors and offer them a more consistent pipeline of information on future opportunities, provide a channel for raising grievances and allow DFID to better understand the challenges they face and how it can help overcome them.** (Paragraph 85)

**Conduct and performance of contractors**

20. Recent reporting on the conduct of certain contractors shows that some have behaved in a way that is completely unacceptable, is not in line with the principles of the Department and is harmful to the public’s view of DFID’s work. While we
firmly believe that this is not representative of all of DFID’s suppliers, we affirm that there is a serious problem in the practices of certain organisations and that this is unacceptable. It is not clear whether the gravity of this is appreciated by certain contractors and we are yet to be convinced that they share our view that the sector needs a genuine rethink in terms of its approach. The allegations made of ASI should not be approached as an isolated incident by DFID, but as evidence that there is something inherently wrong with the culture in certain organisations. DFID needs to take a more robust approach in creating regulations and incentives that shape the sector so that it operates to the highest ethical standards. It is clear that DFID cannot rely on its approach of self-regulation. While it is up to contractors to adjust their practices, it is the Department’s responsibility to establish a set of rules and parameters and, critically, to enforce them. (Paragraph 89)

21. Many of the key areas of concern with respect to DFID’s use of contractors, such as profits, treatment of sub-contractors, commitment to ethical codes of conduct and honesty about capacity and capability in bids, are all addressed in DFID’s Statement of Priorities and Expectations (SoPE) for Suppliers. The fact that certain contractors breach the conditions of the SoPE suggest that not enough is being done to enforce it. While the prospect of adding to the SoPE might be well-intentioned, it is also likely to have the effect of overburdening smaller organisations to the point where they can no longer bid for DFID contracts. This will work against DFID's objective of expanding the supplier base. We also note that in particularly complex environments, staff rotations may be too short for them adequately to get to grips with the development context, and this may put them on the back foot in managing experienced contractors. (Paragraph 93)

22. Rather than expand compliance regulations, DFID should do more to ensure that the regulations set out in the current SoPE are effectively enforced. In its Supplier Review, DFID should explore ways that it can track compliance, with a particular focus on the issues raised in this report. DFID should also set out a clear set of consequences for contractors is they fail to comply with the SoPE. While such consequences should be proportionate, they should also be sufficiently firm to act as an effective deterrent against poor conduct. It should also consider extended postings in challenging environments, particularly where contractors are the dominant channel for delivery. This will help ensure that DFID staff have the requisite in-country experience to effectively manage complex programmes and ensure optimal delivery. (Paragraph 94)

23. DFID’s due diligence of contractors appears to focus excessively on the bidding stage and not enough on the implementation stage. There are examples to suggest this may have skewed the incentives of contractors to focus on winning contracts, not delivering them. While we recognise the logic in using Payment by Results (PbR) to incentivise effective delivery, we are concerned that DFID is not doing enough to mitigate the risks involved and this is to the detriment of quality programming and impact. (Paragraph 99)

24. DFID should rebalance its due diligence efforts to focus increasingly on contract delivery. It should also increase the resources of the Internal Audit Department (IAD) if necessary. Where PbR is used, DFID should use the research it has commissioned—
as well as the forthcoming work from ICAI—to create more robust guidance and training resources for staff on how to design effective programming milestones. (Paragraph 100)

25. Evidence suggests that continued poor programme delivery by contractors does not necessarily lead to the cancellation of contracts. Even in instances where it is recognised that DFID contracts are underperforming, they are cancelled ‘for convenience’ as this is an easier and cheaper route. While this may save money for the taxpayer in the short run, we are concerned about the long run value for money. Failing to recognise and record any fault of the contractor demonstrates a weakness in accountability and may result in missed opportunities for learning and strengthening for future programmes. Given the inherent difficulties faced by DFID in choosing the best organisation for the job, we are concerned by the fact that DFID, unlike other donors, appears to be unable to use past performance in assessing bids. It is unclear as to why this is the case given that the Crown Commercial Service states that this is explicitly permitted under the EU Public Procurement Directives. We are concerned about the potential effect this may have on contractors’ incentives. (Paragraph 105)

26. DFID should take a more robust approach to creating performance incentives and demonstrate practical ways it is going to do this in its Supplier Review. This should include setting out clear parameters on the grounds on which a contract might be cancelled, and ensuring that there is a credible risk of cancellation by adhering to these. DFID should also ensure that where a contractor is seriously underperforming, the contract should be cancelled on the basis of default so that the failure of the contractor is recorded and that lessons can be learned. In light of the UK’s decision to leave the European Union, DFID should ensure that it has substantial input into any discussions of Government-wide public procurement regulations to be implemented after withdrawal. Such regulations should give DFID greater freedom to take into account contractors’ past performance in evaluating bids. Other donors, such as USAID, have this power and use it. (Paragraph 106)

