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Dear George,

ADS' Response to the SSRO's Consultation: Review of the Single Source Regulatory Framework

Thank you for the opportunity to comment on the '*SSRO's Consultation on Recommendations: Review of Part 2 of the Defence Reform Act 2014 and the Single Source Regulations 2014*'. ADS has liaised extensively with our members to develop the comprehensive response enclosed in Annex I, II and III. Annex I outlines ADS' feedback on the questions cited in the SSRO's online response form, while Annex II and III summarise the outcomes of the five SSRO/MOD/Industry tripartite meetings held earlier this year to discuss the topics listed. This information is further supplemented by the extensive analysis detailed in ADS' e-mail dated 9 March 2017 on each of the topic areas.

As previously discussed, at the DSF Main meeting held on 16 March the Secretary of State for Defence indicated his wish for a serious discussion around three key issues relating to single source defence procurement:

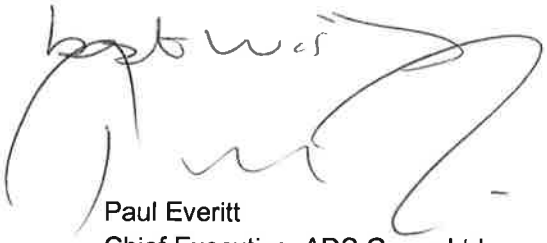
- Increasing the level of incentive available for those accepting the transfer of risk;
- Increasing the level of incentive available for non-financial performance; and
- A review of the Allowable Cost Guidance to clarify some of the areas where concerns have been identified.

Industry believes that early engagement on these three issues is essential. For the first two issues, in particular, it will likely be necessary to amend the Single Source Contract Regulations in order to implement any reforms in this area. Furthermore, industry believes that until its concerns around Allowable Costs are addressed, the SSRO will be unable to truly fulfil its statutory obligation to ensure companies receive a fair and reasonable price for the work undertaken in single source defence contracts.

I would very much welcome a meeting with you to discuss ADS' submission once you have had time to digest its contents. This will provide the SSRO with an opportunity to seek any clarification required on the feedback provided and will enable industry to better understand the SSRO's views on the issues raised, together with the likely direction of travel. I appreciate that the timescale for reviewing

the consultation responses received is tight and that the SSRO is required to provide its recommendations to the Secretary of State by mid-June. I would be grateful if your office could contact my Executive Assistant, Gemma Brown at gemma.brown@adsgroup.org.uk to arrange a time for us to meet at your earliest convenience.

As always, if you or any of your staff have any queries, I hope you will feel free to contact me directly.



Paul Everitt
Chief Executive, ADS Group Ltd

Annex I - ADS' Response to SSRO's Consultation on 'Recommendations – Review of Part 2 of the Defence Reform Act 2014 and the Single Source Contract Regulations 2014'

Introduction

ADS is pleased to offer the following responses to the above consultation on Recommendations. The text shown in text boxes represents the issues detailed in the consultation document and upon which views are sought.

Since the beginning of 2017 there has been a series of tripartite meetings held between the MOD, the SSRO and Industry during which the issues raised in the consultation document and a number of additional matters have been discussed in considerable detail. Annex II and III reflect the outcome of these discussions, including responses to the matters raised in sections 19 and 22-25 of the consultation document.

Responses

6. The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

ADS Response

1. ADS is mindful that the regulatory framework has only been operative for a little over two years and that the rules have been applied to only a comparatively small number of Qualifying Defence Contracts (QDCs) or Qualifying Sub Contracts (QSCs). Additionally, the number of contractors and subcontractors with experience of performing these types of contracts is still comparatively small. Overall, experience with the regulatory framework is limited and there are a number of aspects (e.g. completion, post-completion activities and enforcement) where there is no experience at all since these aspects have yet to be tested.

2. ADS feels that, on balance, the transparency provided by the current regime provides adequate exposure of single source procurement decisions and that the arguments in Sections 7 and 10 lack merit. Adopting the proposals would increase costs and the administrative burden (particularly for SMEs) without providing corresponding benefits. It also felt that the 'limitations' in paragraph 10.2 are proportionate and appropriate components of the regulatory regime. ADS believes that the regulatory regime in its current form already gives the SSRO access to the information it requires to discharge its statutory duties and its intended purpose.

3. ADS believes the consultation document offers insufficient evidence that initiatives aimed at promoting competition, increasing innovation or monitoring the involvement of SMEs in single source contracts will deliver improved value for money for the MOD or increase the certainty

that suppliers will receive a fair and reasonable prices. It also notes that the MOD (and wider government) already have significant initiatives in this area and that introducing additional requirements or reporting in this area is likely to duplicate work being undertaken elsewhere. For these reasons ADS does not support modifying the regulatory framework on the basis suggested.

7. Treating material contract amendments as new contracts and judging materiality by reference to the £5 million threshold (paragraph 6.12).

ADS Response

1. ADS does not support the proposal to amend either the Act or Regulations on the basis that if a contract amendment is £5m or greater, it will be considered to be a material amendment and automatically be treated as if a new contract has been entered into for the purpose of the Act and Regulations. ADS believes the proposed amendment is unnecessary on the following grounds:

    a. Materiality in the context of contract amendments is dealt with adequately in contract and case law. There is no need to introduce another definition or threshold. These should be applied to determine materiality (see *Pressetext, Edenred etc.).*
    b. The amendment would represent a major policy change which is that, in the event of an amendment, agreement of the parties is required to convert the contract to a QDC.
    c. There is a significant chance the proposed change if introduced would destabilise the contract and the bargain that was made at the outset.
    d. There is no evidence offered that the current regime is causing a problem the proposed change will resolve.

2. These issues have been discussed at length between the MOD, Industry and the SSRO in recent tripartite meetings. ADS agrees that the concept of severability in Reg. 14(2) is unhelpful and should be removed. At the same time, it is recognised that it is the attributes of the amendment that are key to determining whether or not the whole contract should be repriced. ADS believes that in all but a few cases, the estimated allowable costs associated with a contract amendment will be identifiable (severable), and that the only circumstances where a change to the contract profit rate may be considered is if the amendment results in a significant change in the allocation of risk (e.g. conversion of the contract from a cost plus basis to a firm price or TCIF basis).

3. ADS believes that further work is required to determine the extent and form of the changes required to Reg. 14, together with the need for new or amended guidance for deciding whether or not the whole contract profit rate should be amended. In particular, issues of repricing existing work and the profit rate to be applied as part of the repricing, and the extent to which Steps 2-6 are applied need further discussion.

8. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

ADS Response

1. ADS supports the proposed change at paragraph 6.13 in principle; however, before agreeing we wish to have clarification of the following:

    a. What is meant by 'committed' costs and associated profit (sunk costs). If this was taken to mean the MOD's commitment to the contract scope immediately prior to the amendment (whether discharged or future work by the contractor) then there is a strong likelihood the proposed change would be supported by ADS and its members.
    b. How a change in pricing methodology on amendment would be considered in relation to actual costs incurred immediately prior to the amendment.
    c. The extent of reporting on a contract that becomes a QDC on amendment. ADS believes this should be limited to the new scope with limited reporting (e.g. lump sums) on the original scope prior to the amendment. An exception to this might be in circumstances where the whole contract was repriced.

9. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

ADS Response

1. ADS does not support the proposal in paragraph 7.20 that a contract may be a QSC if it provides anything for a proposed QDC or QSC as it is likely to create significant uncertainty. For example, it may result in a contract becoming a QSC (i.e. a regulated contract) before the QDC which it will serve comes into existence. It is recognised that there is potential for avoidance; however, ADS feels that §29(3) and §29(4) recognise Parliament's intentions in this area and provide adequate anti-avoidance measures. It would be helpful if there was guidance available to the parties that defined the rules and conditions for determining when a potential subcontract became a single source contract and potentially a QSC.

10. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

ADS Response

1. ADS would support removing the 20 contract restriction provided that the requirement was limited to potential subcontracts with a value of £20m or greater. This will ensure that potential subcontracts near the QSC threshold are identified and deter creative assessments of subcontract values.

2. Major subcontracts will be identified prior to contract award and appear in the Contract Pricing Statement. It is, however, recognised that additional potential QSCs may be identified during the contract delivery phase and where this occurs, ADS believes new QSCs should be notified within 30 days of subcontract award.

3. ADS does not believe there is any merit in notifying unreported outcomes or negative assessments, and that reporting should continue to be by exception. The outcome of the vast majority of assessments will be self-evident (i.e. the subcontract was awarded on the basis of competition). However, assessments should be made exceptionally when the subcontract value may be near the threshold that triggers a QSC.

11. Reducing the QSC threshold to £10 million (paragraph 8.5).

ADS Response

1. ADS is mindful that, to date, there has been only a small number of QSCs awarded and feels that this sample is too small to judge the effectiveness of the current regime. We also believe that it is still too early to form a view on whether the current requirements are not working as intended or if there is some other form of problem that needs solving. Before supporting any proposal to lower the QSC threshold, ADS would wish to see a validated cost/benefit analysis which demonstrates the benefits that the parties would accrue from the change, as well as any other information to support the recommendations.

2. The consultation document offers insufficient evidence that lowering the threshold will bring meaningful benefits to the parties, in particular that it will increase the likelihood of the MOD securing better value for money or improve the prospects for subcontractors receiving fair and reasonable prices. It will, however, create a significant administrative burden and additional costs for subcontractors. ADS is aware from its membership that the further down a supply chain a supplier enters the market, the less likely it is to be dependent on the MOD customer. It is felt that reducing the threshold from £25m to £10m may result in some companies for whom defence is only a small or marginal part of their business exiting the market rather than opting to shoulder the additional administrative burden and cost of performing QSCs. This is contrary to the Government's stated desire to increase productivity and encourage SMEs to do more business with the MOD. Furthermore, if the proposed change is implemented, it may disrupt supply chains and jeopardise security of supply of critical components.

3. On a practical level, it is worth noting that the responsibility for agreeing prices on QSCs lies with MOD and not the contracting authority. Lowering the threshold in the manner proposed would result in a significant increase in the number of subcontracts and sub-subcontracts (and possibly sub-sub-subcontracts) falling within the regulatory framework. There needs to be certainty that MOD has the necessary resources required to price the additional contracts within a reasonable timeframe before lowering the threshold. Without this certainty there is a danger of disrupting supply chains and programmes.

4. ADS would, however, support a proposal to remove the anomaly that arises out of Regulation 58. A single source subcontract with a value of £24m, all of whose performance is for one or more QDCs or QSCs, will not be a QSC. In contrast, a single source subcontract with a value of £25m, of which 50% of the performance will be for one or more QDCs or QSCs, will be a QSC. Additionally, the pricing of that part of the QSC that does not enable the performance

of a QDC or QSC must be priced in accordance with the DRA pricing formula. ADS considers this to be disproportionate and believes that a significantly higher financial threshold (£50m) should apply if a contract is only partially enabling performance of QDCs and QSCs.

12. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

ADS Response

Intelligence Activities:

1. ADS does not support the proposal to bring any single source contract wholly for the purposes of Intelligence Activities under the regulatory framework provided that the subject matter of the contract does not disclose the associated operational purpose. ADS believes this change may jeopardise aspects of national security and the wider political context, as well as operational aspects.

2. ADS is also sensitive to the fact that information held by the SSRO may be subject to release under the Freedom of Information Act (FOIA). Whilst the FOIA contains a number of exemptions, including §24 National Security and §27 International Relations exemptions, ADS considers that the very use of such an exemption to prevent a release of information would in itself give the information an unwelcome profile, potentially harming either national security, international relations or both.

3. ADS would, however, be minded to support a proposal that single source contracts for Intelligence Activities, where brought under the regulatory regime, if there was an exclusion for those contracts where knowledge of the fact that the MOD was procuring a particular type of goods or service (or a combination of both) would jeopardise either national security or international relations. In making this suggestion ADS recognises that there must be safeguards developed to ensure the exemption is used only in appropriate circumstances. The ultimate decision on this issue must, however, always lie with the MOD.

International Co-operative Defence Agreements:

4. ADS recognises that the drafting of Regulations 7 and 58(2) create uncertainty. Particular issues requiring clarification include:

    a. Contracts where only part of the output relates to an international programme;
    b. Those where a significant proportion of the contract is procured on a bilateral arrangement and the remainder under a Memorandum of Understanding (MOU); and
    c. Quantities procured as part of an international workshare versus a follow-on buy solely for the UK.

