



National Audit Office

Report

by the Comptroller
and Auditor General

Cabinet Office

Transforming government's contract management

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Transforming government's contract management

Report by the Comptroller and Auditor General

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Sir Amyas Morse KCB
Comptroller and Auditor General
National Audit Office

2 September 2014

Following revelations of G4S and Serco's overbilling, and weaknesses in contract management procedures in a December 2013 review, the government is starting a large change programme to improve how it manages its contracts.

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Key facts

£40bn

spent by central government on procuring goods and services, 2013-14 (estimated)

60

contracts tested for overbilling

34

had issues with billing to some extent

- 5 contracts** have been referred to the police or the Serious Fraud Office
- £179.4 million** has been paid by G4S and Serco, after identifying overbilling
- 73 contracts** were reviewed against our 2008 framework by the Ministry of Justice, Home Office, Cabinet Office and the Department for Work & Pensions (each contract assessed against 8 areas, a total of 584 assessments)
- 343 out of 584** areas of contract management assessed as weak (of this, 73 were considered to create a material risk of overbilling)
- >100,000** contracts in central government (estimated)
- 4,000 people** commercial specialists across central government (estimated)

Summary

1 In November 2013 we set out how government was facing what we described as a crisis of confidence in its contracting of public services. Contracting out services is a useful tool to reform public services and improve value for money. However, we raised questions about competition in the market for government services and whether contractors' returns were transparent and their performance satisfactory. We also showed how government must improve oversight, control and assurance over contracted-out services.

2 Last year, a series of government contractor and contract management failures emerged. In particular, the Ministry of Justice announced in July 2013 that it had found significant overbilling in its electronic monitoring contracts with G4S and Serco dating back to 2005. The Ministry commissioned further reviews of their other contracts and the Cabinet Office did the same for the major G4S and Serco contracts across government. The Home Office and the Department for Work & Pensions also commissioned internal reviews of contracts with a range of contractors. In total, central government tested 60 contracts for overbilling and 73 for contract management practice.

3 The reviews found widespread problems in administering government contracts, including poor governance, record keeping and capacity issues. These findings echo our work on contracts and contract management dating back to 2006. The reviews recommended how the new Crown Commercial Service (CCS) and departments could improve contract management.

Scope of this report

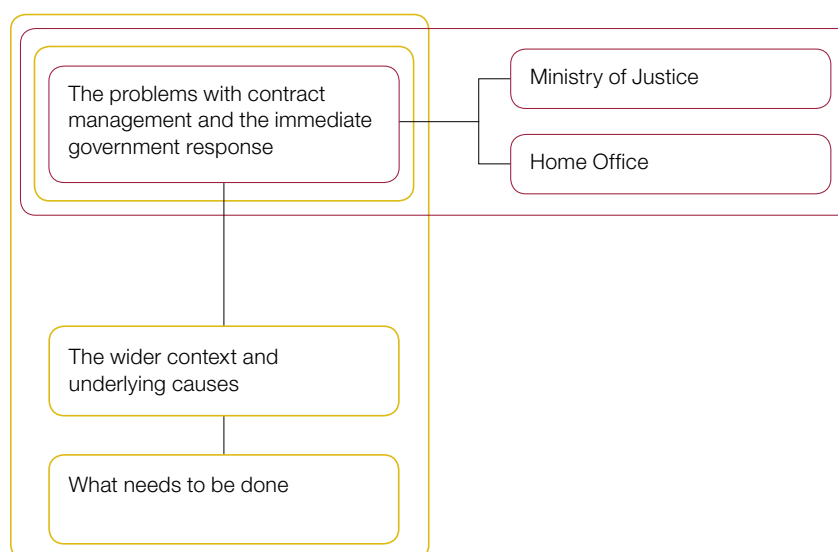
4 This report looks at how government has responded to the findings about its weak contract management in its procurement of services:

- **Part One**
Sets out the findings of the government reviews and government's response.
- **Part Two**
Sets out the wider context and underlying causes of weaknesses in contract management.
- **Part Three**
Sets out our view of the way in which contract management needs to change, building on current government initiatives.

5 We are publishing an accompanying report: *Transforming contract management in the Ministry of Justice and the Home Office*. This shows a detailed example of these reforms and challenges in practice (**Figure 1**).

Figure 1

Our two reports on contract management



- Cross-government report: High-level findings across government
- Home Office and Ministry of Justice report: What this means for Home Office and Ministry of Justice

Source: National Audit Office

Key findings

Response to overbilling

6 **The Cabinet Office, HM Treasury, and the Ministry of Justice reacted strongly in handling G4S's and Serco's overbilling.** However, government was constrained in its actions and acted as if the firms were too important to fail: their failure could create widespread disruption to public services and government wanted their ongoing participation in competitions. They referred both companies to the Serious Fraud Office (SFO), whose investigations are still ongoing. They demanded that both companies change, and both companies proposed formal processes of 'corporate renewal'. These included changes to management, organisational structures, ethical training and controls. There was no official ban on letting new contracts to the companies, but departments had to get the Minister for the Cabinet Office to approve new contracts and the companies withdrew from several tender processes.

7 Government secured payments of £179.4 million from the contractors related to overbilling issues. Government negotiated payments of £104.4 million from G4S and agreed £68.5 million from Serco covering rebates, investigation costs and interest relating to the overbilling on electronic monitoring. Following reviews of further contracts, G4S paid government £4.5 million in respect of billing issues on 2 court facilities management contracts, which were also referred to the SFO. Serco paid £2.0 million relating to its prisoner escorting and custodial services contract, which has been referred to the City of London Police.

8 Government's reviews provided evidence of further billing or reporting errors across government contracts, though no evidence of deliberate wrongdoing.

The government reviews were thorough, but only 60 central government contracts were tested for overbilling, of which some 34 had issues in the amount billed. These issues included both under- and overbilling. Given the flaws in contract management controls across government, it is in our view probable that other instances of overbilling have occurred across government's wider contract portfolio. We cannot be sure of the extent of such overbilling or whether it is material.

Problems with contract management

9 The reviews found widespread problems with how government manages its service contracts. As well as testing for overbilling, 73 contracts were tested against the 8 areas of the NAO's 2008 good practice framework for contract management.¹ Issues were found on all 8 areas, for example:

- **Planning and governance (issues on 38 out of 73 contracts tested)**
Departments lack visibility of contract management at board level and lacked senior-level involvement.
- **People (40 issues)**
Government does not have the right people in the right place for contract management. There were gaps between the numbers and capability of staff allocated to contract management and the level actually required.
- **Administration (39 issues)**
Contract management is not operating as a multi-disciplinary function. There was often limited interaction between finance, commercial and operational contract management functions.
- **Payment and incentives (48 issues)**
Government is not fully using commercial incentives to improve public services. Levels of payment deductions allowed by contracts are often insufficient to incentivise performance. Open-book clauses were rarely used.

¹ National Audit Office, *Good practice contract management framework*, December 2008.

- **Managing performance (50 issues)**

Contractual performance indicators are often weak and government is too reliant on data supplied by contractors.

- **Risk (47 issues)**

Government does not have sufficient understanding of the level of risk it is retaining on contracted-out services. None of those in the cross-government review shared risk registers with the contractors to ensure all understood who was managing what.

- **Contract development (50 issues)**

Departments are paying insufficient attention to the impact of contract change. For example, departments made changes at operational level in isolation from other service areas. Systems for maintaining up-to-date versions of contracts remain weak.

- **Managing relationships (31 issues)**

Not all departments have had a strategic approach to managing supplier relationships. Senior management engagement with suppliers has not been widespread across government. A lack of meaningful incentives for innovation can inhibit shared approaches to problem solving and service improvement.

10 Poor contract management is a long-standing issue. By the middle of the last decade there was a large number of mature contracted-out services across government. Our work started to highlight widespread problems with contract management. In our 2008 cross-government report on the management of service contracts we said that no commercial director or head of procurement rated the resources allocated to managing major contracts as 'good'. We highlighted poor risk management, inadequate performance measurement and limited use of performance incentives.² Since then, we have reported on many contracts with weak contract management. These weaknesses have far-reaching consequences, including:

- **Fraud and error**

For instance, better scrutiny of payments and understanding of the contract could have prevented the overbilling found in the Ministry of Justice's contracts referred to authorities.

- **Not managing risk**

For instance, the Ministry of Defence's failure to provide ICT infrastructure critical to the success of the Army's recruitment contract with Capita impacted on recruitment activities and increased costs.³

2 Comptroller and Auditor General, *Central government's management of service contracts*, Session 2008-09, HC 65, National Audit Office, December 2008.

3 Comptroller and Auditor General, *Army 2020*, Session 2014-15, HC 263, National Audit Office, June 2014.

- **Risk of contractual dispute**

For instance, ambiguities in the Home Office's immigration removal centre contracts meant that disagreements were difficult to settle.⁴

- **Performance deductions are not always enforced**

For instance, the Home Office did not enforce penalties for defects in asylum seeker accommodation as it felt that the contracts were at an early stage.⁵

- **Not understanding how contracts meet policy objectives**

For instance, poor senior oversight meant the risk profile on the Department for Work & Pensions' Work Programme was changed in the contractors' favour.⁶

- **Use of commercial levers**

For instance, pressures to find cost savings led HM Revenue & Customs (HMRC) to trade away some of its negotiating power and hindered its ability to get strategic value from its long-term Aspire ICT contract. When negotiating cost savings in response to successive funding settlements, HMRC conceded many of its commercial safeguards through major renegotiations of the contract between 2007 and 2009, including the right to share in supplier profits when they were higher than target and the right to compete services. HMRC estimates it achieved savings of £750 million through such negotiations. Since 2012, HMRC has negotiated some of these commercial controls back.⁷

11 Previous attempts to improve contract management have not delivered sufficient change. Government has sought to improve its general commercial capability since the early 1990s, most notably with the Gershon reforms from 1999 and the more recent efforts by the Cabinet Office. We published a good practice framework for contract management with our 2008 report⁸ and the Committee of Public Accounts recommended how to improve contract management in 2009. The Office for Government Commerce (then part of HM Treasury) accepted this, but it failed to influence departments and focus drifted away. More recently, the Cabinet Office has focused on using government's collective buying power to make savings, rather than improving individual departments' contract management.

4 HM Government, *Cross Government Review of Major Contracts*, December 2013.

5 Comptroller and Auditor General, *COMPASS contracts for the provision of accommodation for asylum seekers*, Session 2013-14, HC 880, National Audit Office, January 2014.

6 Finding from cross-government review.

7 Comptroller and Auditor General, *Managing and replacing the Aspire contract*, Session 2014-15, HC 444, National Audit Office, July 2014.

8 National Audit Office, *Good practice contract management framework*, December 2008.

12 The underlying causes of problems in contract management go beyond poor administration and lapsed awareness. Although it is difficult to generalise across 17 departments, from our collective experience of looking at government contracts, we have identified 4 root causes of these problems with contract management:

- **Government fails to recognise the value of contract management.** The purpose of contract management is to use commercial mechanisms to improve services and reduce costs. Too often contract management has been seen as delivering the deal that was agreed when the contract was signed. This has meant that contract management has been seen as a way to avoid things going wrong, rather than unlocking value. Government needs to recognise that value is achieved over the life of the contract. This means designing policies it has the capability to deliver, planning for the contract management stage earlier, and paying it more attention.
- **Senior managers in central government departments have not taken contract management seriously.** Central government has yet to adapt to the commissioning role it aspires to. Departments have not adapted governance to the expanding role of government contracting: they have lacked the basic infrastructure of oversight, senior engagement, challenge and scrutiny. Systems of governance have focused on approving new projects, as if government's responsibility ends when the contract is signed.
- **Senior managers have not demanded visibility over their contracts.** Senior managers have not always acted as if they recognised that departments are responsible and carry the risk for the services they have contracted. Managers have rarely demanded combined portfolio information to scrutinise and challenge operational contracts. Senior managers have often only engaged on contracting issues to firefight problems. As a result, they have put little pressure on teams to improve the information they rely on to manage the contract.
- **Government has a permanent disadvantage in commercial capability.** There have been many initiatives aimed at improving commercial capability in the past and more improvement is possible. Traditionally, the procurement profession has had a low status in the civil service, while contract management has been seen as low status within the procurement profession. Cabinet Office estimates government as a whole deploys less of its specialist commercial resources on contract management than the private sector. The profession has lacked the sway over colleagues to implement good practice, and struggled to attract the best talent and skills. Furthermore, without a way to measure the value of this deployment, contract management has been vulnerable to administration cuts and under-investment. Yet it is doubtful that the government can improve its capability to be able to have the best contract managers on all its contracts. It will not pay either to bring in or retain commercial experts to match the combined expertise of its contractors.

Government's response

13 The Government is taking the findings of contracting problems very seriously. Since autumn 2013, accounting officers and senior commercial officials have met regularly to oversee the reviews and the resulting change programmes. The group is known as 'Markets for Government Services (Officials)' (MGS(O)) and is led by the Head of the Civil Service and the Cabinet Secretary. The group is coordinating government's strategic response including market development, contingency plans for supplier failure and transparency (**Figure 2**). Its focus on contracting provides a window of opportunity to embed a sustainable change in how government manages providers.