**Value for money**

27. We agree with DFID’s position that, where contractors offer the best value for money, programmes should be tendered rather than delivered through multilaterals or civil society organisations. However, we stress that there is a critical difference between profiting and profiteering. The vague definition of “fair but not excessive” profits provides little reassurance to the public that contractors are not getting rich from UK Aid. While we recognise that being too prescriptive on what is “fair but not excessive” may distort the market, there is room for discussion on what this constitutes. Benchmarking against the rates paid by other donor agencies to contractors is key to ensuring that DFID is getting value for money. The fact that this is done internally with no reporting or details of methodology points towards a lack of transparency. (Paragraph 111)

28. DFID should determine some clear parameters on what constitutes fair but not excessive profits. It should also commission an independent review which benchmarks contractor fees across DFID programmes (including in different locations and
comparing fragile and non-fragile states) as well as against other donors. It should also consider whether other donors are achieving better value for money through their differing procurement processes. (Paragraph 112)

29. We recognise that much of the media focus on the fees paid to consultants has been misleading, and that comparing these daily rates to the annual salaries of employees (and their benefits) is not comparing like for like. We welcome DFID’s move towards more transparent, open book contracting. However we also note concerns that this only happened last year and that, in the past, contractors may have exploited DFID’s inability to see costing breakdowns at the expense of value for money. We also note the approach of other donors towards fees, particularly Australia and its Aid Adviser Remuneration Framework (ARF). While we recognise concerns that such a prescriptive framework could distort the market, we believe that, if designed carefully, it can enhance transparency and deliver better value for money. (Paragraph 116)

30. We recommend that DFID consider an Australian-style consultant remuneration framework as an output of its Supplier Review. This framework should be prepared in collaboration with contractors to take into account their views, and should be designed carefully—building in an appropriate level of flexibility—to avoid any market distortions that may emerge. (Paragraph 117)

31. Disability inclusion is a key part of DFID’s strategy, as outlined in its Disability Framework. However, there is evidence to suggest that this issue is not being addressed in programmes delivered through contractors. A narrow definition of value for money may encourage contractors to focus on the easiest and cheapest to reach. The competitive nature of the contractor market and DFID’s strong focus on value for money may therefore be creating worrying incentives for them to overlook disability inclusion. (Paragraph 121)

32. DFID should ensure that the principles outlined in its Disability Framework are enforced in programming delivered through contractors and it should require that disability inclusion be written into contracts. (Paragraph 122)
Annex 1: Confidential oral evidence

As is outlined in the report, the Committee agreed to accept confidential evidence because it appreciated that those who know most about the detail of DFID’s use of contractors work in the sector and may have otherwise had reservations in being frank with the Committee for fear of jeopardising working relationships.

We held an oral evidence session with two experienced contractors who are referred to in the report as Contractor A and Contractor B. Extracts from this session that are featured in the report are below.

Contractor B

Q2: On the contractor market:

- Q2: “One of my biggest concerns is that not only does this market exist such that DFID is not really able to measure the delivery of its contractors and measure between them, but it is a DFID controlled market, so they are actually the market-makers. They are the regulator. Now, they do procurement and they do it okay, but they make a market and that market does not work well, because they do not understand it sufficiently well. That is not just to say that the contractors are all there trying to squeeze out every last penny and ripping off DFID; there is failure with DFID as well, and frustrations in not understanding how contractors work.”

Q2: On assymetric information in the market:

- “The issues, as [Contractor A] has started to allude to, are systemic in the market. There is some correlation between DFID’s control of its contracting structures to the old classic economics paper, “The Market for Lemons”, in that there is asymmetric information between the supply and the demand. Suppliers know how good they are, know what their availability is and know when they are having to tweak things. Unfortunately, and this comes on to [Contractor A’s] final point there, DFID is not really able to tell how good one person is versus another person, in terms of delivering non quantifiable results. How much better is the governance in Iraq this year than last year? I was once asked for a quantifiable gender indicator on the quality of the Iraqi budget. I said it would be 43% more gender-friendly. It is not going to work that way, so what are you buying? This leads into the safety of quantifiability or quantification, which then loses the nuance of whether we are making a difference to the Iraqi people, the Afghan people or the Tanzanian people.