5. These issues have been reviewed in outline during recent tripartite discussions.ADS believes further work is required to ensure any amendment to the regulatory regime covers all the likely scenarios, provides a comprehensive solution and clarity on the boundaries of the exclusion, together with safeguards to prevent its misuse.

13. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

ADS Response

1. ADS believes the government (MOD) is the arbiter of what is, and is not, value for money and it is therefore inappropriate for it to comment on this part of the question.

2. For those single source contracts that are not priced directly under the regulatory framework (i.e. those with values <£5m, their single source subcontracts, and single source subcontracts with values <£25m required to enable the performance of QDCs) the MOD seeks to include the provisions of DEFCON 811-815 in the contract. These conditions are intended to provide a proxy for the regulatory framework and will provide the assurance of value for money.

3. ADS considers that the pricing requirements contained in DEFCONs 811-815 and the associated project reporting requirements act as a proxy for the regulatory framework. This proxy provides adequate assurance that value for money in government single source contracts not covered by the regulatory regime will be achieved and that, simultaneously, suppliers will receive a fair and reasonable price. It is unnecessary to extend the scope of the DRA and SSCRs to include single source contracts and subcontracts described in the above paragraph.

4. These above views are, however, caveated by recognition that some companies will not accept these terms. In such instances other means of providing the assurance may be required.

5. ADS also notes that the price of some goods and services provided on a single source basis will be subject to market forces which will also provide the required level of assurance that value for money is being obtained.

14. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15); and
15. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

ADS Response

1. ADS does not support the proposed amendment as it believes that the powers afforded to the SSRO by the Act and Regulations already provide sufficient access to information to enable it to perform its statutory obligations. The MOD has open book access for all of their requirements.

2. In circumstances where the SSRO seeks access to a contractor's private information additional to that which it is required to provide under the regulatory framework (e.g. as part of an study it is performing on behalf of the Secretary of State or to its own account) ADS believes the onus lies on the SSRO to establish the following prior to committing to the study:

    a. That the contractor holds or is able to generate the information required.

b. The contractor's willingness to volunteer its private information and any conditions it may attach to the disclosure (e.g. requiring a direct confidentiality agreement between itself the SSRO, limits on the uses which may be made of the information or further disclosure (including within government)).

Key to achieving access to the information will be the trust, respect and the relationship the SSRO is able to establish with contractors.

3. If access to a contractor's private information is essential for an additional task being performed, the SSRO should canvas the MOD to leverage its influence to obtain the information.

16. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

ADS Response

1. Section 11 of the consultation document does not make a clear case that there is a problem to be solved. The arguments presented are based on speculation about conditions which may or may not occur at some time in the future. ADS considers that the requirements in the Act and Regulations regarding these aspects are clear and unambiguous, albeit they are complex and difficult for the non-specialist to understand.

2. ADS also considers that inexperience may lie at the heart of the examples of non-compliance reported in the consultation document. We believe as the MOD and its suppliers become more familiar with the regulatory regime and the understanding of its requirements grows, these will not be seen as issues requiring changes to either the Act or the Regulations.

3. Notwithstanding the above, ADS believes there is merit in exploring the proposal further with a view to identifying the best method of providing guidance that the contracting parties can refer to when establishing the rates to be used for Steps 1-6, and determining whether or not a contract is a QDC or QSC.

17. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

ADS Response

1. ADS strongly disagrees with the proposal that the SSRO should be given powers to issue compliance notices or any right to enforce penalties. The Act clearly establishes the MOD as the enforcement body and the SSRO as an arm's length and impartial arbiter that can offer opinions and make determinations in a set of clearly defined circumstances. Affording the SSRO the suggested additional powers would completely undermine it primary function and represent a major shift in policy. It would, in effect, become the prosecutor, judge and jury whose powers would be asymmetric since it would have no right of sanction against the MOD. ADS supports the existing process which it believes is adequate and allows the MOD

to assess the intent behind any non-compliance and its materiality before issuing a compliance or penalty notice.

2. The consultation document does touch on the problems contractors and subcontractors have experienced with the reporting regime. Notwithstanding that the regime is still comparatively new and that experience in completing and submitting reports is still comparatively limited, it is clear that there are a number of aspects of the reports and report formats where the requirement is unclear and contractors are having difficulty understanding what information they are required to provide and when. ADS suggests that the reporting regime and the report format are subject to a detailed tripartite review aimed at ensuring:

    a. The information being provided is useful and has an impact on the way the project and future projects are priced and managed; and
    b. Reporting requirements are clearly stated and readily understandable

18. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

ADS Response

1. ADS believes the regulatory framework reflects the government's intentions with regard to referrals and enforcement, and it is not clear what the problem is that the proposals are seeking to solve. It is appropriate that the SSRO should give opinions and make determinations only when asked to do so by one or both of the parties. ADS does not support the proposal that the SSRO should be able to initiate opinions or determinations as this will undermine its impartiality.

2. The proposal(s) to give the SSRO additional powers is based on supposition of what might happen at some future time. ADS believes this is an insufficient basis on which to proceed, and that the SSRO already has adequate powers to discharge its functions and statutory obligations in a manner that makes single source procurement a credible alternative when competition is not available or impractical. Giving the SSRO additional powers in the manner suggested would represent a significant shift in its role and government policy.

20. Issues raised concerning exclusion of government-to-government contracts (section 14).

ADS Response

1. ADS believes this is an issue to be resolved with the MOD.

2. ADS observes that persuading an overseas government to instruct its supplier to open up its books will likely be unachievable. It will also require the overseas government's consent before the enforcement powers in the DRA could be enforced on an overseas supplier. Additionally, it is likely there will be other issues with privity of contract and under whose law the contract has been placed.

21. Issues raised concerning enforcement of price control (section 15).

ADS Response

1. ADS does not support any assertion that the SSRO has a duty enforce price controls or that the SSRO has a role to play in this area. The SSRO's functions are stated in paragraph 1.3 of the consultation document and this does not include reference to a duty to enforce price controls. The term 'price controls' is one of the SSRO's own construction as contracts must be priced using the pricing formula. 'Price control' has no meaning in this context.

2. The primary aims of the SSRO given in §13(2) are to ensure:

    a. That good value for money is obtained in government expenditure on qualifying defence contracts; and
    b. That persons other than the Secretary of State who are parties to the qualifying defence contracts are paid a fair and reasonable price under those contracts.

The Act and Regulations are silent on the need to 'strike a balance' between the objectives cited above, implying that they have to be achieved simultaneously.

3. ADS agrees with the statement in paragraph 15.3 of the consultation document that notes the primary responsibility for ensuring that pricing complies with the requirements of the regulatory framework (not with the pricing controls as stated) lies with the contracting parties. It also supports the policy contained within the regulatory framework whereby the SSRO does not have a role to play in setting prices unless there is a dispute between the parties and one or both refer the dispute to the SSRO for an opinion or a determination. If at any time the SSRO believes a price may not have been set in accordance with the regulatory framework, it should refer to the MOD in the first instance.

4. ADS does not support any of the remaining changes suggested for the Act or Regulations outlined in section 15 on grounds that the SSRO's functions are already adequately described by the regulatory framework and that the powers it has been given are adequate for it to discharge its statutory functions.

19. The SSRO's recommendations.
22. The proposal for disapplying the price formula (section 17).
23. Stakeholder proposals supported by the SSRO (section 18).
24. Stakeholder proposals not presently supported by the SSRO (section 19).
25. Stakeholder proposals where additional explanation or evidence is required (section 20).

ADS Response

1. The issues raised under these headings, together with a number of other issues identified by Industry, have been discussed in detail at the recent tripartite meetings referred to in the introduction to this response. During the course of these discussions a number of items have been identified as a priority issue needing to be addressed and requiring proposed changes

to the regulatory framework made as part the recommendations due to be submitted to Secretary of State in June 2017. Other items have been classed as being of lesser importance or urgency which can be addressed between June and December 2017 by either changes to the Regulations or in Guidance (statutory or otherwise). A small number of items have been withdrawn. Although described as lesser important/urgent items, many of which are technical in nature, industry requires them to be resolved. ADS believes that the focus of the Review should be on making the changes that help make the regulatory regime work as intended, and that it is premature to make wider changes to the scope of the regulatory regime or the role of the SSRO.

2. Details of outcome of the discussion on each of the above items and where appropriate, the proposed action(s) for each of the 92 items identified, are contained in Annex II and III.

26. Other suggestions for amendments to the legislation.

ADS Response

1. Experience with the regulatory framework to date has shown that contractors find its requirements complex and difficult to understand. ADS believes that this complexity and lack of understanding lies behind the majority of the non-compliance issues encountered to date. The changes to the detail of the regulatory framework proposed in the attached will improve this situation and, as further experience is gained, contractors will become more confident and better able to respond to reporting requirements. Notwithstanding this, ADS believes it would be prudent to have the next review of the regulatory framework in three years' time and not five years.

27. Alternative approaches to improve the regulatory framework that do not require legislation.

ADS Response

1. ADS' views on alternative approaches to improve the regulatory framework that do not require legislation are contained in Annexes II and III to this response.

Annex II – Defence Reform Act 2014: ADS' Review of Legislative Issues

Item	Issue	Reference	ADS Position
	QDCs and parts of them		
1.	QDCs and QSCs are referred to as complete contracts which do not allow the Regulations to address parts of a contract. The legislation should be revised to enable parts to be excluded from the regime. Only the value of those parts of a contract which the contractor is authorised to perform should be included when calculating the value of the contract for the purpose of determining whether the contact is a QDC. AAR should be qualified to accommodate situations when parts are excluded from the pricing regime and recognise that they cannot be applied to the whole contract. There should be an express disapplication of the legislation to parts of the contract that are subject to competition or otherwise to market forces.	14(1) 14(2)(b) 20(2)	ADS regards this as a priority item which should be addressed as soon as possible and that it should be included in the SSRO's review of the regulations. It has been discussed with MOD and the SSRO in during recent tripartite workshops in February
	Pricing amendments		
2.	Pricing of amendments should be limited to just that and not repricing the whole contract as amended. Section 15(3)(a) should be deleted.	15(3)(a), Reg 14(2)	ADS regards this as a priority item which should be addressed as soon as possible and that it should be included in the SSRO's review of the regulations. It has been discussed with MOD and the SSRO in during recent tripartite workshops in February
	Pricing formula		
3.	The pricing formula should be supplemented in specified circumstances to allow for items subject to market prices, commercial price lists, COTS, MOTS and additional quantities of items previously competed.	15(2), 15(4)	ADS regards this as a priority item which should be addressed as soon as possible and that it should be included in the SSRO's review of the regulations. It has been discussed with MOD and the SSRO in during recent tripartite workshops in February
	Contract profit rate		
4.	Step 3 (POCO) should be adjusted to exclude deductions where input prices have been established by market forces or constrained by	17(2) Step 3.	ADS considers this as a lesser priority and may be deferred until later. It has been discussed with MOD

Item	Issue	Reference	ADS Position
	market forces.		and the SSRO as a matter for being dealt with in guidance.
5.	Clarity is required on the process to adopt if a contacting authority is unable to agree prices with its subcontractor because the latter will not provide adequate information to the contracting authority e.g. the assessment of risk.	17 (4)	ADS considers this as an issue for consideration by the SSRO in its June review. We believe that this should be deferred until later and discussed with the SSRO as a matter for being dealt with in guidance.
	Return on fixed and working capital		
6.	"....for the purpose of enabling the primary contractor to perform the contract" should be deleted as being too limiting, since the capital for the business as a whole. "Having regard to" should be replaced by "taking" to ensure consistency. Reference should be made to "direct" allowable costs for clarity.	17(2) Step 6 17(2) Step 6 (a) 17(2) Step 6 (b)	ADS withdraws this proposed change. ADS considers this is a lesser priority item and may be deferred until later. It has been discussed with MOD and SSRO as a matter that could be dealt with in guidance. ADS withdraws this proposed change
7.	Secretary of State should be required to justify the circumstances that cause him to require the contractor to show AAR.	20(4)	ADS withdraws this proposed change

	Final Price Adjustment		
8.	A "purpose" should be stated to limit the scope of "final price adjustments".	21(1)	ADS considers this is a lesser priority item and may be deferred until later. Further discussion is required to evaluate if the issue may be dealt with in guidance.
9.	Parts of a contract should be excluded from final price adjustments e.g. gain-sharing and market prices.	21(4)	ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate if the issue may be dealt with in guidance.
	Recovery of unpaid amounts		
10.	Amounts should be payable to or from the Secretary of State rather than a higher tier contractor for: • SSRO determinations on allowable costs; • SSRO determinations on profit allowances; • SSRO determinations on final price adjustments; and • when there is an agreement between the parties.	22(1)(b) 20(6) 18(3)(b) 21(3)(b), 22(1)(a)	ADS considers this is a lesser priority item and may be deferred until later. The issue is currently only covered to a limited extent in 22(1)(b)
	Records		
11.	The purposes for which the retained records may be used by the Secretary of State should be limited to establishing: • any "material" difference between estimated and actual allowable costs • any other "material" matter "directly concerning" the price payable	 23(3)(b)(ii) 23(3)(b)(iii)	ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate if the issue may be dealt with in guidance.
12.	The Regulations should be amended to require that the standard of explanation should be to the extent necessary for a person suitably qualified and experienced in interpreting management and financial information of that type to understand.	23(5)(d)	ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate if the issue may be dealt with in guidance.