Figure 2

The government's response

The government, led by the 'Markets for Government Services (Officials)' group has taken the findings very seriously. In response it has:

- Secured payments of £179.4 million from G4S and Serco related to overbilling issues. They also demanded that both companies change, and both companies proposed formal processes of 'corporate renewal'.
- Undertook a number of reviews across government to test for overbilling and assess the quality of contract management.
- Asked all departments to put in place plans to improve their contract management. These change programmes are currently underway.
- Launched commercial capability reviews to test how far departments have embedded changes.
- Increased its focus on some of the underlying issues, by:
 - Examining how government can maintain and further develop competitive markets for government services, to encourage new entrants through both overall market design and specific procurement competitions.
 - Starting to work with independent groups such as the CBI to review the transparency around procurement competitions, ongoing contract performance and the use of open book.
 - Starting to test departments' contingency planning so government is better-placed to deal with supplier failure.
 - Improving data on government's strategic suppliers and managing its relationships more strategically as a single customer through the use of crown representatives.
 - Further reforming the public procurement process to speed up procurement and make procurement more accessible to SMEs.
 - Improving government's overall commercial capability through the establishment of the crown commercial service and initiatives to improve commercial recruitment, training and development.

Source: Interviews with officials and review of MGS(O) papers

14 Departments have launched significant change programmes to improve how they manage contracts. The Cabinet Office asked all departments to put in place plans to improve their contract management by February 2014. All accepted the need to improve. Our accompanying report looks in detail at the changes under way in the Ministry of Justice and the Home Office. Together with the Department for Work & Pensions and the Ministry of Defence, they are the most advanced in their change programmes. The Cabinet Office and HM Treasury are undertaking commercial capability reviews on departments to test how far departments have embedded these changes.

15 The Cabinet Office is also trying to improve its management of common goods and services. The CCS was launched on 1 April 2014. Departmental commercial staff and responsibility for procuring certain categories of goods and services have already started to move across to the new service. Concentrating commercial expertise in a single organisation is likely to help with general capability constraints. However, moving staff to CCS may make departmental reform more complicated in the short term. Furthermore, the CCS is still developing its own capability, with recent changes to its senior management and governance, and new systems and procedures being introduced to manage contracts.

Transforming the management of contracts

16 The current reforms are going in the right direction. Below we set out the steps we see as important to transforming the management of contracts and how current initiatives are contributing to this.

Enabling a commissioning approach

17 Government needs to put in place the systems and processes to enable the effective oversight and management of contracts. A common understanding of the structures and systems is emerging from the current reforms under way within departments. In particular:

- **Governance**
Departments are improving their governance of operational contracts. Departments are appointing senior champions for contract management; clarifying senior responsible owners and lines of escalation; and having a senior forum to challenge, scrutinise and oversee working contracts and liaise with strategic suppliers.

- **Basic contract information**

Departments do not have information systems that combine the needs of finance (paying contractors), procurement (planning for and conducting bidding), or contract management (understanding performance, costs, the commercial position and the agreed contract). A few larger departments are still putting in place contract registers. We have yet to see a system that shows departments their current contracts including all changes and contractor communications. The Cabinet Office is setting up a common set of data requirements for government contracts. It will re-launch the Contracts Finder database by October 2014, which is designed to meet procurement needs. It also intends to provide a contractor relationship management system for the new CCS by the end of 2014. However, this plan is undeveloped.

- **Integrated structures**

Departments are taking different approaches to integrating contract management within the business. Some are building end-to-end commercial teams that follow the contract through its life. Others are building specialist commercial teams to focus on each project stage. Some departments are also clarifying how the commercial and operational teams will manage the contract.

- **Integrated processes**

Contract management needs to be integrated into the commissioning process. This means designing policies and contracts with a view to the contract management capability available and any flexibility required. The Cabinet Office has updated its guideline standard operating procedures to ensure contract management is mobilised earlier.

Understanding and influencing suppliers

18 Government needs to ensure responsibility for the delivery of contracted-out services and the control environment rests with contractors. Government needs to create a situation where it can rely on its contractors even when it is not deploying its best contract managers to oversee them. Senior executives within contractors should accept, through the contract, the personal accountability for delivery that senior responsible owners accept within the civil service. Such a system would have 3 features:

- **Intelligence on strategic suppliers**

The example of G4S and Serco shows how government needs to be far more inquisitive about the strategy, internal operations and culture of its strategic providers. Where government is reliant on strategic contractors, it is reasonable that it has very clear expectations about how that organisation behaves and manages itself. Information is readily available through sources such as public announcements, investor information and the work of market analysts. Skilled analysis, collation and sharing of this information will improve the intelligence currently provided to the crown representatives who lead cross-government negotiations with strategic suppliers.

- **Transparency**

The Cabinet Office and the Confederation of British Industry (CBI) are working together to produce a joint set of principles for improved transparency over contracting. Internal audit divisions are increasing their work devoted to contract management and starting to think about how to assure the controls for strategic providers. The Department for Work & Pensions, for example, is requiring new contractors to commission external reviews to give assurance on the contractor's controls. These initiatives need to be brought together into an integrated system of control, transparency and assurance. Departments should set out the objectives of the control environment, and use transparency and assurance mechanisms to ensure compliance.

- **Incentives**

Government needs to be better at enforcing its contracts and deducting penalties. We see post-contract audit reviews, gain-share arrangements and profit claw-back playing a greater role in ensuring incentives are aligned and value is not lost in adversarial behaviour. Government and industry now accept that open-book accounting needs to be widely used to build trust and ensure incentives are aligned. However, there are a lot of details to be worked out. The Cabinet Office is undertaking pilots to establish how its regular use will be implemented. This needs to draw on knowledge from departments such as the Ministry of Defence which have experience in this area. We would expect government to develop data analytics to compare costs and margins between contracts.

Making the most of limited commercial capability

19 Government needs to find ways of making the most of its commercially experienced people. There needs to be a balance struck between departments retaining sufficient capability to manage their contracts day-to-day and the role of the centre in targeting resources where needed. The Cabinet Office's current initiatives are at an early stage, but are likely to have a positive impact:

- **An enhanced role for commercial staff**

The Cabinet Office and departments recognise that they have focused too much on procurement, and neglected the scoping and operational stages where they can add most value. It is not clear to what extent the current commercial workforce has the right skills. Departments need to consider carefully how they manage any restructuring. However, the new role is likely to be more exciting and influential within the civil service. We hope that it will improve staff engagement and make the profession more attractive to those starting their career or coming from outside the civil service.

- **Central support**

There is a growing central capacity to support departments. The Crown Commercial Service's complex transactions team provides support to departments with complex negotiations or commercial issues. Crown representatives support departments on negotiations with strategic suppliers. Infrastructure UK within HM Treasury provides supports for projects involving private finance. The Cabinet Office is also establishing a common data set for contracts across government (paragraph 17 above) and has issued guidance on how contracts can ensure that procurement information can be shared within government.⁹ Better sharing of information on contracts would allow departments and the centre to make better use of a central shared capability.

- **Structured professional development**

Commercial skills are a core part of *The Civil Service Reform Plan*¹⁰ and the accompanying capabilities plan. The CCS is taking on more responsibility for the development and deployment of skills and experience across the profession. It is recruiting centrally for senior posts, setting up a commercial fast-stream and apprenticeship scheme, developing links with universities, putting in place an interchange programme with industry, identifying a framework of skills and experience for staff to attain, and developing core training. Commercial skills also forms part of the Major Projects Leadership Academy syllabus, while departments are also developing their own extra training.

⁹ Cabinet Office, *Procurement Policy Note – Information sharing in Government procurement exercises*, available at: www.gov.uk/government/publications/procurement-policy-note-0114-sharing-information-within-government, February 2014.

¹⁰ HM Government, *The Civil Service Reform Plan*, June 2012, available at: www.gov.uk/government/organisations/civil-service-reform

Value for money conclusion

20 The government will not get value for money from its contracts until it improves contract management. The Cabinet Office, HM Treasury and major spending departments have recognised the scale of the issue and have responded accordingly. The major spending departments have launched significant change programmes to improve their contract management. The Cabinet Office is strengthening its role in supporting the commercial profession, managing collective spending on common goods and services and supporting departments. We believe this represents an opportunity to bring about needed change. Nonetheless, there is a lot still to be worked out. In our view there needs to be widespread change in the culture of the civil service and the way in which contractors are managed. There needs to be more emphasis on a commissioning approach, transparency over the contractors, use of open-book to align incentives and a targeted focus of the government's commercial capability.

Recommendations

21 We have set out above the transformation needed in government's management of its contracts. We make 2 recommendations to the centre of government (HM Treasury and the Cabinet Office) aimed at ensuring that these come about:

- a** **The Cabinet Office should set up a cross-government programme to improve contract management, building on the work of the Markets for Government Services (Officials) group.** This will help to formalise existing arrangements and help to make improvement plans more sustainable. Departments' programmes are not joined up and central departments have not coordinated a formal programme, supported by appropriate management techniques. Given the culture change required and the need to sustain efforts across government, the programme should be part of the Major Project Authority's portfolio. The Cabinet Secretary, the Head of the Civil Service and government's Chief Procurement Officer should champion better contract management, especially to senior managers outside the commercial function.
- b** **HM Treasury and the Cabinet Office should continue to use commercial capability reviews to ensure reforms are embedded.** Our 2008 good practice framework gives a reasonable guide to the basic administration and governance every contract needs. The current departmental reforms are creating a common understanding of good practice in the organisational governance, systems and structures, information and capability needed for effective contract management (Figure 5 on page 25). Given current progress, we would expect all departments to have these in place by the end of 2015. The commercial capability reviews should also cover the Crown Commercial Service (CSS). The CCS needs to integrate its contract management processes with these new arrangements within departments. The Cabinet Office should measure the CCS's success by its ability to meet departments' needs.

Part One

Government's response to overbilling on major contracts

1.1 This part of the report sets out government's initial response to the discovery of overbilling. It looks at:

- government's contract management reviews;
- the central response to the reviews, including action on G4S and Serco; and
- the role of the new Crown Commercial Service (CCS).

Government reviews of overbilling and contract management

Instances of overbilling and error

1.2 In July 2013 the Ministry of Justice announced that it had found significant overbilling in its electronic monitoring contracts with G4S and Serco dating back to 2005. The Home Office let contracts to G4S and Serco for electronic monitoring in 2005, which were transferred to the Ministry of Justice in 2008.¹¹ The contracts were due to end in April 2013. Ministry staff working on the competition for new contracts discovered data anomalies and separately a whistleblower reported their concerns about operating practices at G4S. The Ministry commissioned PwC to undertake a forensic audit of the contracts in May 2013. The Secretary of State later announced that he was referring the matter to the Serious Fraud Office (SFO), whose investigation is ongoing.¹²

¹¹ Comptroller and Auditor General, *The Electronic Monitoring of Adult Offenders*, Session 2005-06, HC 800, National Audit Office, February 2006.

¹² Further details on the history of these reviews are included in our report: Comptroller and Auditor General, *The Ministry of Justice's electronic monitoring contracts*, Session 2013-14, HC 737, National Audit Office, November 2013.

1.3 Departments undertook a number of separate reviews to determine whether there was any further overbilling and assess the quality of contract management:

- The Cabinet Office announced a review of central government contracts with G4S and Serco on 11 July 2013 (the cross-government review).¹³ It commissioned PwC and Moore Stephens to audit 28 of the largest contracts held with G4S and Serco across 8 central government bodies.
- The Ministry of Justice and the Home Office decided to further review a selection of their major contracts with various contractors.¹⁴
- In June 2014 the Department for Work & Pensions (DWP) commissioned its own internal review on its management of 15 of its major contracts. This did not look for overbilling; 5 other DWP contracts had already been tested as part of the cross-government review.

1.4 The cross-government¹⁵ and Ministry of Justice¹⁶ reviews reported publicly on 19 December 2013. The other reviews reported their findings internally. The reviews were thorough. Those that looked at overbilling examined a large enough sample of invoices to give reasonable assurance that contractors had provided the service and the amount billed agreed with the contract. Across all the reviews, 60 different contracts were tested for overbilling and 73 were tested for contract management control (**Figure 3**).

1.5 The cross-government review did not find evidence of deliberate wrongdoing by Serco or G4S. It found some instances of small unexplained discrepancies between amounts billed and the underlying contract. These included under- and overbilling thought to be through error rather than deliberate intent.

1.6 The Ministry Of Justice's review found 3 possible instances of wrongdoing. Early findings from the Ministry's review suggested that Serco staff may have falsified data on prisoner arrival times. The Ministry and Serco jointly referred the matter to the City of London Police on 28 August 2013.¹⁷ The Ministry also referred 2 G4S contracts for facilities management in courts to the Serious Fraud Office (SFO) on 19 December 2013.¹⁸ The Home Office review found no evidence of deliberate wrongdoing, but did find minor billing errors and weaknesses with the control environment.

1.7 Of the 60 contracts tested, some 34 had issues with billing, including instances of underbilling and lack of documentation to determine whether the service had been provided.

13 Available at: www.gov.uk/government/news/review-of-government-g4s-and-serco-contracts, 11 July 2013.

14 Further details of the Home Office and Ministry of Justice reviews are in our report: Comptroller and Auditor General, *Transforming contract management in the Ministry of Justice and the Home Office*, Session 2014-15, HC 268, National Audit Office, September 2014.