Q3: On the reasons for issues in the contractor market:

- “Yes, it is human capacity, but it is also institutional systems and how the market actually operates, particularly around procurement. Rambling on just a bit, the point at which a procurement is finalised is an important pinch point in the market, because there is every incentive to win that contract and there is very little punishment for not delivering on the contract. You will say everything you possibly can to win that contract. With the increase in the aid budget and the decrease in the headcount, the arithmetic says that the contract size is going up,
so you get bigger, more integrated contracts, which means that the risk of not winning is greater, so the contractors will play every card they have and some they should not have to win the contract.”

Q5: On barriers to market entry for smaller contractors:

- “Starting with existing contractors in the UK, there are probably two particular types of barrier to entry. One is simply access to framework contracts. Where increasing amounts of DFID work are let through framework contracts, if you are not on the right framework, you are simply locked out. There has been an increasing amount of flexibility in the DFID procurement department, allowing people to jump between frameworks, but that still means that you are not at the front of the queue or you do not necessarily have an equal seat at the table.”

Q22: On the treatment of subcontractors:

- “There are a couple of other examples at the procurement stage where two firms [...] had pre bid agreements with a prime contractor on two different contracts. They said, “We will consult with you. We will share knowledge on how this bid is put together before we submit.” In one case, there was a rate cut of 25% imposed about four days before the bid submission, on the inputs by the subcontractor. In the other case, the bid was submitted and [...] despite there being a pre bid agreement on consultation, saying, “We did not have time to review with you. We submitted the bid. We cut your inputs by 25%. Take it or leave it.”

Q28: On DFID in-house capacity:

- “In answer to Nigel’s question, yes, there is capacity in there. It is not as good as it was in the past. A lot of those 20 year veterans have moved on. There is the potential capacity, but it is not well organised. If you had longer tours, specialists in particular regions rather than somebody popping from Jakarta to Islamabad to Kinshasa, clever though that person is, DFID would have the ability to drill down into what is going on in its projects. There is a degree of complacency among the contractors, because they go, “It is alright. We can outlast any two year posting on our programme so, if we have to deal with a troublesome person who is meddling a bit too much, then we will crack on. We will do it. We will fill in the forms and, in two years, we will get a new programme officer. That is fine.”

Q36: On the Australian Aid Adviser Remuneration Framework:

- “The Aid Adviser Remuneration Framework is the DFAT system, as [Contractor A] went through with the various bands of people. Obviously, you are typically trying to push people to the highest level you can. The main drawback was that, on occasion, I could not get people who I knew were good to work for those rates, so it does reduce flexibility, so I would prefer not to have absolute caps, but to have transparency.”

Q39: On whether examples of poor contractor conduct are commonplace:

- “As somebody who has spent [many years working with large contractors], it is absolutely embedded in the culture—absolutely.”
Q40: On possible conflicts with contractors feeding into programme design then bidding for the contracts:

- “There is one other quick issue on this, which is that it again comes back to lack of in house resources. DFID contracts out design work or they do not contract out design work, but contract out research to inform the design, so they can say there is no conflict of interest. [A contractor] pitched a low ball amount and undercut somebody who was better qualified to do some design work in [a country where DFID has a bilateral programme] recently. They hired freelancers to do it, but I cannot imagine that they produced that low ball bid for any other reason other than to make sure that they were ahead of the game in getting information, which is why everything should be published quickly without waiting. DFID procurement department says, “All the information will be shared at the time of bidding”. That is fine, but if somebody has inside information, asymmetric information or upstream information, they will have already tied up the best consultants, talked to the local partners, got better information, got their consortium together, etc.”

Q40: On possible conflicts with contractors feeding into programme design then bidding for the contracts:

- “I have an idea on it, which is to have an arm’s length organisation for your programme management. As [Contractor A] has said, a lot of really good talent has retired or moved to the consulting sector. I think, if you create some sort of arm’s length entity that can also do this whole of life programme design and management, so somebody who is willing to sign up for 25% of their time for the next six years to design this programme, see the procurement, see it through, recommend what inputs are needed, can be flexible and can be good to the contractors—the contractors are not always just trying to screw us; they are trying to deliver—that arm’s length organisation could bring in people who have left DFID or who want to come from the private sector, or you could bring in people from Australia, Germany, the US, Canada or whatever. You can bring people in with Foreign Office experience, as well as DFID experience, but you would have a cadre of people. The one thing is that those people will never then work for a contractor. We will give you a retainer. We will give you that, but you never sit on the other side of the table.”
Annex 2: Confidential written evidence

Following receipt of evidence from a number of contractors, we followed up with a list of questions seeking further information. We express our gratitude to Coffey International Development Ltd, Crown Agents, DAI, KPMG, Mott MacDonald, Nathan Associates, Palladium and PWC.