	Designated Person		
13.	The ultimate parent undertaking may be too remote from the operations of the contractor for the purposes of reporting – would the "highest tier company performing material regulated work" be more sensible.	25(3)(a)	ADS withdraws this item.
	Reports on overheads and forward planning		
14.	Reference to "financial year" should be qualified as the "contractor's" financial year to be more practical and clearer.	25(1), 25(5), 25(8)	ADS considers this is a lesser priority item and may be deferred until later.
	Duty to report relevant events		
15.	Secretary of State should be required to notify the contractor of relevant events.	26(1)	ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate if the issue may be dealt with in guidance.
	Qualifying Subcontracts		
16.	A QSC should be limited to contracts "solely" for the provision of "goods, works or services" "directly allocated" for a QDC. A QSC should exclude contracts (and parts of them) where the price has been established by market forces (e.g. proprietary list prices) as well as by competition. The regulations should make provision for determining whether prices for the whole or parts of a contract are established by market forces, as well as by competition. Application of the Part 2 of the Act to QSCs should also allow for application to only part of a QSC, e.g. to allow for the exclusion of proprietary and market priced items in the QSC.	28(2)(b), 28(3)(a), 28(4)(a), 29(1)(a), 29(3)(c) 28(3)(b) 28(4)(b) 28(5) 30(1)	ADS withdraws this item.

	Application of Part 2 to QSCs		
17.	The contracting authority should be able to give notice to the SSRO that Part 2 of the Act and the Regulations should cease to apply to a QSC as well as the subcontractor.	30(4)	ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to determine the best way of dealing with the matter.
	Schedule 5, Restrictions on Disclosing Information		
18.	A person holding information should be required to "take adequate technical and organisational measures against unlawful disclosure of, and against accidental loss of, information".	Sch 5, 2(1)	ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate the merits of the issue and thee best way of dealing with the matter..
19.	A company that suffers damage, by reason of any contravention [of the requirement to take adequate measures] by a person who holds information, should be entitled to compensation from that person for that damaged. It should it be a defence for the holder of that information to show that they had taken such care as in all the circumstances was reasonably required to comply with the requirement.		ADS withdraws this item.
20.	Disapplication of an offence of disclosure should be limited only to information "lawfully" disclosed to the public?	Sch 5, 4.	ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate if the issue may be dealt with in guidance.
21.	Disapplication of an offence of disclosure to be limited to those disclosures under the Freedom of Information Act 2000 "where there is a requirement to disclose notwithstanding available defences"?	5(1)(g)	ADS withdraws this item
22.	Where disclosures are made within government or for administrative purposes, those disclosures should be limited to only those where strictly necessary, in confidence, with a reminder that an offence of disclosure continues to apply.	Sch 5, 5(1)(a) to (d) and (h) to (k)	ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate if the issue may be dealt with in guidance
23.	An independent industry body should have the right to verify the technical and organisational measures implemented by the holder of information for protecting the information to which the Schedule applies?		ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate if the issue may be dealt with in guidance.

24.	A version of the Act as it applies to subcontracts should be produced.		ADS withdraws this item.
25.	Provision should be made to disapply the regulatory framework when contracts or subcontracts are placed in countries that have a single source regulation to cover pricing as that scheme and the UK scheme may conflict.		ADS considers this is a lesser priority item and may be deferred until later. Further discussion between the parties is required to evaluate if the issue may be dealt with in guidance.

Annex III – Single Source Contract Regulations: ADS' Review of Legislative Issues

Item	Issue	Ref.	ADS Position
	Interpretation		
1.	There should be a definition of a "regulated contract", which can be used to refer to a QDC or a QSC.	2(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
2.	There should be a definition of "contract value" (as distinct from "contract price" or "value of a contract"- per Reg 5) e.g. "means the estimated price of the contract for the requirements on contract at the time of valuation".	2(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
3.	There should be a <definition> for "allowable costs" to say that it includes standards and variances as described by professionally recognised accounting standards. The Regulations should clarify whether "pegged costs" are admissible as allowable costs or otherwise.	2(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
4.	There should be definitions of "framework agreement" and "framework contract" to distinguish between them and to clarify the incidence of QDCs arising from them.	2(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
5.	There should be a reference to the Euro conversion rate to be used in the definition of SME. This should be by reference to the latest Communication from the Commission on Corresponding values of the thresholds (2015/C 392/01), or to some other identified conversion method.	2(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
6.	The Regulation should allow cost recovery base and cost recovery rates to include PV IR&D which may have been incurred in prior periods.	2(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.

Item	Issue	Ref.	ADS Position
7.	The contract completion date definition is adequate only for subcontracts where MOD has driven the need for a subcontract to be put in place; it does not work for: • Indirect activities of an indefinite duration; and • Framework agreements put in place to enable multiple acquisitions for various customers.	4	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	Valuation		
8.	Regulation 5(4)(b) should be amended to exclude the value of any land, buildings, equipment, information, personnel or other resource that is provided by the **Secretary of State**	5(4)(b)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
9. See also Item 41	Conversion rates for currencies are not normally in accounting policies; "accounting" should be deleted.	5(4)(c) 22(8)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
10.	Aggregation of contracts for a common "requirement" in order to determine if the value for a subject contract is a QDC leads to perverse outcomes e.g. 6 contracts worth £10m in total awarded or to be awarded over time to the same contractor to fulfil parts of the same requirement, having individual contract prices of £1.1m, £0.9m, £4.5m, £2.2m, £0.5m and £0.8m: all of the contract have values lower than the normal value for a QDC (£5m) and three contracts have contract values lower than the current £1m threshold in Regulation 5. The Regulations should be amended such that determining QDCs in this manner is removed.	5(5) to (9)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
11.	The Regulations should be adjusted such that the value of individual Framework Contract or Framework Agreement	5(6)-5(8)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and

Item	Issue	Ref.	ADS Position
	tasks or orders that qualify to become QDCs is set at an appropriately high value and regulation 6 amended to reflect same.		further discussion may be deferred until later.
12.	The provisions at Regulation 5(12) should be deleted as not applicable to single source procurement, as they are derived from public procurement regulations that apply to intra trading within a public contract authority?	5(12)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	Contracts that may not be qualifying defence contracts		
13.	Certain parts of contracts should be excluded from the pricing mechanism where a price can be established by other means, e.g. Commercial Items, market priced items, non-developmental items,	7	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
14.	The definition for the exclusion for "intelligence activities" and its scope of application needs clarification.	7(c)(iii)	ADS regards this as a priority item which should be addressed as soon as possible and that it should be included in the SSRO's review of the regulations. It has been discussed with MOD and the SSRO in during recent tripartite workshops in February.
	Pricing of Contracts		
15.	The Regulations should be adjusted to allow for a supplement to it in specified circumstances e.g. market prices, commercial price lists, COTS, MOTS and additional quantities of items previously competed.	10(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
16.	The regulations should be amended to allow other forms of regulated pricing methods e.g. cost plus fixed fee, and a fuller description of the "Target pricing method" at 10(11) provided.	10(4) to (11)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
17.	Sub para 10(12) looks as though it might be part of the "Target pricing method"; the drafting should be adjusted to separate the formatting or the clarification the clarification should be put in the relevant sub-para.		This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.

Item	Issue	Ref.	ADS Position
	Calculation of profit on cost once (POCO) adjustment		
18.	The phrase "necessary to enable the performance of the qualifying defence contract" should be amended to avoid indirect purchases where only some or part of which are relevant to the contract.	12(5)(e) and (6)(e), and 13(5)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	Rates agreed on a group basis		
19.	Withdrawn – an issue for the Act		Withdrawn
20.	Withdrawn – an issue for the Act	13(6)(b)	Withdrawn
	Redetermination of contract price		
21.	Reg 14(2), the circumstances when the allowable costs relating to an amendment are not severable should be defined. Reg 14(4), should be amended such that the whole contract price is only redetermined in the circumstances defined by the amended Reg 14(2).	14(2) 14(4)	ADS regards this as a priority item which should be addressed as soon as possible and that it should be included in the SSRO's review of the regulations. It has been discussed with MOD and the SSRO in during recent tripartite workshops in February.
22.	Change the heading of this section to pricing of contract changes. This regulation needs to be removed in its entirety and replaced with a new regulation saying how contract changes should be priced in a range of differing circumstances (e.g. sub-contract changes not caused by a change to the MOD requirement). Also exclude from the regulations any requirement to price concessions/production permits in accordance with the pricing formula.	14	ADS regards this as a priority item which should be addressed as soon as possible and that it should be included in the SSRO's review of the regulations. It has been discussed with MOD and the SSRO in during recent tripartite workshops in February.
	Final price adjustment		
23.	Amend the Regulations to clarify whether the price adjustment for a qualifying subcontract falls between: (1) MOD and the subcontractor, or (2) The contracting authority and the subcontractor. If (1) then clarify the rights of the contracting authority in	16	ADS regards this as a priority item which should be addressed as soon as possible and that it should be included in the SSRO's review of the regulations. It has been discussed with MOD and the SSRO in during recent tripartite workshops in February.

Item	Issue	Ref.	ADS Position
	these circumstances. If (2) then the paragraphs need to give rights to the contracting authority in sub paragraphs 5, 6 and 7 and place an obligation upon MOD to inform the parties of the amount of money needs to pass.		
24.	The words "Unless a direction is given under section 21(5)," should be added to the start of Reg 17(1) to reflect the provisions that disapply the calculation.	17(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	Duty to keep relevant records		
25.	A further time limit on the keeping of records should be added to Reg 20(7)(a): "or the date from which it is determined that the contract is no longer a qualifying defence contract".	20(7)(a)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	Examination of relevant records		
26.	The qualification "acting reasonably" should be added before "may request P to provide further information or explanation" in Reg 21(5).	21(5)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
27.	The Regulations should be amended to require that the standard of explanation should be to the extent necessary for a person suitably qualified and experienced in interpreting management and financial information of that type to understand.	21(5)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
28.	Reg 21(5) should be amended to include a time limit within which a request for "further information or explanation" must be made e.g. 6 weeks after the records are made available for examination	21(5)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	Reports – General requirements and interpretations		
29.	General issues on reports:		This issue has been reviewed as part of recent tripartite

Item	Issue	Ref.	ADS Position
	• The regulations should address fundamental reporting issues such as the timing of recognition of costs. • The regulations should make clear about how and when changes should be incorporated e.g. when they are priced or when committed, as they arise or on a periodicity within the reporting cycle (MRP and non-segregated project stock issues must be resolved) • Reporting risk/contingency is very confused, and requires clarification in line with changes suggested to SSCSs		discussions. ADS considers it is a lesser priority item and further discussion may be deferred until after June. A workshop on these items may be required to identify and bound the problems.
30.	The term "business unit" should be qualified by the addition of "of the primary contractor".	22(2)(l)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
31.	The base on which "5%" is measured should be clarified.	22(6)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
32.	The Regulations should be amended to either: • Allow reports to be expressed in the contractor's functional currency, or • Specify how the conversion rate should be determined and used. The rate should be set for the whole term of the contract.	22(8)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
33.	Amend regulations to require reports to be compiled for specified quarters allow a ±4 day variance on the date to reflect the practicality of closing accounting records.	22(10)(b)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.