15 HM Government, *Cross Government Review of Major Contracts*, December 2013.

16 Ministry of Justice, *Contract management review*, December 2013.

17 Available at: www.gov.uk/government/news/moj-audit-of-serco-contracts-prison-escort-services

18 G4S website, Investor News announcement, 19 December 2013.

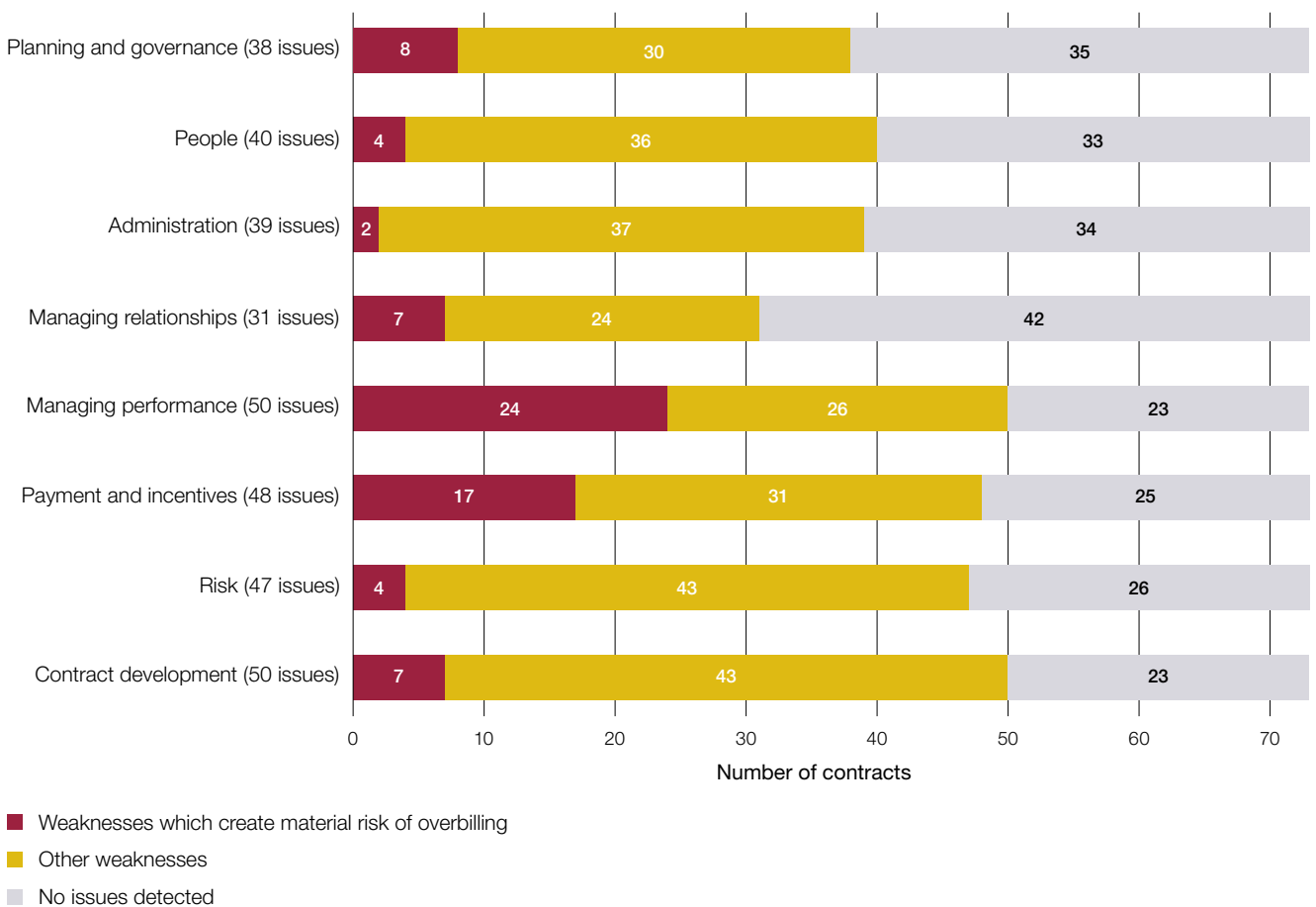
Wider contract management problems

1.8 The reviews also identified a range of contract management weaknesses across government (Figure 3). Contracts were tested against the 8 areas of our 2008 good practice framework and problems were found across all areas. Contract management weaknesses and their causes are examined in more detail in Part Two of this report.

Figure 3

The reviews found issues against all areas of our framework

Contract management framework area



Notes

- Includes the cross-government review (28 contracts with G4S and Serco, all of which were tested for overbilling), the Ministry of Justice (17 reviewed, of which 7 were also tested for overbilling), the Home Office (13 additional to the cross-government review, of which 5 were tested for overbilling) and the Department for Work & Pensions (15 contracts, which were only tested against the framework). This does not include a further 20 Ministry of Justice contracts tested only for overbilling.
- In total 73 contracts (with various contractors) were reviewed against the NAO framework and 60 were tested for overbilling.

Source: National Audit Office analysis of government reviews of contract management

1.9 It is likely that there is further overbilling in other contracts across government. The reviews found particular weaknesses in managing performance. These include weak verification of information provided by contractors. For example, in one contract the Ministry of Defence's poor record-keeping meant the reviewers could not verify whether a contractor provided the number of staff billed for, although the service was satisfactory. The reviews tested billing in 60 contracts and controls in 73 contracts, but central government has well over 100,000 contracts.

1.10 Weaknesses in contract management have far-reaching consequences for departments:

- **Fraud and error risk**

Without basic scrutiny of payments and performance, departments rely on the contractor to interpret the contract correctly, and meet the standards the public expects. For instance, better scrutiny of payments and understanding of the contract could have prevented the overbilling found in the Ministry of Justice contracts referred to authorities.

- **Not managing risk**

Departments often do not understand what the risks on their contracts are, or who bears them. They then do not manage the risks properly. For instance, the Ministry of Defence's failure to provide ICT infrastructure critical to the success of the Army's recruitment contract with Capita impacted on recruitment activities and increased costs.

- **Risk of contractual dispute**

Without good change control, departments risk not knowing what the contract requires the supplier to do. Without both parties understanding the contract the relationship with the supplier suffers, potentially leading to disagreements. For instance, ambiguities in the Home Office's immigration removal centre contracts meant that disagreements were difficult to settle, often to the contractors' favour.

- **Performance deductions are not always enforced**

For instance, the Home Office did not enforce penalties for defects in COMPASS asylum seeker accommodation as it felt that the contracts were at an early stage. Also, as the contractors could pass the penalties down the supply chain, the Home Office felt enforcing penalties may have threatened subcontractors' financial stability and led to overall service failure.

- **Not understanding how contracts meet policy objectives**

Senior staff do not always understand what their contracts are achieving, which leaves departments unable to shape contracts and contractual incentives to their needs or work with contractors to get the required results. For instance, poor senior oversight meant the risk profile on the Department for Work & Pensions' Work Programme was changed in the contractors' favour.

- **Use of commercial levers**

Absent data, or limited scrutiny of performance data, means departments do not understand how a service is provided, or how to challenge poor performance. Without market testing, departments can be locked into inflexible or expensive contracts which they cannot revise to reflect innovation or learning from the outside world. Not using performance incentives means that departments do not challenge poor performance. For instance, pressures to find cost savings led HM Revenue & Customs (HMRC) to trade away some of its negotiating power and hindered its ability to get strategic value from its long-term Aspire ICT contract. When negotiating cost savings in response to successive funding settlements, HMRC conceded many of its commercial safeguards through major renegotiations of the contract between 2007 and 2009, including the right to share in supplier profits when they were higher than target and the right to compete services. HMRC estimates it achieved savings of £750 million through such negotiations. Since 2012, HMRC has negotiated some of these commercial controls back.¹⁹

Recommendations from the cross-government review

1.11 The cross-government review made 8 recommendations to improve contract management. The recommendations required action from both departments and the new central Crown Commercial Service (**Figure 4** overleaf and paragraphs 1.17 to 1.20).

The central response to the contract management reviews

Senior leadership across government

1.12 In October 2013 the Chancellor of the Exchequer asked the Head of the Civil Service and the Cabinet Secretary to chair a group, 'Markets for Government Services (Officials)' (MGS(O)).²⁰ The new group would coordinate the government response to the G4S and Serco revelations. The group comprised accounting officers from the major spending departments and senior officials from the Cabinet Office and HM Treasury. Its role has evolved:

- Between October 2013 and February 2014 MGS(O) met weekly to coordinate the government's settlements with G4S and Serco.
- Since February 2014 MGS(O) has met monthly to coordinate the government's strategic response to market supply and development; contingency planning; commercial capability; strategic supplier management; government relations with ICT suppliers; strategic planning for ICT contracts; and transparency.

¹⁹ Comptroller and Auditor General, *Managing and replacing the Aspire contract*, Session 2014-15, HC 444, National Audit Office, July 2014.

²⁰ Officially, the 'ad hoc officials committee on markets for government services', under the ministerial Cabinet sub-committee 'markets for government services'.

Figure 4
Recommendations of the cross-government review

Theme	Central action	Action for departments
1 Internal audit	Greater integration of internal audit functions between departments (as set out in the <i>Review of Financial Management in government</i>) ¹	Internal audit should improve capability so it can review major contracts
2 Commercial director's role	–	Commercial directors should have responsibility for contract management as well as procurement More senior assurance on contract changes More links between finance and commercial throughout the life of a contract
3 Leading the commercial profession	Crown Commercial Service (CCS) to focus more on leading the profession The Chief Procurement Officer should contribute to recruitment and performance management of departments' commercial capability	–
4 Contract management capability	CCS to develop its contract management capability so it can set standards and advise departments	–
5 Contract management plans and review	–	Commercial director to approve contract management plans before any new award Senior responsible owners (SROs) appointed for major contracts SROs should review, refine or develop contract management plans for all existing major contracts
6 Central support for departments	Evaluate whether to 'step in' and help departments manage major contracts	–
7 Supplier relationships	Central management of relationship with strategic government suppliers	Departments to manage other suppliers, seeking input from CCS where required
8 Implementation plans	CCS to develop detailed plans for recommendations 3 to 7	Departments to develop detailed plans for implementing recommendations by the end of February 2014

Note

1 HM Treasury, *Review of Financial Management in government*, December 2013.

Source: National Audit Office analysis of recommendations in the cross-government review

1.13 MGS(O) includes the accounting officers from all the main departments involved. Each individual accounting officer remains responsible for their own department's decisions. MGS(O)'s initiatives are not part of a programme and do not include management techniques such as an integrated plan, budget, or benefit realisation. HM Treasury or the Cabinet Office (including the new Crown Commercial Service) lead each initiative, and departments manage their own change management programmes. The Cabinet Office Board separately oversees the Crown Commercial Service.

Negotiations with G4S and Serco

1.14 The members of MGS(O) took a robust approach in negotiations with G4S and Serco. However, government was constrained in its actions and acted as if the firms were too important to fail: if either contractor walked away it would cause severe disruption to public services and would threaten government's ability to have competition across several policy areas. Furthermore, government could not terminate its £1.8 billion a year of contracts with G4S and Serco without paying significant damages and there were not well-developed contingency plans to prevent severe disruption to public services. Under EU law, government could not easily 'blacklist' the contractors and stop them from bidding for contracts. However, it could put significant political and reputational pressure on the contractors to demand the following:

- **Significant 'corporate renewal'**

Including replacing senior managers, restructuring and new governance procedures, new ethical training and greater transparency. G4S and Serco separately prepared corporate renewal programmes. HM Treasury appointed Grant Thornton to assess the sufficiency of the respective programmes and to monitor their initial implementation.

- **Financial settlement**

In total, across the contracts referred to authorities, G4S and Serco have paid the government £179.4 million.²¹ This represents the total amount overbilled plus some of the previously recognised profit and reimbursement of government costs for the investigation. The SFO and police investigations are ongoing.

²¹ Serco has paid £68.5 million relating to electronic monitoring and £2.0 million for prisoner escorting. G4S has paid £104.4 million relating to electronic monitoring and £4.5 million on court facilities management. Sums comprise rebates, interest and payment of government investigation costs. These amounts do not include VAT, which will be repaid but then reclaimed from HMRC.

Central monitoring of departments' responses to the cross-government review

1.15 In October 2013 the Cabinet Office wrote to all central government departments asking them to provide assurance on their contract management capability. The cross-government review subsequently required departments to set out plans by March 2014 for how they would improve their contract management. All departments have submitted their plans except HM Treasury, which was not asked to submit a plan as it has few operational contracts. All accepted the need for improvement. The major spending departments – the Department for Work & Pensions, the Ministry of Defence, the Home Office and the Ministry of Justice – are the most advanced in their change programmes. We have published a detailed review of the responses of the Home Office and the Ministry of Justice in our accompanying report.²² Emerging best practice in cross-organisational contract management is shown in **Figure 5**.

1.16 HM Treasury and the Cabinet Office are undertaking commercial capability reviews of all departments. This will allow central government to check progress on enhancing commercial capability, including on contract management. The first reviews have begun with the Ministry of Justice and the Home Office.

The role of the new Crown Commercial Service

1.17 In April 2014 the Cabinet Office formed the Crown Commercial Service (CCS). The CCS is now the central body to help departments buy common goods and services such as facilities management, consultancy and travel. The CCS replaces the Government Procurement Service and incorporates parts of the Cabinet Office focused on commercial policy. It aims to become government's centre of expertise for commercial issues and help departments to:

- improve their commercial skills;
- resolve complex contracting issues;
- improve data and systems for contracting;
- buy common goods and services;
- support the crown representatives²³ to manage government's strategic supplier relationships; and
- implement the recommendations of the cross-government review of contract management.

²² Comptroller and Auditor General, *Transforming contract management in the Ministry of Justice and the Home Office*, Session 2014-15, HC 268, National Audit Office, September 2014.