This additional evidence is not published in full due to the commercial sensitivity of some of the questions. Non-confidential responses and anonymised quotations referenced in the report are included below.

Q1: How many sub-contractors or local NGOs do you use on average to deliver a DFID-funded programme?

DAI Europe: “This varies quite widely depending on the purpose and design of each programme. For example, on the Expert Advisory Call Down Service which DAI manages for DFID, there are more than 60 sub-contractors and NGO members of the DAI consortium. In the last report on the use of SMEs that we prepared for DFID in December 2015, we identified more than 550 sub-contractors or local NGOs working across 27 DFID contracts, for an average of more than 20 per DFID-funded programme.”

Coffey International Development Ltd: “We are not aware of the number of cancelled DFID contracts or procurements over the last five years. However we have observed a recent increase in the number of procurement cancellations and retenders. We are aware of five cancelled tenders in the last eight weeks.”

Q3: How many contracts from DFID have been cancelled over the last five years? How does this work compare with your private sector clients?

Coffey International Development Ltd: “We are not aware of the number of cancelled DFID contracts or procurements over the last five years. However we have observed a recent increase in the number of procurement cancellations and retenders. We are aware of five cancelled tenders in the last eight weeks.”

Q7: What is the impact on programme design and execution of the often long lead times between DFID issuing an ITT [invitation to tender], the winning bid being selected and the contracts being executed so work can be begin?

Mott MacDonald: “Clearly, the longer it takes for DFID to tender and award a contract the greater the risk that there is a disconnect between the programme design (the drafting and approval of the business case), the inception phase if there is one, and project implementation. The longer it takes, the greater the risk that the social, political and economic environment may have changed, and the harder it is to retain key staff and sub-consultants so they are available once implementation begins. The greatest impact is, of course, on beneficiaries. We note that the time between issuing a tender and contract starting has considerably lengthened in recent years due to increased procurement scrutiny.”

Coffey International Development Ltd: “Third, long delays can also erode local stakeholders’ and beneficiaries’ trust in the supplier and in DFID’s commitments. This, in turn, can hinder effective delivery.”
Q14: How much do you estimate that you would spend in preparing a bid for a contract worth approximately £10 million? £50 million? £100 million?

Coffey International Development Ltd: “The level of spending that goes into preparing a bid is dependent on the timescales provided to us by DFID, the size and complexity of the programme, the level of grants / funds that make up the contract, and the extent to which we have a presence in the target countries. On average we spend £40,000 on a £10m proposal and up to £120,000 on a £50m proposal. This includes expenses and assigned staff time. This does not take into account staff overtime, including the weekends and evenings often required with the tight turnaround times and parallel project requirements. This can amount to an additional £10,000 to £15,000 per proposal.”

Confidential: “The cost of bidding for DFID contracts has increased significantly in recent years. In our experience, DFID tenders are more expensive to submit than those of other donors, and certainly of our private sector clients. This is due to both the competitive nature of the market and also the depth of content that DFID requires. We believe this represents a significant barrier to entry for both new and small firms.”
Appendix: DFID Statement of Priorities and Expectations for DFID’s Supplier and Partner Relationships (including Suppliers; Private Sector Partners, NGOs)

This Statement sets out a single set of expectations that DFID has of external organisations with which it works, alongside standard elements of good practice.

The statement outlines the activities and behaviours we expect organisations we work with to adhere to including policies and practices relevant to DFID and wider HMG priorities. DFID is committed to acting responsibly and with integrity, being transparent and accountable, focusing on poverty and development impact and continually improving value for money.

Partner organisations should demonstrate commitment to poverty reduction and to DFID’s priorities including work undertaken in fragile or conflict affected states, for girls and women, youth engagement, climate change and wealth creation.

DFID expects partner organisations to:

1) **Act responsibly and with integrity by:**
   a) making available a statement of compliance with key legislation and international principles on labour, social and environmental matters;
   b) demonstrating commitment through actively seeking and making a positive contribution to development, social and environmental sustainability through its business activities;
   c) pursuing and adhering to anti-discrimination policies, with particular attention to girls and women;
   d) applying risk management and mitigation processes that assure a zero tolerance approach to tax avoidance, corruption, bribery and fraud throughout the supply chain;
   e) engaging supply chain partners in a way that is consistent with DFID’s treatment of its suppliers or partners (when pricing, in subsequent service delivery, or in partnership agreements), and demonstrating this to DFID where required;
   f) building local capacity by proactively seeking ways to develop local markets and institutions;
   g) safeguarding the integrity and security of their systems, for example, as per the HM Government Cyber Essentials Scheme[^208];
   h) assuring that UK Government funding provided is not used in any way that contravenes the provisions of applicable terrorism legislation.