Item	Issue	Ref.	ADS Position
	Contract reporting plan		
34.	The "value of the contract" or just "value" should be defined for reporting purposes as the "contract value" estimated by the contracting authority in Reg 5 may be a much higher number and not reflect work authorised and on contract.	24(2)(a) and 26(5) and 27(2) and 31(2)(a) & (b) and 50(5)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	Contract notification report		
35.	The term "non-recurring" should be defined as there could be different interpretations of its meaning.	25(2)(e)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	Quarterly contract report		
36.	The Regulations should be amended to clarify that the basis of reporting estimates at completion "EAC". The one month deadline for reporting may require estimates in excess of the 5% allowed in Reg 22(6).	26(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
37.	The Regulations should be amended to remove the requirement to provide the quarterly profile of the previous financial year.	26(6)(e)(ii)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
38.	The term "a quantified analysis of the causes of variance" should be qualified by referring to "an estimated quantified analysis of the causes of variance exceeding 2% of the value of the contract"	26(6)(f) and 27(4)(i) and 28(2)(i)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
	Part 6 – Interpretation/Application		
39.	The Regulations should be amended to clarify the: • Requirements of Regulations 31 and 32 which are		ADS regards this as a priority item which should be addressed as soon as possible and that it should be

Item	Issue	Ref.	ADS Position
	complicated and poorly understood, and • Term financial year which is used widely throughout Part 6 for requirements for the production of reports. This drafting needs to make clear that the requirement is against the contractor's accounting period and not HMG's or there needs to be a means of accommodating the contractor's FY within the reporting regime.		included in the SSRO's review of the regulations. It has been discussed with MOD and the SSRO in during recent tripartite workshops in February.
40.	The phrase "provides anything for the purposes of any qualifying defence contract" is very broad and difficult to ascertain (particularly for indirect subcontracts and group services when the period of performance can be long/indefinite). The Regulations should be amended to limit its scope to goods/works/services supplied on a single source basis.	32(3)(c) and (4)d) and 5(e) and 40(3)(b) and 58(3)(a) & 58(4)(a)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
41.	The provisions of Reg 32(6) should be limited to extant single-source contracts and supplies.	32(6)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
	Part 6 –General requirements		
42.	The distinction between employees and contractors, which are usually both are classified by companies as labour, should be clarified and any differences in reporting requirements stated.	33(3)(b) and (d)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
	Actual rates claim report		
43.	The Regulations should be amended to limit supply of information to that adequate to support the costs being claimed.	34(3)(d) and (e)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.

Item	Issue	Ref.	ADS Position
44.	The requirements in Reg 34(3)(f) should be clarified and any restrictions in scope identified. At present the requirement includes prepayments or accruals or both, and depreciation or amortisation or both.	34(3)(f)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
45.	The requirement to report direct costs should be deleted: it is inappropriate to include them in a rates report.	34(3)(g)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
	QBU actual cost analysis report		
46.	The requirement should be limited to reporting only costs claimed (not 'total actual operating costs incurred').	35(7)(a)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
47.	The requirement in 35(8)(b) should be limited to explaining 'key' or 'material' cost differences only.	35(8)(b	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
	Estimated rates claim report		
48.	The requirement to report the budget for the QBU will result in significant amounts of price sensitive and personal data being supplied which are unnecessary to assess the overheads being claimed. The regulation requirement should be limited to budget data for estimated rates claims and volumes only.	36(3)(d) &(e)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.
49.	Remove the requirement to report direct costs as this is a rates claim report.	36(3)(g)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.

Item	Issue	Ref.	ADS Position
	QBU estimated cost analysis report		
50.	The requirement should be revised to explaining 'key' or 'material' cost differences only.	37(8)(a)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
	Rates comparison report		
51.	Reg 39(4) appears to be calling for the wrong information: it should be asking for data for the business in total, actual vs priced, then taken into significant contract assessment.	39(4)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
	Strategic industry capacity report: corporate structure		
52.	Information regarding 'anticipated changes to the corporate structure' involves very sensitive data known only to a few in the organisation. The requirement for this aspect should be removed from the report and made the subject for discussions between CEOs and Main Building.	41(f)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The very limited circulation of the SICR report is acknowledged.
	Strategic industry capacity report: activities, people and infrastructure		
53.	The requirement should refer to "key" activities only.	42(1)(a) and 42(1)(b)(v) & (vi)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
54.	The physical site reporting threshold should be raised to a more realistic level from £1m to £10m.	42(1)(b)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.

Item	Issue	Ref.	ADS Position
	Strategic industry capacity report: forecast costs of maintaining industrial capacity		
55.	The requirement to describe employment/bonus/training policy (and approximate cost) is too wide and should be limited to a more meaningful and practical extent.	43(2)(d)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
56.	The requirement to analyse the information by other defence contracts and all other contracts should be deleted as it is unreasonably burdensome and will produce dubious outcomes.	43(3)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
	Small or medium enterprises ("SME") report		
57.	The requirement to provide an SME report should be limited to providing data that does not form part of the information already being supplied in Cabinet Office SMEs reports	45	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
58.	Indirect SME activity should be reported only on a total business basis as any other basis is difficult/meaningless (subject to item 57 above).	45(4)(c)(ii) and (iii)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.
	Information specified for the purposes of paragraph 1(1)(c) of Schedule 5		
59.	The term "substantially" should be deleted from the phrase "its disclosure would be likely to substantially prejudice the commercial interests of any person", as it is too high a standard for information obtained under compulsion.	56(2)(b) and 56(5)(b)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. The topic should be considered as part of the proposed tripartite workshop on reports and reporting.

Item	Issue	Ref.	ADS Position
	Qualifying sub-contracts		
60.	The definition of 'contracting authority' as applied to a qualifying subcontract lacks subtlety. MOD is responsible for agreement of allowable costs that go into the price and settlements of any errors between MOD and the subcontractor which means the contracting authority is not the only party which is liable to pay the contract price under a QSC	57	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
61.	The Regulations should be amended to limit occasions when a subcontract, 50% of whose output by value is (or may be) required to enable the performance of one or more QDCs or QSCs, becomes a QSC to direct subcontracts only.	58(3)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
62.	The pricing of QSCs should be amended to allow them to be priced on the basis of price reasonableness e.g. commercial items or additional quantities following on from a previous competition where the price can be shown to be reasonable by bridging between two procurements with the same supplier.	59 & 60	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
63.	**'anything for the purposes of'** is far too expansive and the regulation should be amended to exclude: • outside of goods, works, and services • it should not include indirect acquisitions. The MOD and the contractor should be able to agree what is a subcontract that should be included within these regulations and not be excluded as business as normal for the contractor.	61(1)	ADS withdraws this item.
64.	Amend Regulation to allow the contracting authority to apply for cessation of application of SSCRs to qualifying sub-contracts.	63(1)	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.

Item	Issue	Ref.	ADS Position
	Modifications of Part 2 of the Act **Modifications of these Regulations**		
65.	These Regulations (and the Act at §31) create confusion and uncertainty as to what should be changed to apply the provisions to a subcontractor. As there will be far more QSCs than QDCs, it is more important to have clarity for QSCs. At the very least, working copies of the Act and the Regulations should be prepared that make the necessary changes, so that there is a definitive record of how those documents should read when the changes have been made.	64 and 65	This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
	Other matters		
66.	Amend Regulation to require MOD to respond to reports, or raise queries, within a specified time period.		This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
67.	Amend Regulations so that restructuring costs are taken outside of the scope of the regulatory framework.		This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later.
68.	Amend Regulations to allow the requirement for reports or some report content to be disapplied when MOD and the contractor agree it provides no utility or the cost of producing does not represent VFM.		This issue has been reviewed as part of recent tripartite discussions. ADS considers it is a lesser priority item and further discussion may be deferred until later. It is thought it may be possible to deal with the issue in guidance.

Consultation response - Babcock International Group

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response.

If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Gary Lambert***
Organisation: ***Babcock International Group***
Position: ***Naval Marine Finance Director***
Respondent type:
Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☑	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
	Other, please specify:

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.
- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes. The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

Whilst we are supportive of the principle of working in an open book partnering arrangement with the MoD having done so for a number of years, we are concerned about some of the suggested changes to the regulations put forward by the SSRO, further detailed below. We don't consider that add value to either MoD procurement or industry and there is a danger of increasing the regulatory and cost burden to both parties for no discernible benefit. We would also state that we agree in principle to the promotion of competition and innovation, and the involvement of SMEs, all of which we have been involved with, and continue to support.

It is clearly an important point to note that any changes to the regulations and the powers of the SSRO need to show quantifiable benefits. The SSRO is a regulating body, not a contracting party, and as such any changes must also ensure there is no duplication of the work which MoD must, as a contracting entity, perform in undertaking due diligence of industrial partners and the negotiation and execution of contracts affected by the legislation. We welcome the SSRO's recognition of these points in their attempt to show benefits in the document, however we would suggest that the document does not fully demonstrate any compelling cases with proven benefits. Instead there are unsubstantiated references to delivery of additional benefits or the collection of more data. All of this comes with a very real cost to both the MoD and industry and therefore a more comprehensive, quantitative 'business case' justification is needed to justify any changes that may introduce a new cost burden.

Industry has participated in a large number of consultations and calls for input in relation to the SSCR over the last couple of years. To date we have seen few of our concerns incorporated in the final outcome. In the vast majority of cases any comments or feedback provided to the SSRO has at best been ignored, and in many cases openly criticised. Furthermore, we would highlight that it is difficult to envisage industry, and the MoD, supporting expansion of the powers and remit of the SSRO when we have experienced significant reduction in profit margin, increases to regulatory costs, reduced flexibility around innovative contracting and an increase in risk. These issues have arisen in large part through the implementation of the regulations in a way contrary to the original intent of the Currie report.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.

Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

The SSRO recommends that material contract amendments are brought into the regime, removing the current requirement for agreement by both parties. The recommendation also states that this should be treated as entering into a new contract (which, in itself, is a misconception from the generally held understanding of a contract amendment; that it is a process to modify an existing contract). The impact of this would likely be far greater than the SSRO realises. Currently both the MoD and Contractors have the option to enter new contracts or amend current ones, and the selection to use the route of amending an extant contract is primarily one of expediency and efficiency. The move to a new contract usually involves significant negotiation, commercial and legal cost for both parties and takes significant amounts of time. In addition, the amendment would have to adopt the appropriate DPS which the original contract would not, which would add complexity and confusion. By removing the safeguard of agreement between both parties, thereby moving a contract into the regime, the SSRO will be introducing a significant extra cost burden for no quantifiable benefit. In practical terms this is likely to limit the parties' ability to contract as there is no incentive to agree to amendments that would bring them into the regime. Furthermore, many contracts define how contract amendments are to be treated (pricing, commercial terms etc.) so to enforce a different pricing approach could be seen as retrospectively applying law to an existing contractual agreement which may have legal consequences.

We would also highlight that the benefits and impact statement in section 6.16 does not provide any evidence to support this recommendation. It merely restates the overall estimated benefits for the single source regime. The SSRO also fail to recognise that protracted new negotiations over items which may previously have been amended will reduce the flexibility of MoD procurement and may impact operational availability of assets.

Most contract amendments relate to changes in volumes and specification. In terms of materiality, the scope of the contract doesn't change. We do not follow the logic that understanding the materiality of the contract change can be expressed purely by virtue of value. Also if the contract is already extant and industry are obliged to amend the contract to meet the MoD needs then it's negotiating position is weakened significantly and may lead to industry refusing to accept contract amendments if they are forced into the SSCR regime, particularly where the original contract was won in competition. Imposing the SSCR regime on previously negotiated contracts on amendment will significantly slow down the customers' ability to amend volume and specification and put Defence Outputs at risk. Our first QDC took 2 years to negotiate and amendments are likely to take even longer.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

We agree entirely with this recommendation as it will remove a significant risk area under the current legislation.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

We would agree with this in principle as our understanding of the intention of the Regulations was that they were intended to capture sub-contracts that were for the purposes of a QDC, regardless of when they were signed.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

Whilst we can understand the intention behind the SSRO's recommendation, we would be concerned at the scope of the change in comparison to the benefits. There will inevitably be increases in costs associated with placing an assessment deadline as this will require the reallocation of resources to perform. The SSRO themselves refer to the limited benefits to some of the changes, e.g. section 7.29, and so we feel that the issue is not significant enough to warrant increasing the regulatory burden.