²³ These are senior people brought into government from industry with experience of commercial relationships. They manage the relationship with strategic suppliers for government as a whole.

Figure 5

Departments need the right support for effective contract management

The following is based on the emerging best practice from departments' current reforms. It sets out the organisational architecture necessary to support good contract management as defined by our 2008 good contract management framework.¹

Governance

Governance and accountability will be more effective if:

- the senior leadership team has clearly defined responsibilities for championing contract management across the organisation;
- a senior management forum scrutinises and challenges contract teams to continuously improve;
- senior staff manage relations with key suppliers, assisted by both commercial and operational staff;
- departments allocate contract management and oversight resources to individual contracts, based on operational risk to the organisation;
- clearly defined systems of problem escalation support senior engagement at a level that mirrors the contractor;
- internal audit skills and capacity are sufficient to give the accounting officer assurance that contract management is effective. Internal audit work on contract management is proportionate to the risk; and
- commercial directors retain control of commercial levers. For instance, penalties should always be applied unless the commercial director signs off that there is good reason not to.

Integration

Contract management will be well-integrated into the business when:

- contract management is recognised as a cross-organisational competence, supported by policy, operations, finance, legal, human resources and commercial functions;
- the contract is led by an owner within the business, who ensures the contract is aligned with service user needs. Commercial and other functions then support the contract manager and hold them to account;
- the contract management approach and resources are planned during the approval of the procurement. For example, they should be included in the business case;
- lessons from contract management are captured and fed back into policy and commissioning design; and
- contracts are reviewed periodically, so they meet business needs. Change management systems and governance reflect the likely pace of business change.

Visibility

Departments could improve their use of contract information if:

- information to manage the contract is stored in an integrated information system. This includes financial, performance, risk and project management information, information about the contract, supplier information including correspondence, and vital guidance materials;
- contract managers share contract risk management strategies within the organisation and with suppliers;
- departments review and verify performance data in a way which is commensurate with contract risk;
- cost data is used to ensure costs are competitive and that incentives are aligned to reduce costs; and
- contract data is aggregated and reported clearly to support senior management scrutiny of the contract and its risk.

Capability

Departments will have made best use of their resources when:

- contract management skills and roles are defined and understood with regular skills audits of commercial and operational staff;
- resources and expertise are allocated by risk, and the return on investment for resources deployed is understood;
- professional development for contract managers is aligned with the cross-government contract management profession, with tailored development for specific contexts where required;
- contract management staff are incentivised through objectives and performance management to continuously improve contracted services; and
- senior contract management staff can challenge senior internal and contractor staff on an equal basis.

Note

¹ National Audit Office, *Good practice contract management framework*, December 2008.

1.18 Departments have started transferring procurement staff to the CCS. The CCS expects to have some 1,050 procurement staff managing an estimated £14 billion of spend on behalf of departments by April 2018. The transfer will proceed in phases starting with 4 'trailblazer' departments: the Department for Communities and Local Government, the Department for Transport, the Ministry of Defence and the Department for Work & Pensions. The first has already transferred most of its procurement staff to the CCS.

The challenges faced by the Crown Commercial Service

1.19 The Crown Commercial Service (CCS) is a new organisation with ambitious plans to change how central government buys some £14 billion of common goods and services (35% of the estimated £40 billion spent on procurement). In November 2013 we reported the Cabinet Office's ambitions for central government may not be matched by the right resources, capability and information.²⁴ The creation of the CCS was designed to strengthen its governance over commercial issues. It is in the process of developing its own capability, and has made some progress. It:

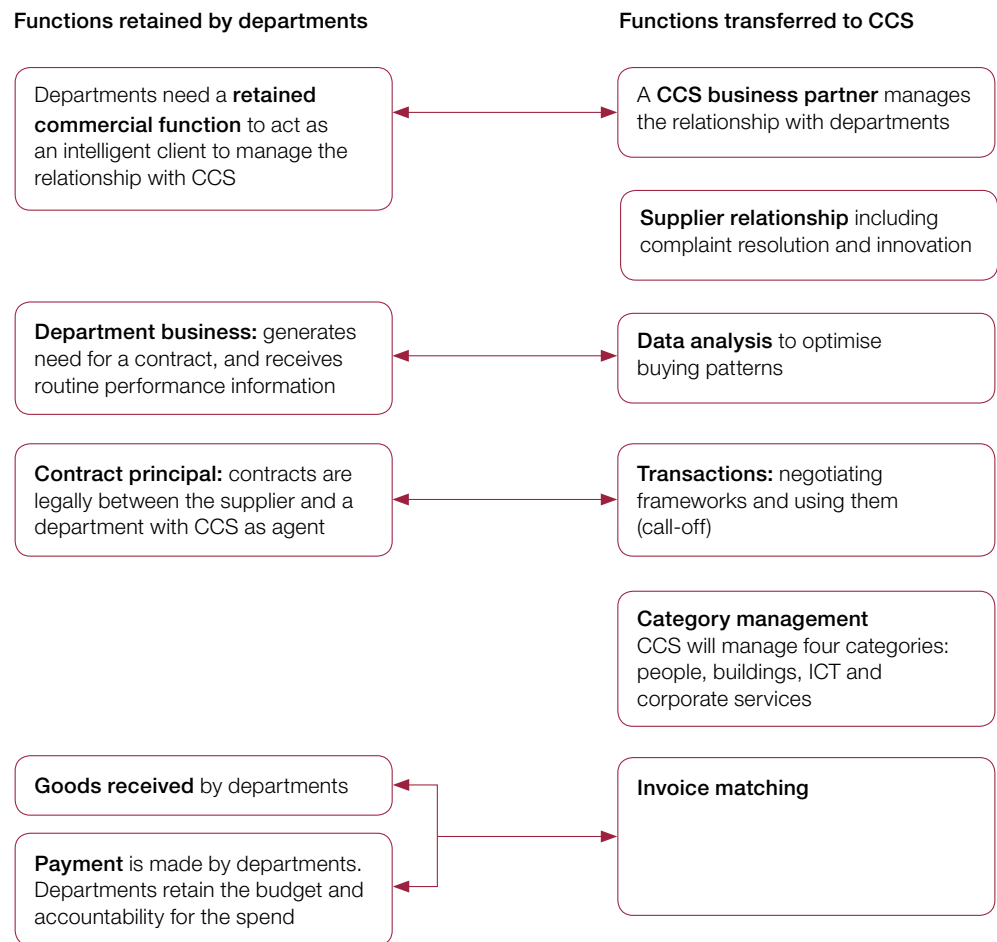
- gained HM Treasury approval for its business case in March 2014 and refreshed it again in July;
- appointed a new management team below the Accounting Officer and is seeking a new non-executive chair;
- appointed a new head of contract management, who is introducing new operating procedures for its own contract management;
- recruited new staff with 118 external recruitments; and
- started to review the way that it communicates with the commercial profession and departments.

1.20 Once common goods and services are transferred to the CCS, departments will retain responsibility for the day-to-day management of the service (**Figure 6**). There is a risk, as with all central buying functions, that the commercial function in CCS will become too remote from the end-user and day-to-day manager. Departments will thus need to 'contract manage' the CCS as a key supplier. CCS managers are keen to promote a service culture and the CCS is putting in place memorandums of understanding with each department as it transfers in. These set out mutual responsibilities, and will enable departments to influence the CCS's performance by withholding fees if the service is not delivered to the required standard. CCS has also established business partners for each department whose responsibility it is to ensure that the CCS meets departments' needs.

²⁴ Comptroller and Auditor General, *The role of major contractors in the delivery of public services*, Session 2013-14, HC 810, National Audit Office, November 2013.

Figure 6

After transferring their functions, departments will need to work with the Crown Commercial Service (CCS)



Source: National Audit Office

Part Two

The causes of contract management weakness

2.1 This part of the report sets out the growth in importance of contract management and the persistent problems government is experiencing in this area. It then sets out our commentary on the causes that underlie these problems.

Contract management has grown in importance over the last 2 decades

2.2 Since the 1990s central government has increasingly sought to involve the private sector in providing public services (**Figure 7** on pages 30 and 31). Government:

- launched the private finance initiative (PFI) in 1992;
- started to outsource administration, such as ICT, call centres and pensions administration from the mid 1990s; and
- towards the decade's end, started to contract-out services such as prisons, electronic tagging and medical assessments.

2.3 We reported on these trends in 1999. We said that contract management had become more important as contracts moved from simple fixed-price deals to more complex contracts with performance incentives, requiring tighter performance monitoring.²⁵

2.4 By 2005 there were mature contracts across many parts of government. We started to notice that some teams managed contracts particularly well, but many did not. Our 2006 report on the Ministry of Defence found that it did not share pockets of good practice routinely within the department.²⁶ Our 2007 PFI benchmarking report²⁷ and 2008 report on changing PFI contracts²⁸ found few departments used market-testing to give competitive tension to high-value changes to PFI contracts.

25 Comptroller and Auditor General, *Modernising Procurement*, Session 1998-99, HC 808, National Audit Office, October 1999.

26 Comptroller and Auditor General, *Using the contract to maximise the likelihood of successful project outcomes*, Session 2005-06, HC 1047, National Audit Office, June 2006.

27 Comptroller and Auditor General, *Benchmarking and market testing the ongoing services component of PFI projects*, Session 2006-07, HC 453, National Audit Office, June 2007.

28 Comptroller and Auditor General, *Making Changes in Operational PFI Projects*, Session 2007-08, HC 205, National Audit Office, January 2008.

Current weaknesses reflect long-standing problems

The findings of our 2008 report

2.5 The reviews commissioned by government in response to the G4S and Serco overbilling revelations found systemic weaknesses in its contract management (**Figure 8** on pages 32 and 33). Many of the findings echo issues raised in earlier NAO reports. In particular, the 2008 NAO report *Central government's management of service contracts* found that government:

- had not prioritised contract management enough;
- had allocated insufficient skills and resources;
- had not used penalties to encourage good performance;
- had weak risk management;
- had variable measures to improve contracts;
- had not widely carried out a supplier relationship management programme (less than half of organisations); and
- needed to do more to support central government organisations.

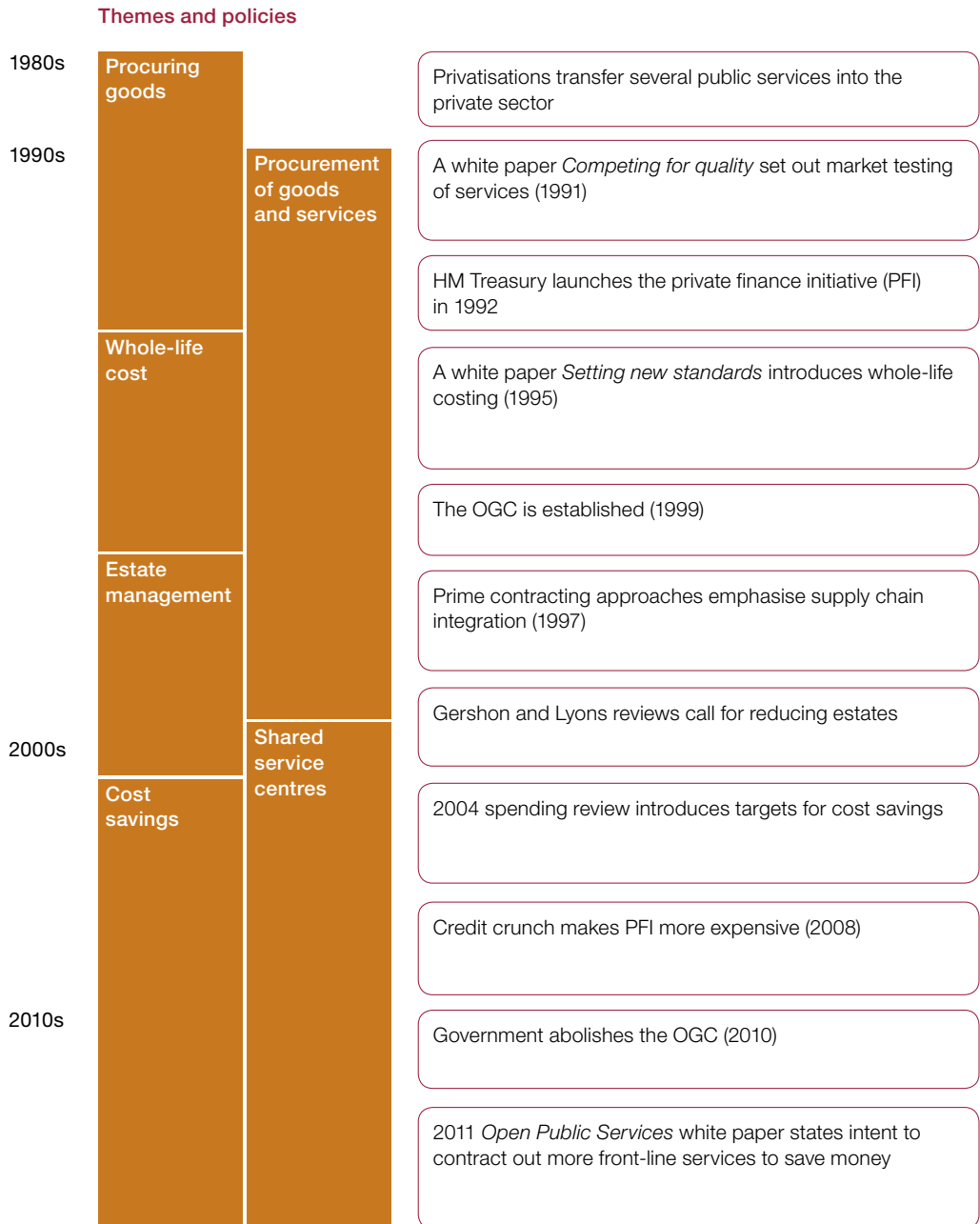
2.6 The 2009 Committee of Public Accounts report that followed made 9 recommendations to improve government contract management. The government accepted them. The Office for Government Commerce (OGC), then part of HM Treasury, set up a programme to 'build an active community that is incentivised and encouraged to build its professional capacity and capability' across central government. However, the OGC struggled to influence departments and progress in improving contract management was slow.²⁹

²⁹ For example, in *Commercial skills for complex government projects* (Session 2008-09, HC 962, November 2009), we reported that "there has been a lack of departmental engagement with some OGC initiatives".