2) **Be transparent** – in relation to organisational practices and the use of government funding by:

a) publishing a statement of how delivery on social and environmental values are articulated;

b) making available a list of relevant policies together with a description of measures of how these are put into practice (e.g. supplier codes on fraud & corruption, due diligence);

c) demonstrating commitment to ethical codes of conduct, for example through membership/signatory of codes, both directly and within the supply chain, e.g. conventions, standards or certification bodies (such as ETI, UNGC, Global Reporting Initiative, Extractive Industries Transparency Initiative), as appropriate;

d) publishing reports as a minimum on an annual basis, on environmental, social and governance performance (including but not limited to improving the lives of girls and women, Environmental, or Sustainability Reports).

e) Publishing DFID funding data in accordance with the International Aid Transparency Initiative (IATI) standard

3) **Be Accountable** - whether in every day and exceptional situations by:

a) developing and implementing policies that address the need for remedy and redress if things go wrong, in line with the UN Guiding Principles on Business and Human Rights;

b) actively seeking to promote the involvement of people in the business decisions that affect their lives.

4) **Support DFID priorities and objectives by:**

a) sharing innovation and knowledge to maximise overall development impact in ways that do not adversely impact competitive advantage;

b) supporting wider HM Government Policy initiatives including the support of SMEs, prompt payment, Human Rights and modern slavery issues and the support of economic growth in developing countries.

5) **Improve Value for Money** – demonstrate and continually strive to improve value for money in all that they do by:

a) actively seeking to maximise international Aid or Development results whilst maintaining or reducing costs throughout the life of the programme;

b) budgeting and pricing realistically and appropriately to reflect programme requirements and risk levels over the life of the programme;

c) being honest and realistic about capacity and capability;

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1 [https://www.unglobalcompact.org/issues/human_rights/The_UN_SRSG_and_the_UN_Global_Compact](https://www.unglobalcompact.org/issues/human_rights/The_UN_SRSG_and_the_UN_Global_Compact)
D) accepting that DFID works in challenging environments, acting to manage uncertainty and change in ways that protects value with government funding;

E) proactively pursuing continuous improvement to reduce waste and improve efficiency in internal operations and within the supply/delivery chain;

F) incorporating fair but not excessive rewards;

G) implementing a transparent, open book approach which enables scrutiny on value for money choices;

H) avoiding the use of restrictive exclusivity agreements;

I) providing assurance that the policies and practices of supply/delivery chain partners and affiliates are aligned to the expectations outlined in this statement;

J) applying pricing structures that align payments to results and reflect an appropriate balance of performance risk;

K) Accepting accountability and responsibility for performance, with timely identification and resolution of issues ensuring lessons learned are shared.

March 2016
Formal Minutes

Monday 27 March 2017

Members present:

Stephen Twigg, in the Chair

Stephen Doughty        Wendy Morton
Pauline Latham

Draft Report (DFID's use of private sector contractors), proposed by the Chair, brought up and read.

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

Paragraphs 1 to 122 read and agreed to.

Annexes agreed to.

Summary agreed to.

A Paper was appended to the Report.

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

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

Ordered, That embargoed copies of the Report be made available (Standing Order No. 134).

[Adjourned till tomorrow at 9.00 a.m.]
Witnesses

The following witnesses gave evidence in public. Transcripts can be viewed on the inquiry publications page of the Committee’s website.

Monday 20 February 2017

Joy Hutcheon, Director General, Finance and Corporate Performance, Department for International Development; Nick Ford, Head of Procurement and Commercial Department, Department for International Development

Q46–142
Published written evidence

The following written evidence was received and can be viewed on the inquiry publications page of the Committee’s website.

DUC numbers are generated by the evidence processing system and so may not be complete.

1. Adam Smith International (DUC0009)
2. Bond (DUC0012)
3. Centre for Development Results (DUC0007)
4. Coffey UK (DUC0011)
5. Crown Agents (DUC0013)
6. DAI Europe (DUC0002)
7. Department for International Development (DUC0016), (DUC0018), (DUC0019), (DUC0020), (DUC0017)
8. Dr James Morton (DUC0003)
9. Hambleside Group (DUC0006)
10. Mott MacDonald (DUC0010)
11. Nathan Associates (DUC0005)
12. Palladium (DUC0008)
### List of Reports from the Committee during the current Parliament

All publications from the Committee are available on the [publications page](#) of the Committee’s website.

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

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