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

We strongly disagree with this recommendation. There seems to be a desire to align the QDC and QSC thresholds, but no consideration that the alignment should actually be that both thresholds are set at £25m. The intention behind the regulatory regime was to give the MoD better insight into the material single source contracts and we reiterate our contention that the £5m threshold is too low as it captures immaterial contracts, in comparison to the MoD's total spend, and increases the regulatory burden to such an extent that it acts as a disincentive to contracting with the MoD. As the cost of maintaining compliance processes and knowledge (as opposed to reporting processes) is similar if you have one £5m contract or multiple billion pound contracts, it acts as a disincentive to competition.

The analysis provided by the SSRO itself (figure 6) shows that 72% by value of subcontracts would potentially be caught by the regime under the current threshold, which we believe to be material coverage. This value is represented by 18 contracts. The number of contracts caught under the lower thresholds increases significantly, whilst the value decreases, meaning the incremental benefit gained by the MoD through insight into these contracts decreases significantly. We do not see where the benefit to the MoD lies, and in spite of the implication in section 8.7, we do not see how this change would help deliver an improvement to fair and reasonable prices.

Perhaps the most significant issue however, lies in the impact to MoD operational capabilities. The SSRO should recognise that the SSCR is a high compliance regime, which acts as a disincentive to transact with the MoD. This is most apparent from feedback industry has received, and that has been presented to the SSRO in open consultation forums, from suppliers based in the USA. The MoD is in a comparatively weak negotiating position as they would like to procure a range of items from US defence suppliers (which are often via sub-contracts through the main prime contractors as part of wider projects), but the size of the contracts are not necessarily that significant to the US suppliers. If they find their margins eroded through the price control mechanisms, disallowable costs and increased administrative burden, they are in a strong position to refuse to supply. This will impact UK defence capabilities. This seems to contradict the government policy of encouraging SME's into the defence supply chain. The costs of compliance will be a significant factor to an SME entering the defence market.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

We would disagree with the suggestion to isolate elements of the contract such that they would then be qualifying under the SSCR. We think that it is important that the UK Government has the ability to exclude these contracts. There is a very real risk that the UK could lose vital supplies of defence equipment and capabilities if these exclusions are not maintained.

Even if the current proposal is pursued by the SSRO, it will need further clarification around the size of the element that should be included. For example, if a £10m 'excluded' contract has 5% which is deemed should be included under SSCR, then that amounts to £500k of revenue. Using the current baseline profit rate of 8.95%, the profit for that element would be c.£45k. The costs of compliance associated with the regime are significant (monitoring and assessing compliance, reporting, maintaining knowledge of regulatory changes etc.). It is inappropriate for these costs to be born on elements of larger contracts if they are not material and it is also inappropriate that previously unaffected suppliers are brought into the regime. They would, have to suffer the costs identified above for comparatively small elements of their contracts. As such, we would suggest the recommendation be amended to state that the element of the contract deemed to be allowable must meet the SSCR contract size threshold of £5m on its own, separately from the size of the overall contract.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

The SSRO does not have an obligation to ensure either of these requirements are met for contracts outside of the SSCR. The MoD is responsible for ensuring they are comfortable with the contracts they put in place and has the obligation to the UK taxpayer to deliver value for money.

It is important to re-emphasize that it is inappropriate to expand the remit of the current regulatory regime, or the powers of the SSRO, without a clear and quantifiable benefit to all parties affected for each incremental change. There are significant costs borne by industry and the MoD in assuring compliance with the regime and each change that is made. The imposition of more cost needs to come with a justifiable benefit, or by default the change should not be implemented.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

Section 10 raises the issue of increasing the SSRO's powers to ask for information. This has been presented in comparison to other regulatory bodies, however we would argue there is a false equivalency due to the specific nature of single source defence procurement, where both sides have equal economic strength, i.e. a monopoly of

demand as well as supply.

The recommendation itself is concerning for four primary reasons:

I. There is insufficient justification as to how this will add value. There are vague statements about meeting the SSRO's objectives of value for money to the Government and a fair return to industry without specifying how this will be delivered. For example, there is no reference to any added value to industry and the summation of the benefit to the MoD is that there will be more data available, but data on its own is not valuable. There needs to be clarity on how it will be utilised.
II. Related to this is the view that the underlying area of concern for the SSRO is that they do not believe they have sufficient information available to identify if a contract is compliant with the regulations. This is primarily due to the absence of a formal definition of what constitutes 'sufficient evidence' under the regime, rather than the ability to access information. If more thought was placed to defining what evidence is required, and the regulations or guidance adjusted accordingly, then the SSRO would receive all the information needed to assess compliance as the contractor would be required to submit this under the standard reporting obligations.
III. The SSRO appear to minimise the costs that industry and the MoD will incur through having to provide information requested on an ad hoc basis. The point is not that information is not currently available, although this may be the case, but a misunderstanding of process efficiency. Reporting by exception through changing the way data is extracted, cut, presented etc., is much more inefficient and costly than that produced through standard processes. We would suggest the SSRO review what information it currently lacks, define what is needed (if anything) and adjust the current reporting requirements to capture the data to enable industry and the MoD to work out the most efficient way to deliver this.
IV. The recommendation to give the SSRO powers to enforce the significant penalties established within the regulations for not providing ad hoc information (which by definition is not deemed important enough to be included in the regular reporting processes), seems wholly inappropriate and excessive. It is important that the SSRO remain impartial and adoption of this recommendation would jeopardise this.

There also appears to be a continuing move to duplicate information and responsibilities between the SSRO and the MoD. The SSRO has duties under the Regulations (including this regulatory review), but there is no desire by either industry or the MoD to expand the Regulations or the role of the SSRO. To be clear, it is the duty of the MoD to deliver value for money to the taxpayer across all of its supply chain, whether within or without the SSCR, and which it continues to do through its commercial teams. The MoD already has significant rights for information and if this is not sufficient, they can impose further rights within their contracts. In line with the above information, there is no clear justification why the SSRO needs to change the Regulations to have access to more information. If it is for the MoD, they have the capacity to do that for themselves and industry does not see any benefit in the provision of further information where no benefit has been identified. In fact, the production of requested information outside of the current legal requirement for reporting would be likely to incur a cost (possibly significant) for the Contractor and this would need to be funded by either the SSRO or MoD.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

As highlighted in the answer to section 10 above, we make two suggestions as to how the SSRO could ensure it has access to the information it needs to meet is regulatory requirements.

I. Define what is meant by 'sufficient evidence' so that contractors (and the MoD) are fully aware of what is required by the SSRO in terms of providing an evidence base to support compliance
II. Identify any gaps in data needed and include them within the suite of regular reports. This will ensure the SSRO gets the information it needs, gives clarity to contractors as to what they need to record and monitor, and will enable parties to set processes in place to efficiently gather this information.

We also reiterate our initial point, on why this is needed and for what benefit. If the SSRO addresses the two points above, they have all the powers they need to get the information needed to ensure compliance with the SSCR. Anything beyond that needs a clear justification and rationale as to why it needs to be included in regulation rather than being data provided to the MoD through contractual requirements.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

We would agree that it is appropriate that the SSRO be able to receive referrals on these items, notwithstanding our reservations on the current baseline profit rate methodology.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

We wholly disagree with this recommendation. We are of the belief that it is vitally important that there is a segregation of compliance monitoring and penalty enforcement between the MoD and the SSRO. The SSRO recognise in their recommendation that having enforcement powers, whilst retaining the role of adjudicating party for SSCR issues, can affect its objectivity. The recommendation to have a separate panel for referrals on penalty issues merely adds another layer of regulation and complexity where it is not required.

The SSRO needs to retain its independence to monitor and assess compliance within the regime. The MoD, as the representative of the Government and ultimately the taxpayer, needs to balance the potentially competing requirements of assuring defence capabilities and delivering value for money. In paragraph 12.11 the SSRO appear to recognise that the MoD needs to maintain good working relationships with suppliers, but do not seem to place enough emphasis on it. The SSRO does not have the same 'skin in the game' that the MoD has and so may make decisions on enforcement that will have unintended consequences for UK defence capabilities, particularly with regard to overseas defence suppliers, who may not place the same significance on the UK defence market. The SSRO should not assume that a third

party issuing notices or fines at arm's length will enable the MoD to better manage their relationships. The danger is not only the association between the MoD and customers if a fine is issued, but also whether the contracting parties consider the UK defence market to be an attractive market to remain within. This latter point is where the MoD is more likely to be sensitive due to its obligations to ensure ongoing defence capabilities, whilst the SSRO would be more inclined to take binary decisions, without due reference to factors outside of the SSCR, as their remit is just to enforce compliance with the Regulations.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

In line with our earlier responses we cannot see which functions the SSRO believe they cannot discharge. We believe the UK single source procurement regulations are credible as they stand, but we are concerned with ensuring that the MoD retains the appropriate flexibility and supply chain to ensure UK defence capabilities are retained and that industry is incentivised and rewarded appropriately for delivering such work.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

The only additional comments we would like to make are:
- We welcome the desire by the SSRO to analyse the benefits to any changes they have suggested, however we note there are no benefits identified which meet the SSRO's obligation to deliver fair and reasonable prices. We also cannot see how any of these recommendations deliver value for money. Again it is important to emphasise that value for money is wider than merely implementing price and cost controls. Value for money needs an assessment of quality of output and there needs to be consideration of the wider economic and capability consequences, hence the need to ensure fairness to industry within the regulations.
- In addition, the benefits identified need to be quantifiable and specific in regards to the issue they are trying to address. Meeting compliance requirements is very important, but it is different from delivering additional value.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

In previous consultation or 'call for input' responses we have stated that we are comfortable with the exclusion of government-to-government contracts, in order to ensure that the UK is able to meet its defence obligations. The one concern we have raised is that foreign suppliers should not be given competitive advantages through these arrangements at the cost to the UK defence industry, but we are comfortable that the UK Government is cognisant of this issue.

17. Issues raised concerning enforcement of price control (section 15).

There is no clear argument as to why the SSRO is looking at the option of initiating determinations or opinions rather than awaiting referrals. The key reasons appear to be based on an assessment of the level of referrals to the SSRO, which are deemed to be low, but there is no baseline upon which to judge this. The section suggests it would be helpful to enable the SSRO to enforce the regulations, but it is not explained

how this extra power would deliver anything more than the SSRO already has in terms of raising compliance issues if they become aware of them, or providing further clarity over the regime through the publication of guidance.

It is also not clear how the SSRO expect to identify any issues. Section 15.10 suggests that they would not need to be party to negotiations to identify issues. However, this would be the only way they would be able to understand specific issues with regard to contracts before contract agreement (in order to make a determination). If they are seeking to identify more general issues, this is best handled through changes to guidance rather than choosing a potential contract and deciding to make a determination on it, without being party to the ongoing discussions. If they are seeking to address the potential to make an opinion, it is not clear how they will discover issues without a referral. If the SSRO discovers something of concern within the information submitted to them under the regime, they currently have the powers to identify a compliance issue with the MoD, who can then choose to issue compliance or penalty notices.

This appears to be an attempt to gain more powers without clarity of what issue is to be addressed or what the benefits are of having the new powers.

18. The proposal for disapplying the price formula (section 17).

We would support the idea of disapplying the price formula in certain cases. The key point raised in section 17 is that there are qualifying contracts which source information from suppliers, who have market referenced prices or price lists.

The SSRO and MoD both recognise the importance of competition and that a competitive market delivers value for money by definition. To ignore the importance of this principle in this specific context would be inequitable and show inappropriate selectivity bias. If a supplier has a price for its products at which it sells to other consumers, then those are prices which deliver value by definition, as other parties clearly place enough value on the product to buy it. This needs to be recognised and the regulations adjusted to give scope to prevent the situation where the standard price formula needs to be applied. If it does not, then the MoD is highly likely to lose those items from its supply chain.

This is potentially a bigger issue than the SSRO appears to believe as the MoD have a number of equipment supply contracts with outsourced suppliers. These suppliers then manage the supply chain on the MoD's behalf, often with large numbers of small 'commodity' suppliers. Usually these contracts are let on a competitive basis by the MoD, but they might fall under the single source regime if there is an absence of sufficient competitors bidding.

We do not believe that these contracts should need to be referred to the SSRO as it should be a matter for the MoD and the contractor to agree when and where to disapply the pricing formula. We do agree this should be highlighted in any contract reporting. Both of these points would be in line with the 'comply or explain' self-certification regime the SSRO has stated they would prefer.