Figure 7

Contracting out public services has increased since the 1980s

Examples of major themes in contracting 1982 to 2014



Notes

- Organisations referred to in the figure include: MOD – Ministry of Defence; OGC – Office of Government Commerce; DfT – Department for Transport; DWP – Department for Work & Pensions; HMRC – HM Revenue & Customs; DVLA – Driver and Vehicle Licensing Agency; NS&I – National Savings & Investments.
- The ASPIRE and STEPS contracts were originally let by the Inland Revenue, which is now HMRC, and the PRIME contract was originally let by the Department for Social Security, which is now the Department for Work & Pensions.

Source: National Audit Office analysis of value for money reports, 1982 to 2014

Construction and procurement

Services

ICT

The MOD had contracted out royal dockyard management since 1986 and was considering contracting maintenance of RAF equipment in 1987

Private sector consultants needed to address skills gaps in public sector ICT (such as computerisation of PAYE by the Inland Revenue in 1987)

Electricity, gas, telephony become routinely purchased from the private sector

NHS starts using independent health sector facilities (1989)

PFI rapidly used for many services including prisons (1995), hospitals (1997), roads, museums and eventually ICT

NHS centralises procurement (1991)

MOD's general policy to contract out maintenance work (1992)

Call centres begin to be contracted out in the mid 1990s

PFI is used for Contributions Agency ICT (1995)

The DfT contracts out road construction and improvement

New services contracted out from the start, including immigration centres (1995), the National Lottery (1993) and electronic monitoring (1998)

The DVLA combines privatisation with outsourcing ICT (1993)

Our 2003 report shows the growth of PFI with no prisons procured by a non-PFI route in previous 10 years

PFI used for estate and facilities management including DWP's PRIME (1997) and HMRC's STEPS (2001) contracts²

The NS&I outsources most operations via PPP (1997)

PPP is used for London Underground improvement (announced 1998)

NAO report: *Modernising procurement* (1999)

The cohort of early PFI deals begins to be refinanced

HMRC lets ASPIRE ICT contract (2004)²

NAO report: *Using the contract to maximise the likelihood of successful project outcomes* (2006)

NAO report and good practice framework: *Central government's management of service contracts* (2008)

NAO reports on contracts including health and disability assessments, Olympic security, out-of-hours GP services, court language services, asylum accommodation and electronic monitoring increased focus on contractors responsible

HM Treasury leads programme of savings on operational PFI contracts and launches a new 'PF2' approach to public private partnerships

Government mutualises MyCSP pension scheme (2013)

'Next generation' shared service centres created

Cabinet Office launches a cross-government review of contract management (2013)

Figure 8

The findings of the 2013 government reviews echo earlier work

NAO good practice areas	NAO findings (December 2008)	Committee of Public Accounts recommendations (April 2009)
Planning and governance	<p>Poorly prioritised contract management</p> <p>There was often no single individual with overall responsibility for contract management across an organisation, and no documented plan for managing individual contracts in more than a quarter of cases. Where plans did exist, supplier input was limited</p>	<p>Assign responsibility to a single individual. (Including contract governance and creation of documented contract management plans)</p>
People	<p>Insufficient skills and resources</p> <p>27% of commercial directors or heads of procurement rated the level of resources allocated to contract management as poor. Few contract managers hold any formal commercial qualification</p>	<p>Review and put in place appropriate contract management resource</p>
Administration	<p>Lack of central guidance and support</p> <p>The OGC had focused its work developing guidance and training primarily on the ICT sector, rather than on contract management more broadly</p>	
Payment and incentives	<p>Insufficient use of penalties</p> <p>Organisations did not always use the performance information they collected from suppliers. 38% of contract managers did not always invoke payment deductions when supplier performance was below the specified standard</p>	<p>Performance deductions should be enforced (except under very exceptional circumstances supported by guidance)</p>
Managing performance		<p>Performance measures should be in place, and adapted to requirements</p>
Risk	<p>Weak risk management</p> <p>37% of contracts did not have a risk register and 56% did not have contingency plans for supplier failure</p>	<p>Risk management processes and contingency plans should follow good practice, and be supported by guidance</p>
Contract development	<p>Lack of focus on improvement</p> <p>Departments were not always using benchmarking to improve value. Only 53% of contract managers had a formal plan for supplier improvement and development</p>	<p>Value for money testing at least every 3 years and for all significant changes</p>
Managing relationships	<p>Lack of supplier relationship management</p> <p>Ways in which day-to-day working relationships might be improved include defining more clearly the expected behaviours of both parties throughout the duration of the contract</p>	<p>Central guidance, including monitoring major suppliers</p>

Government review findings (2013-14)

Problems on 38 out of 73 contracts including:

- a general lack of visibility of contracting at board or executive level;
- lack of senior involvement; and
- missing or insufficient contract management plans.

Examples from the recent contract management reviews

The Home Office immigration caseworking contract had no contract management plan

Consequence

Departments lack good strategic understanding of how contracting can deliver

Problems on 40 out of 73 contracts including:

- insufficient numbers and capability of staff allocated to contract management; and
- limited knowledge of the detail of the contract among contract operations staff.

Inadequate capability contributed to the Ministry of Justice's contract management problems. The team responsible for the Electronic Monitoring contracts shrunk from 8 to 5 between 2007 and 2012. Following a bottom-up assessment of contract management requirements, staffing has now risen to 7

Departments have reduced knowledge of how their contracts work, and how services are delivered

Problems on 39 of 73 contracts including:

- weak interactions between the finance, commercial and contract management functions.

Serco and G4S had not deducted agreed amounts from invoices for the Home Office's immigration removal centres. The amount was small but larger errors may also not be detected

Departments are unable to detect or prevent overbilling

Problems on 48 of 73 contracts including:

- levels of deductions allowed by the contract insufficient to incentivise contractor performance; and
- lack of use of 'open book' clauses.

Ofsted had only one payment retention mechanism available in its inspection contract with Serco. The grounds for this financial remedy were subjective, not well linked to delivery and the potential financial penalty was small

Contracts are not used to incentivise good performance

Problems on 50 of 73 contracts including:

- over-reliance on performance data provided by suppliers; and
- key performance indicators misaligned with the intended contract objectives.

Performance on the Ministry of Defence's facilities and engineering support contract at RAF Cranwell was only assessed by subjective measures such as complaints

Departments are losing the ability to influence the quality of public services

Problems on 47 of 73 contracts including:

- lack of evidence of comprehensive risk assessment on contracted services.

The Foreign and Commonwealth Office Afghanistan security contract with G4S had no risk register and had not been signed

Departments do not understand the level of risk that they have retained

Problems on 50 of 73 contracts including:

- changes being made to contracts at an operational level in isolation from other service areas, risking unintended consequences to other contracts or to the overall strategic intent of the contract.

Changes to the Ministry of Defence's facilities management contract for the Defence Academy campus (Serco) had been agreed and put in practice, but not formally recorded as contract changes

Departments are not able to change contracts to reflect changing circumstances

Problems on 31 of 73 contracts including:

- lack of meaningful incentives to strongly encourage either the department or the supplier to innovate; and
- reluctance of departments to move away from the original contractual terms.

The service specification for the Ministry of Defence's contract with Serco for marine support services at naval bases specified services was based on old data which did not reflect changes in vessel specifications or current levels of activity

Departments are not well placed to innovate in contracted-out services

Further problems reported since 2010

2.7 In 2010 the OGC transferred into the Cabinet Office's Efficiency and Reform Group. The government began to prioritise savings by using its combined buying power more, and engaging with contractors as a single customer to get a better deal. It deprioritised building departments' individual contract management capability. Many of these issues raised in our 2008 report have recurred in our work on contract management undertaken since 2010. For instance we have recently reported that:

- **Department for Work & Pensions (Universal Credit)**
The DWP had inadequate financial control over supplier spending on Universal Credit. This includes not fully understanding how spending related to progress, poorly managed and documented financial governance, and insufficient review of contractor performance.³⁰
- **Home Office (COMPASS asylum accommodation)**
Although they had been operating for almost 1 year, unresolved issues during transition continued to affect provider performance once the contracts began.³¹ Since then contract compliance and assurance teams are working with operational managers to support performance management. The Home Office reports that issues relating to the key performance indicator regime have been resolved and that property standards are now meeting contractual requirements.
- **Department for Work & Pensions (Work Programme)**
Flawed contractual performance measures meant the DWP could have had to make incentive payments to even the worst-performing contractors on the Work Programme. In 2014-15 all 40 contracts could have been entitled to £31 million in incentive payments but the DWP estimated that only £6 million would be payable using a more accurate performance measure.³² The DWP is now preparing to renegotiate the contracts and expects to improve the link between incentive payments and performance.
- **HM Revenue & Customs (Aspire ICT)**
The Department was overly dependent on the technical capability of the Aspire suppliers between 2004 and 2012, which limited its ability to manage the contract commercially.³³
- **Department of Health (PFI hospitals)**
Some trusts had not devoted sufficient resources to contract management; for example, 9 of the 76 PFI contracts had no one assigned to contract management.³⁴

30 Comptroller and Auditor General, *Universal Credit: early progress*, Session 2013-14, HC 621, National Audit Office, September 2013.

31 Comptroller and Auditor General, *COMPASS contracts for the provision of accommodation for asylum seekers*, Session 2013-14, HC 880, National Audit Office, January 2014.

32 Comptroller and Auditor General, *The Work Programme*, Session 2014-15, HC 266, National Audit Office, July 2014.

33 Comptroller and Auditor General, *Managing and replacing the Aspire contract*, Session 2014-15, HC 444, National Audit Office, July 2014.

34 Comptroller and Auditor General, *The performance and management of hospital PFI contracts*, Session 2010-11, HC 68, National Audit Office, June 2010.

NAO commentary on the causes of poor contract management

2.8 The problems with contract management go beyond lapses in administration and understanding. The problems are rooted in a civil service culture that does not understand the value of contract management, and which has hindered previous attempts to disseminate and implement best practice. Reform of contract management will therefore need to go beyond a tightening of controls. It is difficult to generalise across 17 government departments, but from our collective experience of auditing government contracting we have identified 4 key causes of poor contract management that need to be addressed.

The value of contract management is not understood

2.9 Government officials appear too often to have seen contract management as enforcing the deal that was made when the contract was agreed. Under this procurement model of contracting, commercial functions have seen themselves as adding value through effective procurements that drive down price, mitigate the risk of legal challenge or dispute during the contract life and negotiate economic changes.

2.10 The procurement model of contracting does not work for anything other than the most basic services. It is not possible to fully specify more complex services. Ensuring services have been provided to the appropriate standard requires expert judgement and continually using commercial influence to manage the service. For longer-term contracts, the government needs flexibility to ensure that services continue to meet changing business requirements.

2.11 Government needs to recognise that value is achieved over the life of the contract. Good contract management requires a multi-disciplinary approach, owned by the business. All those responsible for the contracted-out service must use commercial influence to bring about improvements in the service and cost reductions. This includes using contractual incentives, damages, threats to reputation, promises of future opportunities and withholding consent to any key approvals required. Good management also requires effective relationship management and understanding the service that is meant to be provided. Done well, a department has considerable influence over the contractor even after the initial competition is concluded. Contract management then becomes a vital part of how an organisation meets its objectives.

Managers have not adopted a commissioning role

2.12 The government is trying to reform the civil service to make it smaller and more strategic.³⁵ Successive governments have pursued the idea of splitting the roles of commissioner and provider, and aspired to bring private and third sector providers into public service markets.³⁶ This process has started to shift departments' roles from directly providing services to managing other providers.

2.13 However, departments' senior managers and governance processes have been slow to adapt. Senior management have not taken contract management seriously. Too often, departments' structures and systems are set up as if their responsibility stops at contract signature. Governance systems have usually comprised investment boards and business case approval processes that have focused on approving spending decisions and awarding contracts. Senior engagement has not generally been maintained during the operational phase. Contract managers have often worked at more junior levels than managers of directly provided services. Senior ownership of contracts, and who is allowed to make decisions, has often been unclear.

2.14 As a result, senior managers have often intervened only to react to problems and disputes with contractors. They have not given scrutiny and challenge to their own teams and contractors, to encourage continuous service improvement and value for money.

Senior managers have poor visibility of contracts

2.15 Senior management's lack of engagement has meant they have not demanded robust information. We do not often see the contract summaries and manuals that would allow senior managers to understand their contracts. Departments do not have ways to aggregate cost, risk and performance data, so senior managers can scrutinise their portfolio of contracts.