19. Stakeholder proposals supported by the SSRO (section 18).

We broadly agree with the document on this point. Our only comment is that we do not think it is necessary to submit a QMAC with the rates claim reports. The QMAC is already available to the MoD so this appears to be a duplication of work with no clear benefit.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

We would support the proposals to revisit the regulations in relation to repricing contracts on amendment. The largest issue is that contracts have historically been let with certain provisions outstanding e.g. agreement on rates. The contracts usually specify that these items are to be agreed subsequent to signing and the contract updated afterwards. The implementation of these contractual terms is often done by contract amendment. These amendments however do not change the scope or intent of the contract, but merely implement the agreed terms and the original intention of the parties. The regulations, as currently worded, create an ambiguity that could be interpreted as requiring a repricing exercise once these outstanding terms are agreed. Aside from being against all normal contracting principles, whereby agreements on pricing are honoured throughout the contract, this needs to be addressed in order to prevent contracting grinding to a halt. The risk of having to reprice upon closure of any items finalised after signing means that parties will no longer agree to contracts unless all items have been closed out. This will be impractical in a significant number of cases.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

No further comments.

22. Other suggestions for amendments to the legislation.

We support the submission provided by ADS with regard to this.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

We support the SSRO's continuing drive for engagement across industry, the MoD and themselves. We believe that through these dialogues we should be able to address significant issues, and suggest that it might be appropriate to look at ways to formally table and agree issues at such forums, provided there is sufficient early visibility of items, a quorum of attendance and agreement by all parties.

Consultation response - the Boeing Company

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Michael Hayes***
Organisation: ***The Boeing Company***
Position: ***Commercial Director, Boeing Defence UK Ltd***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☐	Defence contractor with QDC/QSC
☑	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
	Other, please specify:

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes.
The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

1. BDUK is mindful that the regulatory framework has only been operative for a little over two years and that the rules have been applied to only a comparatively small number of Qualifying Defence Contracts (QDCs) or Qualifying Sub Contracts (QSCs) awarded. Additionally, the number of contractors and subcontractors with experience of performing these types of contracts is also still comparatively small. Overall, experience with the regulatory framework is still limited and there are a number of aspects e.g. completion and post completion activities, and enforcement where there is no experience at all as these aspects have yet to be tested. BDUK feels that on balance, the transparency provided by the current regime gives adequate exposure of single source procurement decisions and notes that the consultation document does not offer any evidence that there is insufficient transparency. It also feels that what are described in paragraph 10.2 as limitations are proportionate and appropriate components of the regulatory regime. BDUK believes that the regulatory regime in its current form already gives the SSRO access to the information it requires to discharge its statutory duties and its intended purpose.

2. BDUK notes that the consultation document does describe or offer any evidence that initiatives aimed at promoting competition or increasing innovation or monitoring the involvement of SMEs in will improve either the delivery of value for money in government procurement or the certainty that suppliers will receive a fair and reasonable prices. It also notes that MOD (and wider government) already has significant initiatives in this area and that introducing further requirements or reporting in this area is likely to duplicate work already being done elsewhere. For these reasons BDUK does not support modifying the regulatory framework on the basis suggested.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

1. BDUK does not support the proposal to amend the Act or Regulations, or both, that provides for a contract amendment of £5M or greater to be automatically considered to be a material amendment and accordingly be treated as if a new contract has been entered into for the purpose of the Act and Regulations. BDUK believes the proposed amendment is unnecessary on the following grounds:
a. Materiality in the context of contract amendments is dealt with adequately in contract and case law and there is no need to introduce another definition or threshold.
b. The amendment would represent a major policy change from a free agreement between the parties being required to convert the contract to a QDC.
c. There is a significant chance that the proposed change if introduced would destabilise the contract and the 'deal' that was made at the outset.
d. There is no evidence that there is a fundamental problem that this proposal is correcting.

2. These issues have been discussed at length between MOD, Industry and the SSRO in recent tripartite meetings. BDUK agrees that the concept of severability in Reg. 14(2) is unhelpful and it should be removed. At the same time, it is recognised that it is the attributes of the amendment that are key to determining whether or not the whole contract should be repriced. BDUK believes that in all but a few cases, the estimated allowable costs associated with a contract amendment effect will be identifiable, and that the only circumstances where a change to the contract profit rate may be considered is if the amendment results in a significant change in the allocation of risk.

3. BDUK believes that further work is required to determine the extent and form of the changes required to Reg. 14 and the requirement for new or amended guidance for deciding whether or not the whole contract profit rate should be amended. In particular, issues of repricing existing work and the profit rate to be applied as part of the repricing, and the extent to which Steps 2-6 are applied, need further discussion.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

1. BDUK supports the proposed change at paragraph 6.13 in principle based on a free agreement to a QDC on amendment, but requires clarification of the following:
a. What is meant by 'committed' costs and associated profit (sunk costs). If this was taken to mean that it referred to MOD's commitment to the contract scope immediately prior to the amendment (whether discharged or future work by the contractor) then the proposed change would be supported by BDUK.
b. How would a change in pricing methodology on amendment be considered in relation to actual costs incurred immediately prior to the amendment.
c. The extent of reporting on the contract that becomes a QDC on amendment. BDUK believes this should be limited to the new scope with limited reporting (e.g. lump sums) on the original scope prior to the amendment. An exception to this would be in circumstances where the whole contract was repriced.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

1. BDUK supports the provision of guidance that would clarify the rules for determining the conditions and timing under which a potential subcontract would become a QSC.

2. BDUK does not support the proposal in paragraph 7.20 that a contract may be a QSC if it provides anything for a proposed QDC or QSC. BDUK feels that §29(3) and §29(4) recognise Parliament's intentions in this area and provide adequate anti-avoidance measures.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

1. BDUK would support removing the 20 contract restriction provided that the requirement was limited to potential subcontracts with a value of £25M or greater.

2. Major subcontracts will be identified prior to contract award and appear in the Contract pricing Statement. It is, however, recognised that additional potential QSCs may be identified during the contract delivery phase and where this occurs, BDUK believes new QSCs should be notified within 30 days of subcontract award.

3. BDUK does not believe there is any merit in notifying unreported outcomes or negative assessments and that reporting should continue to be by exception as in the outcome of the vast majority of assessments will be self-evident i.e. the subcontract was awarded on the basis of competition. The consultation document confines itself to speculating that there is an issue without offering any firm evidence that the is a problem that needs solving.

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

1. BDUK is mindful that to date, there has been only a small number of QSCs awarded and feels that this sample is too small to judge the effectiveness of the current regime. BDUK also believes that it is also still too early to form a view on whether the current requirements which place the onus on the Contractor (or contracting authority) to demonstrate that QSC's costs are AAR and that profit has been applied appropriately are not working or that there is some other form of problem that needs solving. Before supporting any proposal to lower the QSC threshold, BDUK would like to see a validated cost/benefit analysis which demonstrated the benefits that the parties would accrue from the change any other information to support the recommendations.

2. Whilst the consultation document offers no evidence that lowering the threshold will result in meaningful benefits to any of the parties or that it will increase the likelihood of MOD securing better value for money from its purchases or improve the prospects for subcontractors receiving a fair and reasonable price, it will create a significant administrative burden and additional costs for subcontractors. It is felt that reducing the threshold from £25M to £10M may result in some companies for whom defence is only a small or marginal part of their business exiting the market rather than shouldering the additional administrative burden and cost of undertaking QSCs. This will disrupt supply chains and may jeopardise security of supply for critical components.

3. There is also a practical consideration that needs to be taken into account in that responsibility for agreeing prices on QSCs lies with MOD and not the contracting authority. Lowering the threshold in the manner proposed would result in a significant increase in the number of subcontracts and sub-subcontracts (and possibly sub-sub-subcontracts) coming within the regulatory framework. The needs to be certainty that MOD has resources required to price the additional contracts within a reasonable timeframe before lowering the threshold otherwise there is a danger of disrupting supply chains and programmes.

4. As a counter proposal BDUK suggest that the QSC threshold should be raised to that of the GBP equivalent of the EU definition of an SME (EUR50M).

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

1. Intelligence Activities: BDUK does not support the proposal to bring any single source contracts wholly for the purposes of intelligence activities under the regulatory framework. The reason for BDUK's position is that disclosure may put at risk aspects of national security and wider political contexts than just the operational aspects.

2. BDUK is also sensitive to the fact that information held by the SSRO may be subject to release under the Freedom of Information Act (FOIA). Whilst the FOIA contains a number of exemptions including §24 National Security and §27 International Relations exemptions BDUK considers that even using these defences to prevent a release of information would in itself give the information an unwelcome profile and potentially harm either national security, international relations or both.

3. BDUK would, however, be minded to support a proposal that single source contracts for Intelligence Activities where brought under the regulatory regime if there was an exclusion for those contracts where knowledge of the fact that MOD was procuring a particular type of goods or service or a combination of both would jeopardise either national security or international relationships. In making this suggestion BDUK recognises that there must be a process for providing safeguards to ensure the exemption is used only in appropriate circumstances. The ultimate decision on this should, however, always lie with MOD.

4. International Co-operative Defence Agreements: BDUK recognises that the drafting of Regulations 7 and 58(2) created uncertainty. Particular issues requiring clarification are: contracts where only part of the output relates to an international programme; programmes where a significant proportion is procured on a bilateral arrangement and the remainder under a Memorandum of Understanding (MOU); quantities procured as part of an international workshare vs a follow-on buy solely for the UK.

5. These issues have been reviewed in outline during recent tripartite discussions and BDUK believes further work is required to ensure any amendment to the regulatory regime covers all the likely scenarios, and provides a comprehensive solution and clarity on the boundaries of the exclusion and any safeguards to prevent its misuse.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

1. BDUK believes that all single source contracts and their single source subcontracts are already subject to the regime, albeit this may be indirectly. Those contracts and subcontracts which are not priced directly under the regulatory framework are subject to the provisions of MOD's 810 series DEFCONs. These contract conditions provide a proxy for the regulatory framework and are used in single source contracts with values <£5M, their single source subcontracts, and single source subcontracts with values <£25M required to enable the performance of QDCs.

2. BDUK considers that the pricing requirements contained in the 810 series DEFCONs and the associated project reporting requirements provide adequate assurance that value for money in government single source contracts not covered by the regulatory regime will be achieved and that simultaneously, suppliers will receive a fair and reasonable price. It is unnecessary to extend the scope of the DRA and SSCRs to include single source contracts and subcontracts described above.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

1. BDUK does not support the proposed amendment as it believes that the powers given to the SSRO by the Act and Regulations provide access to information sufficient to enable it to perform its statutory obligations. MOD has open book access for all of their requirements.

2. In circumstances where the SSRO seeks access to a contractor's private information additional to that which it is required to provide under the regulatory framework as part of a study it is performing on behalf of the Secretary of State or to its own account, BDUK believes the onus is on the SSRO to establish prior to committing to the study that:
a. The contractor holds or is able to generate the information required.
b. Its willingness to divulge its private information and any conditions it may attach to the disclosure e.g. requiring a direct confidentiality agreement between itself the SSRO, limits on the uses which may be made of the information or further disclosure (including within government).

Key to achieving access to the information will be the trust, respect and the relationship the SSRO is able to establish with contractors.

3. If access to a contractor's private information is essential for a task being performed, the SSRO should first canvas MOD to use its Open Book rights to obtain the information.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

See 10.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

1. BDUK believes that Section 11 of the consultation document does not make a clear case that there is a problem to be solved as the arguments presented are based on speculation about conditions that may or may not occur at some time in the future. BDUK considers that the requirements in the Act and Regulations regarding these aspects are stated clearly and unambiguously.

2. BDUK also considers that inexperience may lie at the heart of the examples reported in the consultation document and that as MOD and suppliers become more familiar with the regulatory regime and understanding of its requirements grows, these will not be seen as issues requiring changes to either the Act or the Regulations.

3. Notwithstanding the above, BDUK believes there is merit in exploring the proposal further with a view to identifying the best method of providing guidance to which contracting parties may refer when establishing the rates to be used for steps 1-6, and determining whether or not a contract is a QDC or QSC.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

1. BDUK strongly disagrees with the proposal that the SSRO should be given powers to issue compliance notices or any right to enforce penalties. The Act clearly establishes MOD as the enforcement body and the SSRO as an independent and impartial arbiter that can give opinions and make determinations in a set of clearly defined circumstances. Giving the SSRO the suggested powers would completely undermine it primary function and represent a major shift in policy. It would in effect become the prosecutor, judge and jury whose powers would be asymmetric as it would have no right of sanction against MOD. BDUK supports the existing process which it believes is adequate and allows MOD to assess the intent behind any non-compliance and its materiality before issuing a compliance or penalty notice.

2. The consultation document does touch on the problems contractors and subcontractors have with the reporting regime. Notwithstanding that the regime is still comparatively new and that experience in completing and submitting reports is

still comparatively limited, it is clear that there are a number of aspects of the reports and report formats where the requirement is unclear and contractors are having difficulty understanding what information it is required to provide and when. BDUK suggests that the reporting regime and the report format are subject to a detailed tripartite review aimed at ensuring:
a. The information being provided is valuable and has an impact on the way the project and future projects are priced and managed and
b. Reporting requirements are clearly stated and readily understandable.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

1. BDUK believes the regulatory framework reflects the government's intentions with regards to referrals and enforcement and it is not clear what the problem is that the proposal are seeking to solve. It is appropriate that the SSRO should only give opinions and make determinations when asked to by one or both of the parties. BDUK does not support the proposal that the SSRO should be able to initiate opinions or determinations as this will put it on the 'field of play' and undermine its impartiality and independence.

2. The proposal(s) to give the SSRO additional powers is based on supposition of what might happen at some future time. BDUK believes this is an insufficient basis on which to proceed, and that the SSRO already has adequate powers to discharge its functions and statutory obligations in a manner that makes single source procurement a credible alternative to competition. Giving the SSRO additional powers in the manner suggested would represent a significant shift in its role and government policy.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

No response.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

1. BDUK does not agree with the statement in paragraph 14.2 of the consultation document that that for FMS procurements, the overseas government is effectively acting as an agent. In this type of procurement, the UK government places an order with the overseas government for the supply of a specified type of equipment (or service) used by the overseas government. The overseas government then procures the equipment (or service) from its indigenous supplier for delivery to the UK government. The order placed on the indigenous supplier will be subject to the overseas government's rules for single source contracts. In the case of the US FARs/DFARs, these are internationally well known and respected regulations. BDUK believes application of the local single source pricing regulations provides adequate assurance that value for money is obtained and removal of the exclusion for

government-to-government contracts is unnecessary.

2. Irrespective of the above, BDUK believes persuading an overseas government to instruct its supplier to open up its books will be unachievable and will require the overseas government's consent before the enforcement powers in the DRA could be enforced on an overseas supplier.

17. Issues raised concerning enforcement of price control (section 15).

1. BDUK does not support any assertion that the SSRO has a duty to enforce price controls or that the SSRO has a role in this area. SSRO's functions are stated in paragraph 1.3 of the consultation document, which does not include a reference to a duty to enforce price controls (and somewhat surprisingly omits a reference to the SSRO's duty to set the Baseline Profit Rate). The term price controls is one of the SSRO's own construction: contracts must be priced using the pricing formula and 'price control' has no meaning in this context.

2. The primary aims of the SSRO given in §13(2) are to ensure:
a. That good value for money is obtained in government expenditure on qualifying defence contracts, and
b. That persons other than the Secretary of State who are parties to the qualifying defence contracts are paid a fair and reasonable price under those contracts

The Act and Regulations are silent on the need to strike a balance between the objectives given above and do not imply that they have to be achieved simultaneously.

3. BDUK agrees with the statement in paragraph 15.3 of the consultation document that the primary responsibility for ensuring that pricing complies with the requirements of the regulatory framework (not with the pricing controls as stated) lies with the contracting parties. It also supports the policy contained within the regulatory framework whereby the SSRO does not have role to play in setting prices unless there is a dispute between the parties and one or both refer the dispute to the SSRO for an opinion or a determination. If at any time the SSRO believes a price may not have been set in accordance with the regulatory framework, it should refer to MOD in the first instance.

4. BDUK does not support any of the other changes suggested for the Act or Regulations outlined in section 15 on grounds that the SSRO functions are already adequately described by the regulatory framework and that the powers it has already been given are adequate for it to discharge its statutory functions.

18. The proposal for disapplying the price formula (section 17).

BDUK refers the SSRO to ADS' response, with which it agrees, in this area.

19. Stakeholder proposals supported by the SSRO (section 18).

BDUK refers the SSRO to ADS' response, with which it agrees, in this area.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

BDUK refers the SSRO to ADS' response, with which it agrees, in this area.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

BDUK refers the SSRO to ADS' response, with which it agrees, in this area.

22. Other suggestions for amendments to the legislation.

1. Experience with the regulatory framework to date has shown that contractors find its requirements are complex and difficult to understand. BDUK believes that this lies behind the majority of the non-compliance encountered to date. The changes to the detail of the regulatory framework proposed in the attached will improve this situation and as experience is gained, contractors will become more confident and better able to respond to reporting requirements. Notwithstanding this, BDUK believes it would be prudent to have the next review of the regulatory framework in three years' time and not five years.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

No response.

Consultation response - the Chartered Institute of Public Finance & Accountancy

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Gillian Fawcett***
Organisation: ***The Chartered Institute of Public Finance & Accountancy***
Position: ***Head of Governments Faculty***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☐	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
☑	Other, please specify: ***Not for profit***

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes.

The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

CIPFA supports the principle that when tendering contracts every opportunity should be taken to subject them to open competition. In our view single source contracts prevent competition and can potentially fail to secure value for money (VFM). However, we do acknowledge that in some specific instances there can be exceptions, such as for technical reasons or where a single supplier can only supply the services required. A number of defence contracts will fall into this category, as there are few suppliers with the necessary key industrial capabilities to develop the sophisticated equipment needed for our armed forces.

The size of expenditure £8.8 billion spent by the Ministry of Defence on single source contracts is significant, representing 45% of total procurement spend. Given the magnitude of expenditure delivered through single source procurement with inherent VFM risks, there is an even more compelling case for the suppliers and sub contractors of defence contracts to demonstrate value for money on costs, pricing and contract performance. Similar to other areas of public expenditure, single source contracts should be subjected to rigorous scrutiny by the SSRO and Parliament. The public will want to know that public money is being well spent irrespective of how defence equipment and services are procured.

Also, given that single source contracts are usually let to a few suppliers that dominate the defence market place, this has the potential to crowd out others, in particular SMEs. There is also a strong potential to stifle innovation. With this in mind, it is even more critical that the SSRO has the powers to have access to the relevant information on contract costs, pricing and performance to identify poor contract performance and inefficiencies. The SSRO, as an independent body, should have the powers to access this information and report in the public domain.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.

In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

No response.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

No response.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

No response.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

No response.

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

No response.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

No response.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

In our view all restrictions that create barriers to accountability and transparency on single source contracts for defence expenditure should be removed. The single source procurement framework should bring all single source contracts (without exception) into the framework, including agreements with foreign governments. All contracts should be examined and scrutinised by the SSRO. This change will ensure consistency with all other areas of public spending. The key benefits are that the public will have greater assurance about how money is spent on defence and the procurement process will be simplified providing greater clarity to the commissioner of defence equipment and the contractor.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However,

there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

In order to exercise effective scrutiny and oversight of procurement process for single source contracts, the SSRO should be given powers to access the information it needs to ensure these contracts will deliver value for money. In other areas of service delivery, regulators have the powers to request information. Ofgem, Ofcom and the Civil Aviation Authority are a few notable examples of regulators with such powers. Similarly, auditors have a statutory right to access documents and information from public bodies so that they can make an assessment about value for money. Giving the SSRO the same powers will only help to strengthen accountability and provide more rigour to the regulatory system for single source contracts, as well as introducing greater transparency and accountability.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

See comments in 10 above. The SSRO should be provided with the appropriate powers to access all data relating to the costs and pricing of single source contracts.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

Whilst self-regulation is an important part of any procurement process, it cannot be wholly relied on a lone. The risks are that the principles of good governance, such as objectivity and independence in the commissioning process can be undermined i.e. the Ministry may be less likely to challenge the supplier if it places the delivery of a significantly priced defence contract at risk. Equally, the Ministry may not want to enforce the demands for information for fear of undermining relationships with suppliers and subcontractors. There are of course many other examples, but from a good governance point of view it makes sense that the SSRO has a greater role in enforcement so that it can properly discharge its regulatory duties.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

See response to 12 above. The SSRO should have a greater role in enforcement which includes the issue of compliance and penalty notices.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

No response.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

No response.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

CIPFA can see no obvious rationale for why public money spent with overseas companies should not be regulated. Regulation should be about ensuring a level playing field, particularly where there is not a competitive market.

17. Issues raised concerning enforcement of price control (section 15).

To be an effective regulator you need to given the power to enforce price controls. There also needs to be basic processes in place that ensure the segregation of duties. It cannot be in the public interest to have the specifier of price be also the enforcer of price without effective regulation.

18. The proposal for disapplying the price formula (section 17).

No response.

19. Stakeholder proposals supported by the SSRO (section 18).

CIPFA believes that the SSRO should consider bringing in a requirement for the contractor's Chief Finance Officer to sign a certificate that all report costs are accurate and in line with good accounting and governance practice.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

No response.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

No response.

22. Other suggestions for amendments to the legislation.

No response.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

No response.

Consultation response - Marshall Aerospace and Defence Group

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Neil Goulding***
Organisation: ***Marshall Aerospace and Defence Group***
Position: ***Head of Commercial, Military Aerospace***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☑	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
	Other, please specify:

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes.
The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

Marshall ADG feels that there is very little objective evidence to date upon which to base an opinion on the need to modify the regulatory framework at this time. In broad terms, we would like to allow the framework to have sufficient time for a significant number of QDCs/QSCs to have been let and completed under the framework to see what that experience can teach us about the effectiveness of the current arrangement.

However in respect of the specific questions:

1. ***Marshall ADG understands that the existing framework has been designed to bring about greater transparency and we would wish to give the existing structure time to work to see what benefits are brought about to both MoD and Industry and use the evidence to consider further change before extending the arrangements.***
2. ***Marshall ADG would welcome steps designed to promote competition, innovation and competitiveness in general. Again, as there is little objective evidence about the effectiveness of the current framework, we would support waiting for the evidence before making a change.***
3. ***In terms of SME involvement, there are already initiatives in play such that making a change to this framework would involve duplication of effort and therefore incur unnecessary cost and on these grounds we would not support a change.***

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

1. ***Marshall ADG does not support this proposal. We do not believe that setting an arbitrary figure to determine materiality is appropriate. We also believe that this***

could fundamentally alter the bargain made between the parties at the point of contract award, which we do not support. This could have particular effect on long term contracts where amendments recognising later pricing periods were intended and reflected in the contract structure. We believe that contracting parties should honour their commitments.