2.16 The lack of senior demand for information has negatively affected data quality at a working level. Departments do not have integrated systems to manage their contracts. This means they do not capture all the contract changes and communications with the contractor, leaving them exposed if there is a dispute. The contractor is often best placed to produce performance data. However, instances of data manipulation have shown that departments need to validate and verify this information.³⁷ Departments do not use open-book accounting often enough. This means they do not know if they are getting value for money, and cannot refine incentives or identify areas to cut unnecessary expenditure.

³⁵ HM Government, *The Civil Service Reform Plan*, June 2012, available at: www.gov.uk/government/organisations/civil-service-reform

³⁶ HM Government, *Open Public Services*, white paper, Cm 8145, July 2011, available at: www.gov.uk/government/organisations/open-public-services

³⁷ Comptroller and Auditor General, *The Ministry of Justice's electronic monitoring contracts*, Session 2014-15, HC 737, National Audit Office, November 2013; *Memorandum on the provision of the out-of-hours GP service in Cornwall*, Session 2012-13, HC 1016, National Audit Office, March 2013.

Government is at a permanent disadvantage on commercial capability

2.17 Because departments do not see contract management as a way to enhance services and make efficiency savings, they have no way to measure its value. This has made it hard to make the business case to invest in contract management teams, training and skills. Contract management teams have seen cuts in recent years and funding for administration is likely to be further reduced in the next parliament.

2.18 Procurement has been seen as a low-status profession in the civil service. It has few senior positions and most procurement professionals do not work with ministers and senior management. There have not been the career paths to ensure those working on commercial issues have the experience necessary. The result has been a clear divide between those trained-up through the civil service and those brought in from outside. Relatively few within the civil service have the ability to negotiate with contractors on an equal basis.

2.19 This low status has meant the commercial profession has not been well placed to disseminate best practice across government. Business owners of contracted-out services have often only looked to the commercial profession for advice on navigating EU procurement rules, tendering protocols and major renegotiations of contracts. They have not worked with them to get best value from the contract when the services are in operation.

2.20 There have been many attempts in the past to improve the commercial capability of government. These have included investment in professional qualifications, bringing in outside experts and rolling out commercial awareness training. These will continue and have an important part to play in improving the management of contracts.

2.21 But the reality is that government is unlikely to ever have the commercial capability of its contractors. It does not pay the same overall amount as the contractors at a senior level. It cannot provide the same incentives to focus on value for money as contractors will provide to increase profit. It does not offer the same hope of advancement to the most senior positions as offered by business. And it does not provide the same breadth of experience across both public and private contracts. Instead of trying to match contractors on their commercial capability, it needs to find ways of deploying its scarce capability to where most required, while making the management of its other contracts easier.

Part Three

Transforming contract management

3.1 In the previous part we set out the need to address the systemic problems with government's contract management. This part sets out what can be done, building on government's current actions. We organise this into 3 areas of improvement:

- **Enabling a commissioning approach**
Establishing the governance, information systems and structures to enable senior management to scrutinise, challenge and manage delivery by others.
- **Understanding and influencing suppliers**
Placing responsibility for delivery with contractors, ensuring they have the appropriate control systems in place, and using transparency, assurance and incentives to align their interests with the taxpayer.
- **Making the most of commercial capability**
Deploying commercial expertise as a scarce resource, strengthening career paths and training and making effective use of information to target activity.

Enabling a commissioning approach

Governance

3.2 The civil service culture needs to change so that senior officials take contract management more seriously. Like most programmes aimed at starting a cultural change, government is starting with its governance structures, roles and responsibilities. Departments need to establish systems of governance and oversight that enable senior officials to manage contracted-out services before problems arise. This includes clear ownership of contracts, processes of issues escalation, and senior challenge and scrutiny of contract management teams and contractors.

3.3 There are 5 levels at which departments need to govern contract management. Individuals' accountabilities and authority to make decisions need to be clear at each level. Departments and the Cabinet Office are improving governance at all 5 levels (**Figure 9** overleaf):

- **Day-to-day contract management**

Departments are reviewing their contract management processes to improve governance. The Department for Work & Pensions (DWP) commissioned an external review to identify good practice in its contract management and improve consistency. The Ministry of Defence has commissioned reviews of contract management in contracts not covered by the cross-government review.

- **Senior responsible owners**

Departments have recognised they must assign every major contract a senior responsible owner (SRO). The Department of Health is reviewing its data to make sure ownership information is up to date. It is also strengthening its guidance for SROs.

- **Escalation routes**

There need to be ways of those managing the contract day-to-day to escalate issues to SROs. There has sometimes been too wide a gap between an SRO and the day-to-day manager, meaning that issues are not escalated. The DWP is improving escalation routes by ensuring that all contracts have SROs within the most suitable procurement categories. For example, all facilities management contracts' SROs will report to the head of estates.

- **Strategic oversight**

Commercial directors will be made responsible for contract management as well as procurement. Many departments are also strengthening senior groups responsible for strategic oversight. For example, the Ministry of Justice has established a new commercial and contract governance committee, which has a wider remit and greater seniority than its previous procurement board. Departments are also starting forums to share lessons at working-level with other departments that share common contractors and sometimes have shared the results with crown representatives.

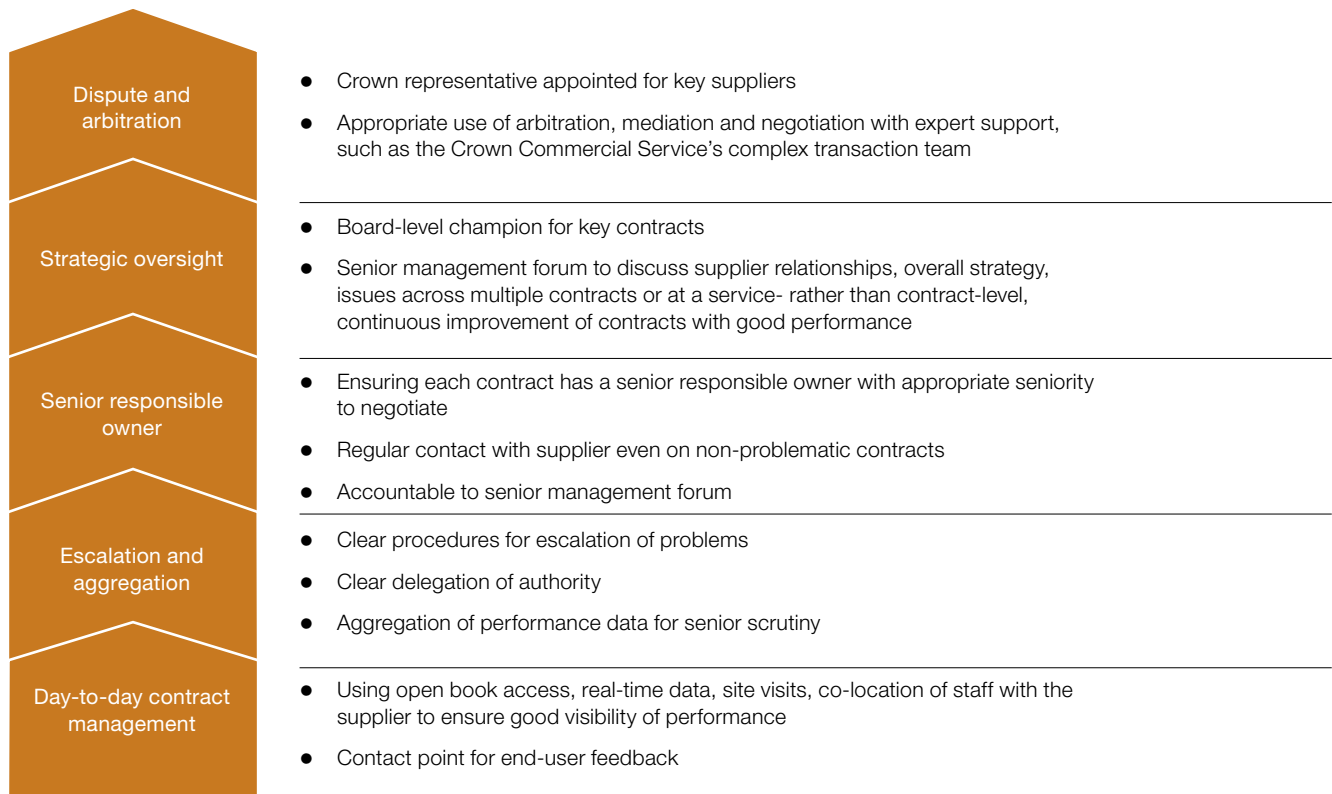
- **Dispute resolution and arbitration**

The Crown Commercial Service (CCS) complex transactions team has started to provide central support to departments with contractual disputes. The team supports departments, at their request, with contractual disputes and complex contract issues. For instance, it recently supported the DWP to close Atos's medical assessment contract for the Employment Support Allowance.

3.4 Departments are generally taking a risk-based approach to governance and so less attention has been given to smaller, less risky contracts. Departments will need to ensure that improved governance is rolled out to these proportionately.

Figure 9
Five levels of governance over contract management

Features of good governance



Source: National Audit Office

Government needs to improve its contract management data

3.5 Basic record keeping and data analytics are essential to contract management. Yet departments lack integrated systems to manage their contracts. We typically find contract management information is spread across disparate systems such as electronic filing, email and sometimes even paper-based systems. Government needs information systems that combine the needs of finance (paying contractors), procurement (planning for and conducting bidding) and contract management (understanding performance, costs, the commercial position and the agreed contract). In particular, government needs systems that help it with 3 challenges:

- **Ensuring they have an up-to-date agreed contract**

This should include all changes and communications with the contractor. It should also include contract management plans, manuals and guides so that people new to the contract can readily understand it.

- **Aggregation of information**

Senior management need to be able to scrutinise and challenge costs and performance on contracts across their portfolio, before issues arise.

- **Comparability across contracts**

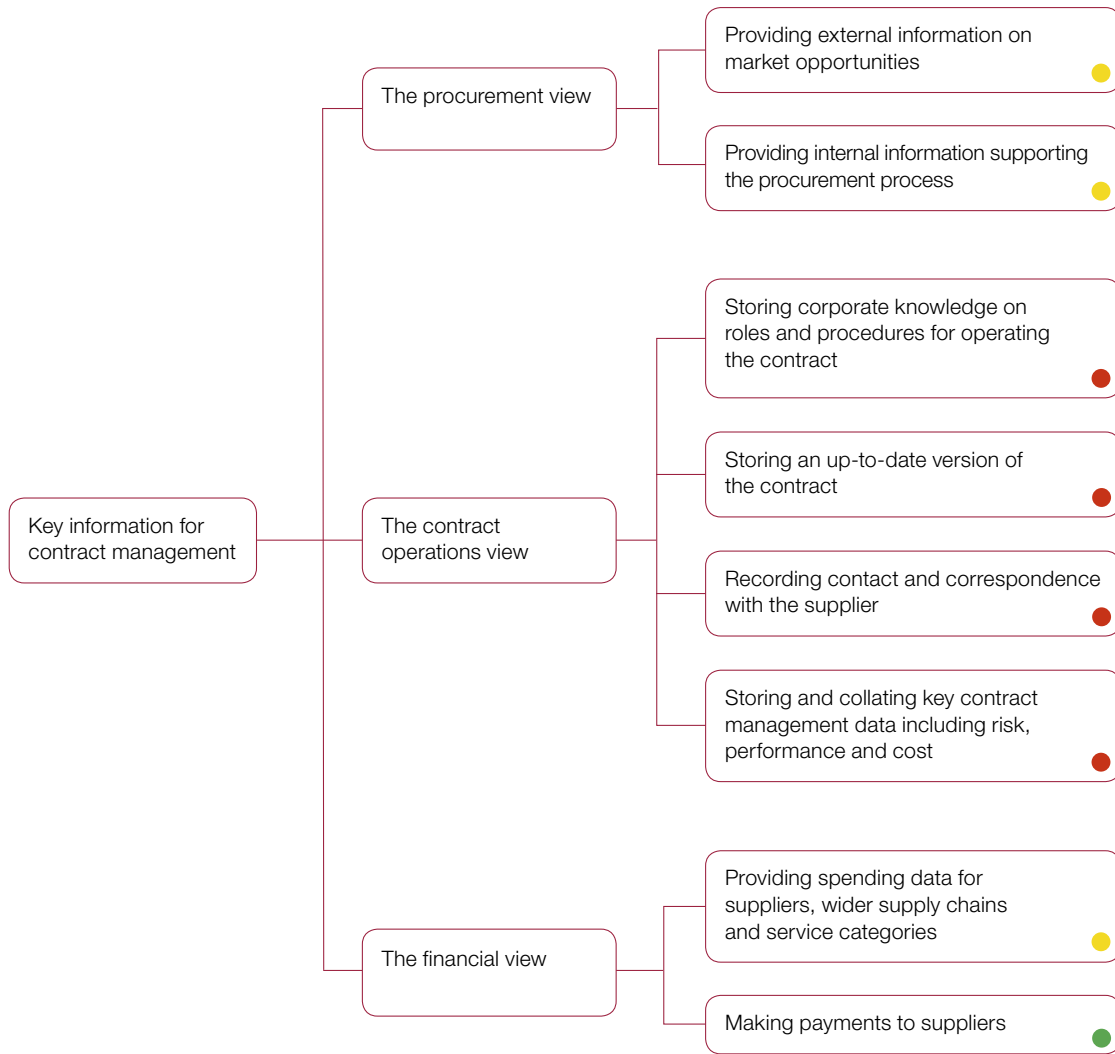
Contract management would be significantly enhanced if information was maintained in a common format to allow the use of data analytics and milestone alerts at a portfolio level. This would allow cost benchmarking and costing of commercial terms and conditions.

3.6 Government is slowly moving towards using digital information to manage its contracts (**Figure 10** overleaf). The centre has a number of ongoing initiatives:

- The Crown Commercial Service (CCS) is developing a common data standard.
- Financial information on spending is generally available through the online spending analysis tool. The quality of this information is improving over time.
- The CCS intends to improve central procurement information through a new version of its Contract Finder website, which it plans to launch by October 2014.³⁸ The current version includes some data on central government's largest contracts at the point they are signed, as well as forthcoming competitions.
- The CCS has made less progress in capturing operational information such as performance data, contractual changes and correspondence with contractors. It has an ambition to create a system for managing the spending under its control. However, its aim to do this by December 2014 is ambitious and we have yet to see developed plans.

Figure 10

Progress towards an integrated system of information for contract management



- System integrated into normal business
- Work under way to strengthen this across much of government
- Some departments are experimenting with this

Source: National Audit Office

3.7 Departments are beginning to improve their aggregation of data. For example, the Ministry of Justice is introducing balanced scorecards for contracts. The Department of Health will require senior responsible owners to indicate contract performance in a way that can be captured and reviewed centrally then reported to senior managers. The Driver and Vehicle Licensing Agency already aggregates risks from its top 10 contracts into a commercial service risk register.

3.8 Some departments are also procuring their own information systems. The Ministry of Defence is commissioning a new business information system, intended to bring together financial and operational information. The Ministry of Justice intends to procure a new system, but is waiting for advice from the Cabinet Office. However, other departments are only now improving basic information. The Department of Health has recently consolidated locally held contract registers, often in the form of simple spreadsheets, into a single, centralised corporate contracts register.

Integrated business structures

3.9 Contracts should be owned by someone able to represent the end user. This person will not normally be within the commercial function. That person then needs to be supported by a multidisciplinary team of commercial, financial, legal and policy professionals. The commercial specialists should support them on how to use commercial influence to manage the contract, improve the service and reduce costs.

3.10 There is a tension between creating teams that integrate commercial staff to provide consistent support through the life of contracts, and accessing specialist support at key stages of the life cycle. Departments are going about this in different ways:

- **Ministry of Justice**

The Ministry will create a single team to manage a contract over its life. The team will have an operational contract manager, a commercial contract manager, and other disciplines will support it, such as performance analysts, finance, legal and human resources.

- **Home Office**

The Home Office has reorganised its centralised commercial capability to develop expert centres for different stages in the contract life cycle. It will allocate a single commercial professional to give end-to-end support to the operational contract manager. As the contract progresses, the commercial partner will report to and be advised by senior commercial staff in different centres of expertise.

- **Department for Work & Pensions**

The DWP will manage different categories of contracts together. It is centralising its commercial staff under several senior category leads in areas such as ICT, welfare to work and health assessments. Category leads will oversee end-to-end commercial support through the full service life cycle.

Integration across the commissioning lifecycle

3.11 Contract management is an essential part of the commissioning cycle (**Figure 11**). Greater planning and consideration of contract management is needed in other parts of the cycle:

- **Designing policy**

Departments should consider their contract management capability when designing their policies and contractual approaches.

- **Generating solutions**

HM Treasury's guidance on the 5 case model already requires contract management to be considered as part of the business case for a project, but this is rarely prioritised.

- **Mobilising contract management**

The cross-government review found a lack of continuity and limited transfer of knowledge from the pre-contract phase to operational contract management in 5 recent contracts.

- **Evaluating projects that have finished**

Departments rarely collate data to enable an evaluation of the best contractual models and techniques. For instance, this has meant that government has not been able to verify whether PFI has achieved value for money compared to conventional financing.³⁹

3.12 Government is now beginning to recognise the importance of considering contract management earlier. The Cabinet Office has updated its standard operating procedures for procurement to include the mobilisation of contract management.⁴⁰

Understanding and influencing suppliers

Building intelligence on strategic suppliers

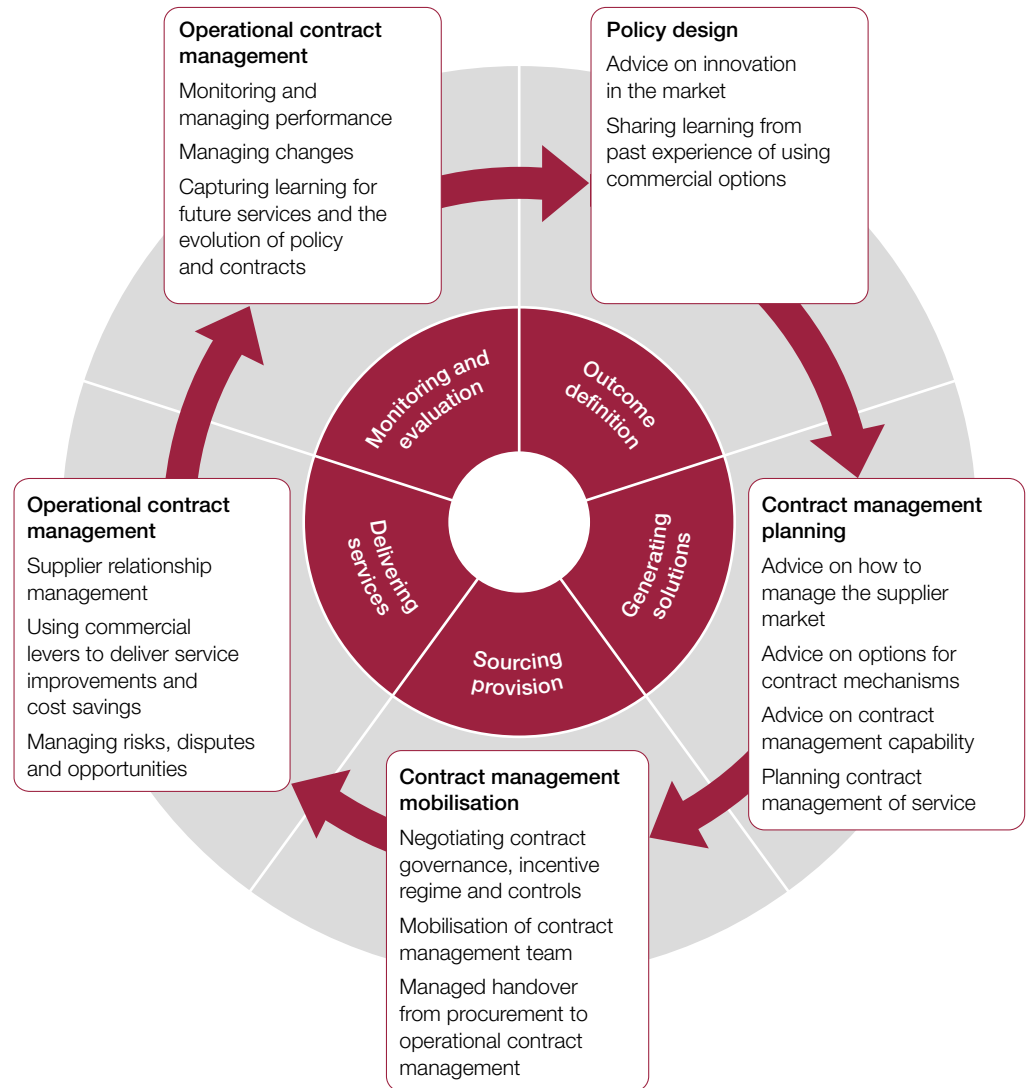
3.13 Government's influence is strongest in markets such as prisons and defence where it is the only buyer. However, many of these markets are dominated by a small number of large suppliers. The experience of dealing with G4S and Serco shows that such suppliers can become too important to fail. Government is exploring ways to reduce its reliance on such dominant suppliers. For example, the electronic monitoring contract has now been retendered using the 'Strategic Integrator and Towers Model' advocated by the Cabinet Office. This allows smaller companies to bid. We intend to report on how government manages its markets for government services later in the year.

³⁹ National Audit Office, *Briefing for the House of Commons Treasury Select Committee: Review of the VFM assessment process for PFI*, October 2013.

⁴⁰ Standard Operating Procedures are published on the Crown Commercial Service website, available at: <https://ccs.cabinetoffice.gov.uk>

Figure 11

Contract management and the commissioning cycle



Source: National Audit Office

3.14 Meanwhile, government needs to be able to rely on its strategic suppliers to behave in the taxpayers' interest. Government thus needs to be much more inquisitive about the internal operations and culture of such companies. It can then use this information to influence them and to set clear expectations. It should know the company's:

- **Leadership**

What are the leaders' espoused values? What do they pay attention to within the business? How do they focus on the government's (their customer's) needs?

- **Business model and strategy**

How does the company make its money? How much profit does it make through new contracts or generating additional revenues on existing contracts? Is it dependent on growth or making a steady return? Is it aiming to expand into new markets? What opportunities is it after?

- **Acquisition policy**

How and why is it acquiring smaller companies? How does it manage the integration of new businesses into the group? Does its growth mean that its control environment is overly stretched and reliance cannot be placed on management?

- **Control environment**

How does accountability work within the organisation? How do senior executives know that operations are working? How do they know what is going on across their diversified business?

- **Promotions policy and staff incentives**

How are managers incentivised? Is a focus on government's (their customer's) needs rewarded? Is misbehaviour punished?

- **Staff engagement and productivity**

How motivated are staff? How focused are they on what they do? Do they see the company as a good place to work?

- **Internal audit and whistleblowing policies**

How do senior management know that corporate policies are implemented? How do they learn of problems? Are these shared with the government as customer? Are staff encouraged to raise issues?

3.15 Government has started to build its understanding and strengthen influence in its relationships with suppliers. In our 2013 report *Managing government suppliers*⁴¹ we outlined the benefits of the Cabinet Office crown representatives who were appointed to manage the relationship with 40 strategic suppliers across government. The crown representatives are now supported by the CCS, which coordinates and maintains intelligence on some of these strategic suppliers. However, the information collated by the CCS is only a fraction of the intelligence we believe should be brought to bear in such relationships.

3.16 Some individual departments are also improving management of key suppliers. The Ministry of Defence has 13 strategic suppliers (reduced from 31 due to resource constraints) where relationships are overseen by board-level sponsors. The Ministry plans to appoint a commercial contracting officer who will lead major supplier management across the organisation. The DWP has had an established strategic supplier approach in its Welfare to Work division, which it is currently spreading to its ICT division.

Increasing transparency and assurance

3.17 Government must create a situation where it can rely on contractors to deliver, even when it is not deploying its best contract managers to oversee them. This requires the contractor to take greater responsibility for the accuracy of the data it supplies, and for providing a control environment which will maintain ethical behaviour and public service standards. We believe government should get written representation from contractors on the integrity of the services they supply. Senior managers would sign statements which, while not necessarily carrying additional legal implications, would have symbolic and reputational importance, and give Parliament clear accountability.

3.18 Ensuring contractors live up this responsibility requires better transparency and assurance to ensure controls are working. The cross-government review highlighted the extent of reliance on supplier performance data, while our work on the NHS out-of-hours GP services in Cornwall showed how performance data can be manipulated.⁴²

41 Comptroller and Auditor General, *Managing government suppliers*, Session 2013-14, HC 811, National Audit Office, November 2013.

42 Comptroller and Auditor General, *Memorandum on the provision of the out-of-hours GP service in Cornwall*, Session 2012-13, HC 1016, National Audit Office, September 2013.

3.19 There is a growing consensus about the need to improve transparency over government contracting. The Committee of Public Accounts report of March 2014, the Confederation of British Industry (CBI) and the government have all called for improved transparency. The Cabinet Office and the CBI have started discussions about what this means in practice.⁴³ However, government has not set a vision for how control, transparency and assurance will be integrated as a system. The Cabinet Office has said that this is the responsibility of departments,⁴⁴ while we view it as a central responsibility. A stronger system (**Figure 12**) would require:

- **Monitoring and control**
The means to understand and manage contractor performance and value for money. Government should set clear standards and objectives for its contractors.
- **Transparency**
The ability to see through the contractor's organisation, performance and costs; and the knowledge that others can raise issues on your behalf.
- **Assurance**
Reason to be confident of the supplier's controls; and know that services provided meet the required standards.

3.20 Meanwhile, departments are to improve assurance on contractor data:

- **Strengthening internal audit**
The cross-government review recommended increasing internal audit focus on contract management and several departments have started to do so. For example, the Ministry of Justice will increase its contract management work from 3% to 15% of the total. Eight departments share a cross-departmental internal audit service, which plans to spend nearly 10% of its audit time on commercial issues in 2014-15.
- **Some departments are requiring contractors to provide assurance**
The Department for Work & Pensions will require major contractors to commission external reviews to give independent assurance on performance and on the control environment of the contractor. Government also needs to require transparency to the public. Although it is improving its Contracts Finder database (paragraph 3.6), this only covers contracts at the point they are signed. It does not include performance information or subsequent changes to contract terms.

43 Available at: www.gov.uk/government/news/government-and-cbi-meet-with-industry-to-discuss-improvements-in-contracting-for-public-services, 2 May 2014.

44 HM Treasury, *Treasury Minutes: government responses on reports from the Committee of Public Accounts*, Cm 8871, June 2014.

Figure 12

A model of an integrated system of control, transparency and assurance



Aligning incentives

3.21 Contractors need to make a profit. But government needs to know that these profits are made in ways that align with the taxpayers' interests. Contractors' profits should vary with the risk taken on, the level of innovation the contractor provides and, crucially, performance. Excessive profits can undermine public confidence and contractors should not be able to make a profit by acting against their customer's (the government's) interest. Expectations about profit levels and how they will vary by performance should be agreed in competition when the contract is let. Retrospective negotiations may be less likely to get a good deal for the taxpayer.

3.22 As with transparency, there is now broad consensus that open-book clauses should be used more, but little guidance on how to do so. The Cabinet Office has developed a new model contract⁴⁵ which includes open-book clauses and audit rights, and contractors are generally amenable to providing the data. Pockets of government such as the Ministry of Defence have particular experience in this area, which may help shape future guidance and approaches. The Cabinet Office and the Confederation of British Industry are piloting ways to implement greater use of open-book clauses.

3.23 Our recent work on both the Work Programme⁴⁶ and Aspire⁴⁷ contracts have shown how open-book can be used to see the contractors' incentives. In our view, an open-book approach should have 3 purposes:

- To build trust and confidence in the relationship.
- To provide assurance that incentives are aligned.
- To identify areas for cost savings.

3.24 Government needs to support an open-book approach with means to enforce the alignment of incentives. These include gain-share mechanisms, claw-back of excess profits and post-contract reviews to ensure profits are in alignment with the original intention. Common data standards within and across contracts would allow government to compare costs and margins across suppliers using analytical techniques.

3.25 Government also needs to ensure that it gets what it pays for. This means stricter use of incentive penalties when performance is not up to standard. It also means use of liquidated damages, with the amount agreed during the initial competition, for any substantial failure.

3.26 Government and contractors can then work together to identify cost savings.

⁴⁵ *Model Services Contract*, available at: <https://ccs.cabinetoffice.gov.uk/about-government-procurement-service/contracting-value-model-services-contract>

⁴⁶ Comptroller and Auditor General, *The Work Programme*, Session 2014-15, HC 266, National Audit Office, July 2014.

⁴⁷ Comptroller and Auditor General, *Managing and replacing the Aspire contract*, Session 2014-15, HC 444, National Audit Office, July 2014.

Capability

Enhancing the role of commercial staff

3.27 The role of commercial staff needs to change. The procurement model whereby commercial staff add value through running effective bidding processes and then ensuring the contractors meet the expectations in that contract does not work for more complex services. Instead, commercial staff need to focus on improving the quality of services and reducing costs over the life of the contract. This starts at the scoping stage.

3.28 Changing the role of commercial staff is also likely to have other advantages. It will make the job more interesting, improving staff engagement. It will make the role more influential, attracting a higher calibre of staff. And it will expose staff to more commercial situations, allowing them to develop the experience they need and be promoted to more senior positions.

3.29 Government recognises that it needs to deploy its staff in a different way. The Cabinet Office believes commercial capability is too focused on the bidding stage and should be redeployed on planning and contract management (**Figure 13** overleaf). They also believe this would align deployment closer to the private sector. For example, the Defence Equipment and Support organisation estimates that under 10% of its commercial staff are involved in contract management, well below the 50% it believes is required. The Department of Health has redeployed some commercial staff to focus purely on contract management support.

3.30 Planning on how to redeploy staff is at an early stage. Departments are currently considering:

- **The size of their resource gap**

It is not clear how many commercial specialists government needs. The reviews identified a gap between the numbers and capability of staff allocated to contracts and the level needed. Government is currently researching best practice, based on evidence from across industry, in order to determine the scale and nature of resources that are needed to successfully manage contracts.

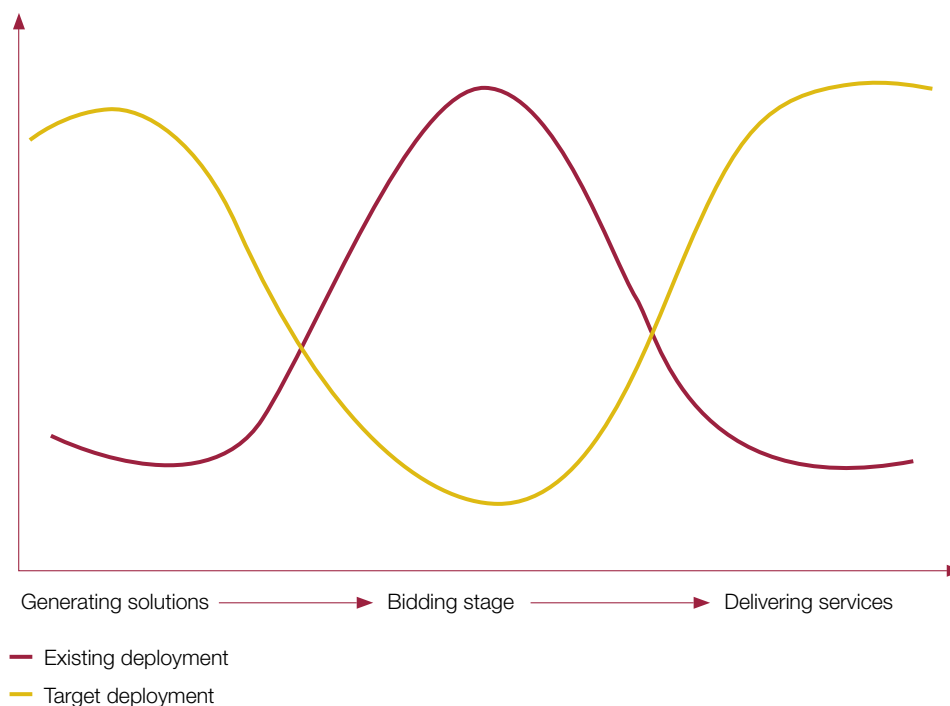
- **The skills that they need**

It is not clear that the current commercial workforce has the skills needed for the new role. The Cabinet Office and departments are working out the skills that they have and that they need. The Cabinet Office has begun to create a central database of commercial skills. While preliminary indications suggest a large skills gap may exist, work is still at an early stage.

Figure 13

Cabinet Office believes that government's commercial capability has been too focused on the bidding stage

Deployment of commercial capability



Note

1 Scales are impressionistic.

Source: Cabinet Office

Guidance and support from the centre

3.31 Government has a permanent disadvantage in its commercial capability compared with its contractors. It therefore needs to ensure that it uses the people that it does have to best advantage. Previous experience has shown the benefit of central centres of expertise. They can provide guidance and support to other teams, and deploy people for the most complex negotiations.⁴⁸

48 For instance, Partnerships UK was important to the successful implementation of PFI projects. Local Partnerships provides support to local government commercial projects.

3.32 The Cabinet Office is building up central resources to provide support to departments. The Crown Commercial Service's (CCS) complex transactions team (paragraph 3.3) consists of around 20 experts with skills in finance, law, engineering and ICT, all with significant experience of working on commercial issues. The CCS also supports crown representatives to provide help with negotiations with strategic suppliers. Infrastructure UK, part of HM Treasury, provides support for private finance projects.

3.33 The CCS's development of standard data on contract management (paragraph 3.6) could also help it to deploy specialist commercial staff with particular experience more effectively. It could use this information to identify patterns across an individual contractor's portfolio. It could also use it to monitor milestones and plan the deployment of its resources.

3.34 The CCS is starting to provide greater guidance to departments. It has published a standard contract for digital services and business process outsourcing. It has also updated its standard operating procedures to include lean sourcing.⁴⁹ This is starting to fill the void in central guidance since the Office for Government Commerce's guidance was abolished.

3.35 Departments will always need to retain a significant amount of capability to manage their own contracts and provide oversight and scrutiny of their portfolios. Some departments are working to improve their guidance and support for contract managers. For example:

- The Department of Health has created a senior responsible officer checklist for its contract managers and has started to promote contract management in events aimed at its procurement network.
- The Home Office has revised its commercial manual and collated new guidance on an updated intranet page for the commercial directorate.
- The Ministry of Justice has hosted commercial awareness events for senior civil service staff.

Professional development of commercial staff

3.36 Government can do better at developing the staff that it does have. There needs to be a clear career path to attract skills into the civil service, and a way to develop staff and give staff experience of managing contracts. This requires coordination to be taken by the centre of government to support a more vibrant commercial profession.

⁴⁹ Available at: ccs.cabinetoffice.gov.uk/about-government-procurement-service/lean-capability/lean-sourcing/lean-sourcing-standard-solution

3.37 The government has recognised that improving commercial skills is a priority. *The Civil Service Reform Plan*⁵⁰ and its supporting capabilities plan⁵¹ set out an ambition to “transform the civil service into a high-skilled, high-performance organisation that’s less bureaucratic and more focused on delivering results” with commercial skills and behaviours forming 1 of 4 priority areas. CCS has started several initiatives to improve commercial recruitment, training and development:

- **Helping departments recruit commercial staff**

In 2014 CCS ran a recruitment campaign for 77 commercial roles for departments and the CCS. Previously, every department ran its own campaign, potentially competing for the same skills. Of 988 applicants for senior roles, some 34 were in post or under offer by 15 July 2014. CCS will use this system to appoint new commercial directors at the Home Office, Department of Health and HM Revenue & Customs.

- **Civil service commercial fast stream**

A ‘commercial fast stream’ will recruit graduates to commercial roles from 2014. Participants will gain experience of commercial work in departments, CCS, an allied role such as finance, and outside the civil service. This builds on, for example, the graduate commercial training programme in the Ministry of Defence.

- **Recruiting from new sources**

School leavers will be recruited as apprentices directly into commercial roles across government from September 2015. Apprentices will train for professional qualifications and receive work experience over a 2-year programme. CCS is also creating internships with 7 universities and working with the CBI to create industry placements for people from the private sector.

- **Framework for commercial skills**

The framework allows commercial staff to be rated at 3 levels across 16 competencies covering pre-procurement, procurement and contract management. CCS is developing a tool to assess its procurement staff against the framework using multiple-choice exams. Staff will gain ‘passports’ to show their experience, with set criteria needed to enter the senior civil service. It also plans to introduce a talent management and development plan for high-potential staff.

- **Better commercial training**

This will include existing eTraining on EU procurement law, new commercial masterclasses provided by Civil Service Learning and the Commissioning Academy. The new courses will align with the skills framework. By March 2014 some 9,500 staff had completed eLearning on commercial awareness, and 1,400 attended the masterclasses.

50 HM Government, *The Civil Service Reform Plan*, June 2012, available at: www.gov.uk/government/organisations/civil-service-reform

51 HM Government, *Civil Service Capabilities Plan*, April 2013 (and updated June 2014), available at: www.gov.uk/government/news/capabilities-plan-for-the-civil-service

Appendix One

Our audit approach

1 We examined the government's response to the reviews of its contract management in late 2013. We considered:

- issues that occurred on government contracts;
- departments' responses to the Cabinet Office's 2013 review; and
- the centre's actions to coordinate the response and build capability across central government.

2 Our audit approach is summarised in **Figure 14** overleaf, and our evidence base is described in Appendix Two.

Figure 14

Our audit approach

The objective of government

Following revelations of G4S and Serco's overbilling, and weaknesses in contract management procedures in a December 2013 review, the government is starting a large change programme to improve how it manages its contracts.

How this will be achieved

The Cabinet Office has asked departments to show how they will improve their contract management. The Cabinet Office has set up a new entity, the Crown Commercial Service, to be the centre of expertise for commercial issues.

Our study

We reviewed issues in individual contracts, looked at how departments were managing their contracts, and how the centre was giving leadership for government contract management. We considered the plans under 4 categories, based on our 2008 framework for contract management.

Our evaluative criteria

Governance and accountability for key decisions.

Visibility of contract information to senior management.

Integrating contract management with business objectives.

Capability and skills to manage contracts.

Our evidence
(see Appendix Two for details)

We reviewed issues in individual contracts from our previous reports; reviewed government departments' plans; and interviewed central commercial teams and departments to understand their proposed responses.

Our conclusions

The government will not get value for money from its contracts until it improves contract management. The Cabinet Office, HM Treasury and major spending departments have recognised the scale of the issue and have responded accordingly. The major spending departments have launched significant change programmes to improve their contract management. The Cabinet Office is strengthening its role in supporting the commercial profession, managing collective spending on common goods and services and supporting departments. We believe this represents an opportunity to bring about needed change. Nonetheless, there is a lot still to be worked out. In our view, there needs to be widespread change in the culture of the civil service and the way in which contractors are managed. There needs to be more emphasis on a commissioning approach, transparency over the contractors, use of open-book to align incentives and a targeted focus of the government's commercial capability.

Appendix Two

Our evidence base

1 We reviewed key documents including:

- our back catalogue of reports on government contracts;
- reviews of government contracts, including the detailed reports on the contracts reviewed;
- departmental plans produced in response to the review; and
- plans produced by the Crown Commercial Service.

2 We did more detailed interviews with 5 government bodies, the Department for Work & Pensions, the Department of Health, the Ministry of Defence, the Foreign & Commonwealth Office, and the Driver and Vehicle Licensing Agency. At each of these we met some of the main decision-makers including:

- commercial directors and their teams;
- senior managers responsible for contract management; and
- internal audit.

We also drew on the more extensive work conducted as part of our separate report on contract management in the Home Office and Ministry of Justice.

3 We interviewed Cabinet Office and Crown Commercial Service senior management to understand work they are planning to provide leadership across government. We reviewed supporting papers and data to verify information given in interviews.

4 We interviewed senior managers at G4S and Serco to understand the actions they are taking to respond to the discovery of issues in their contracts.

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