2. ***The amendment would represent a major policy change which is that in the event of an amendment, agreement of the parties is required to convert the contract to a QDC. In order that a contract remains in place, requiring an agreement between the contracting parties, we believe it is key that any change in the nature of any contract must be agreed by the parties to that contract.***

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

1. ***Marshall ADG supports the proposed change at paragraph 6.13 in principle and up to a point. We believe that if such a change were to be enforced then only costs directly connected to the amendment should be subject to the regime. This would preserve the original contract as envisaged between the parties when it was signed and minimising the harm done to an existing bargain.***

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

1. ***Marshall ADG does not support the proposal in paragraph 7.20 that a contract may be a QSC if it provides anything for a proposed QDC or QSC as it is likely to create as much uncertainty as it is trying to solve. For example, it may result in a contract becoming a QSC i.e. a regulated contract, before the QDC which it will serve comes into existence. If the QDC does not come into existence then the QSC should not have been viewed as a QSC.***

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

1. ***Marshall ADG would support the removal of the current restriction but believes the value should be raised to a figure nearer the QSC threshold of £25M to ensure that only subcontracts near the QSC threshold are identified.***
2. ***Marshall ADG agrees that QSCs should be notified within 30 days of subcontract award.***
3. ***Marshall ADG does not agree with the proposal to include negative assessments in order to avoid excessive effort on subcontracts that are not applicable.***

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

Marshall ADG feels that there is very little objective evidence to date upon which to base an opinion on the need to modify the regulatory framework at this time. In broad terms, we would like to allow the framework to have sufficient time for a significant number of QDCs/QSCs to have been let and completed under the framework to see what that experience can teach us about the effectiveness of the current arrangement before expanding its scope.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

1. ***Intelligence Activities:*** ***Provided that sufficient safeguards are put in place to ensure that national security is always paramount, Marshall ADG supports this change in principle.***
2. ***International Co-operative Defence Agreements:*** ***Subject to this being drafted in such a way that it would be clear that this would not form an obstacle to UK Industry's participation in such programmes, Marshall ADG would support this change in principle.***

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

Marshall ADG believes that any single source contracts not brought within the regime could be procured in a way that demonstrates value for money by employing the same cost and pricing methods as used in the regime. This can be done through the DEFCONs (800 series for example) or through agreement between the parties to use these elements of the regime. It has an advantage to both parties to have a common understanding based on a regime that is being regularly reviewed. If the legislation does not demand inclusion, it is clearly not a priority but may be a useful tool that contracting parties may adopt.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

Marshall ADG does not support the proposed amendment and believes the same result can be achieved via other means. If the data is sensitive, it could ask MoD to procure the information via its data rights under the Act. If the data is not sensitive, SSRO could focus on building and improving collaborative relationships with Industry that would lead to Industry voluntarily sharing this data on request.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

Please see the response to number 10 above.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

It is not clear to us that there are specific problems to overcome based on experience to date. For these reasons, we would not support the proposal at this time.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

Marshall believes it is critical that the SSRO does not gain these powers. The SSRO needs to remain above any potential disputes between MoD and Industry as a neutral third party that can be relied upon to act with complete impartiality. Giving the SSRO powers to decide who to pursue and then to apply a sanction, all without any external oversight, would be a clear extension of powers beyond those originally envisaged and would damage the standing of the SSRO as an independent body.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

Marshall ADG feels that there is very little objective evidence to date upon which to base an opinion on the need to modify the regulatory framework at this time. In broad terms, we would like to allow the framework to have sufficient time for a significant number of QDCs/QSCs to have been let and completed under the framework to see what that experience can teach us about the effectiveness of the current arrangement before expanding its scope.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

Please see our response to number 14 above.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

Our understanding of the use of government-to-government contracts is that these contracts will have already been assessed by the supporting government for value for money in accordance with that nation's single source framework. It is highly likely that different nations will have a degree of variance in their respective frameworks and that this is something that needs to be respected. For these reasons, we do not support changes to the current framework.

17. Issues raised concerning enforcement of price control (section 15).

Marshall ADG believes that the SSRO's duties and responsibilities as laid out in the Act are achievable with the rights it already enjoys. Marshall ADG feels that there is very little objective evidence to date upon which to base an opinion on the need to modify the regulatory framework at this time. In broad terms, we would like to allow the framework to have sufficient time for a significant number of QDCs/QSCs to have been let and completed under the framework to see what that experience can teach us about the effectiveness of the current arrangement before expanding its scope.

18. The proposal for disapplying the price formula (section 17).

Please see our response to number 14 above.

Marshall ADG supports the possible amendment and its use in the limited circumstances described.

19. Stakeholder proposals supported by the SSRO (section 18).

Marshall ADG feels that there is very little objective evidence to date upon which to base an opinion on the need to modify these sections of the regulatory framework at this time. In broad terms, we would like to allow the framework to have sufficient time for a significant number of QDCs/QSCs to have been let and completed under the framework to see what that experience can teach us about the effectiveness of the current arrangement before taking a view on these proposed changes.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

Marshall ADG feels that there is very little objective evidence to date upon which to base an opinion on the need to modify these sections of the regulatory framework at this time. In broad terms, we would like to allow the framework to have sufficient time for a significant number of QDCs/QSCs to have been let and completed under the framework to see what that experience can teach us about the effectiveness of the current arrangement before taking a view on these proposed changes.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

Marshall ADG feels that there is very little objective evidence to date upon which to base an opinion on the need to modify these sections of the regulatory framework at this time. In broad terms, we would like to allow the framework to have sufficient time for a significant number of QDCs/QSCs to have been let and completed under the

framework to see what that experience can teach us about the effectiveness of the current arrangement before taking a view on these proposed changes.

22. Other suggestions for amendments to the legislation.

Marshall ADG has nothing to add in this regard.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

Marshall ADG has nothing to add in this regard.

Consultation response - MBDA UK Ltd

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***ADRIAN DOE***
Organisation: ***MBDA UK Ltd***
Position: ***HEAD OF PROGRAMMES COMMERCIAL OPERATIONS***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☐	Defence contractor with QDC/QSC
☑	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
	Other, please specify:

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes.
The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

1. We recognise that the regulatory framework has only been operative for a little over two years and that the rules have been applied to only a comparatively small number of Qualifying Defence Contracts (QDCs) or Qualifying Sub Contracts (QSCs) awarded. Additionally, the number of contractors and subcontractors with experience of performing these types of contracts is also still comparatively small. Overall, experience with the regulatory framework is still limited and there are a number of aspects e.g. completion and post completion activities, and enforcement where there is no experience at all as these aspects have yet to be tested.

On balance, the transparency provided by the current regime appears to give adequate exposure of single source procurement decisions and we note that the consultation document does not offer any evidence that there is insufficient transparency. We also feel that what are described in paragraph 10.2 as limitations are proportionate and appropriate components of the regulatory regime. MBDA UK Ltd believes that the regulatory regime in its current form already gives the SSRO access to the information it requires to discharge its statutory duties and its intended purpose.

2. We note that the consultation document does not describe or offer any evidence that initiatives aimed at promoting competition or increasing innovation or monitoring the involvement of SMEs in will improve either the delivery of value for money in government procurement or the certainty that suppliers will receive fair and reasonable prices. We also note that MOD (and wider government) already have significant initiatives in this area and that introducing additional requirements or reporting in this area is likely to duplicate work already being done elsewhere. For these reasons MBDA UK Ltd does not support modifying the regulatory framework on the basis suggested.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

1. We do not support the proposal to amend the Act or Regulations or both in manner that if a contract amendment is £5M or greater it will be considered to be a material amendment and automatically be treated as if a new contract has been entered into for the purpose of the Act and Regulations. We believe the proposed amendment is unnecessary on the following grounds:

a. Materiality in the context of contract amendments is dealt with adequately in contract and case law and there is no need to introduce another definition or threshold.
b. The amendment would represent a major policy change which is that in the event of an amendment, agreement of the parties is currently required to convert the contract to a QDC. Removal of the need for agreement by the parties to the contract appears, to us, to run contrary to the norms required under English Law for the establishment of a contract.
c. There is a significant possibility that the proposed change if introduced would destabilise the contract and the bargain that was made at the outset.
d. There is no evidence that there is a problem or issue which this requirement is correcting.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

1. We would support the proposed change at paragraph 6.13 in principle, however, we believe some clarification of the following is necessary:

a. What is meant by 'committed' costs and associated profit (sunk costs). If this was taken to mean that it referred to MOD's commitment to the contract scope immediately prior to the amendment (whether discharged or future work by the contractor) then the proposed change would be acceptable.
b. How a change in pricing methodology on amendment would be considered in relation to actual costs incurred immediately prior to the amendment.
c. The extent of reporting on the contract that becomes a QDC on amendment. We believe this should be limited to the new scope with limited reporting (e.g. lump sums) on the original scope prior to the amendment. An exception to this would be in circumstances where the whole contract was repriced.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

1. We do not support the proposal in paragraph 7.20 that a contract may be a QSC if it provides anything for a proposed QDC or QSC as it is likely to create as much uncertainty as it is trying to solve. For example, it may result in a contract becoming a QSC i.e. a regulated contract, before the QDC which it will serve comes into existence. It is recognised that there is potential for avoidance, however, we feel that §29(3) and §29(4) recognise Parliaments intentions in this area and provide adequate anti-avoidance measures. However, it would be helpful if there was guidance available to the parties that would define the rules for determining the conditions for when it becomes apparent a potential subcontract will become a single source contract and potentially a QSC.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

1. We would support removing the 20 contract restriction provided that the requirement was limited to potential subcontracts with a value of £20M or greater. This will ensure that potential subcontracts near the QSC threshold are identified and deter inappropriate assessments of subcontract values.
2. Many major subcontracts will be identified prior to contract award and appear in the Contract pricing Statement. It is, however, recognised that additional potential QSCs may be identified during the contract delivery phase and where this occurs, we believe new QSCs should be notified within 30 days of subcontract award.
3. We do not believe there is any merit in notifying unreported outcomes or negative assessments and that reporting should continue to be by exception as the outcome of the vast majority of assessments will be self-evident e.g. the subcontract was awarded on the basis of competition. The consultation document appears to confine itself to speculating that there is an issue without offering any firm evidence that a problem actually exists.

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

1. We appreciate that, to date, there have been only a small number of QSCs awarded and feel that this sample is too small to judge the effectiveness of the current regime. We also believe that it is also too early to form a view on whether the current requirements which place the onus on the Contractor (or contracting authority) to demonstrate that QSC's costs are AAR and that profit has been applied appropriately are not working or that there is some other form of problem that needs resolution. Before supporting any proposal to lower the QSC threshold, we would like to see a validated cost/benefit analysis which demonstrated the benefits that the parties would accrue from the change.

2. Whilst the consultation document offers no evidence that lowering the threshold will result in meaningful benefits to any of the parties or that it will increase the likelihood of MOD securing better value for money from its purchases or improve the prospects for subcontractors receiving a fair and reasonable price, the suggested change will create a significant administrative burden and additional costs for subcontractors and MOD. It is felt that reducing the threshold from £25M to £10M may result in some companies for whom defence is only a small or marginal part of their business exiting the market rather than shoulder the additional administrative burden and cost of undertaking QSCs. This will disrupt supply chains and may jeopardise security of supply for critical components.

3. There is also a practical consideration that needs to be taken into account which is that responsibility for agreeing prices on QSCs lies with MOD and not the contracting authority. Lowering the threshold in the manner proposed would result in a significant increase in the number of subcontracts and sub-subcontracts (and possibly sub-sub-subcontracts) coming within the regulatory framework. There needs to be certainty that MOD has resources required to price the additional contracts within a reasonable timeframe before lowering the threshold otherwise there is a danger of disrupting supply chains and programmes.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

1. Intelligence Activities: We recognise the origin of the wording used in the Act to describe the grounds for this particular exclusion and that a different definition may be appropriate – however, this is strictly a matter for Government and whilst we would be prepared to engage in further discussions on the subject, any change can only be made with the positive assent of MOD.

2. International Co-operative Defence Agreements: We recognise that the drafting of Regulations 7 and 58(2) has created some uncertainty. Particular issues requiring clarification are: contracts where only part of the output relates to an international programme; programmes where a significant proportion is procured on a bilateral arrangement and the remainder under a Memorandum of Understanding (MOU); quantities procured as part of an international workshare versus a follow-on buy solely for the UK.

3. These issues have been reviewed in outline during recent tripartite discussions and we support the view that further work is required to ensure any amendment to the regulatory regime covers all the likely scenarios appropriately, and provides a comprehensive solution and clarity on the boundaries of the exclusion and any safeguards to prevent its misuse. It should also be borne in mind in those further discussions that even where a further "UK Only" purchase of a product originally developed by a multi-national contract is undertaken the price of that further purchase may well have a dependency that reaches back to the original construct.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

1. It is our experience for the types of contracts envisaged in the question that CAAS are fully engaged, that the question of affordability will always exist and that contractors will respond appropriately to the price investigation process

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

1. We do not support the proposed amendment as we believe that the powers given to the SSRO by the Act and Regulations provide access to information sufficient to enable it to perform its statutory obligations. MOD has open book access for all of their requirements.

2. In circumstances where the SSRO seeks access to a contractor's private

information additional to that which it is required to provide under the regulatory framework as part of a study it is performing on behalf of the Secretary of State or to its own account, we believe the onus is on the SSRO to establish prior to committing to the study:

a. That contractors hold or are able to generate the information required.
b. The willingness of contractors to divulge private information and any conditions they may attach to the disclosure e.g. requiring a direct confidentiality agreement between themselves and the SSRO, limits on the uses which may be made of the information or further disclosure (including within government).

3. If access to a contractor's private information is essential for a task being performed, the SSRO should canvas MOD to use its Open Book rights to obtain the information.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

Please see above.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

1. Section 11 of the consultation document does not make a clear case that there is a problem to be solved as the arguments presented are based on speculation about conditions which may or may not occur at some time in the future. We consider that the requirements in the Act and Regulations regarding these aspects are stated clearly and unambiguously albeit they are complex and difficult for the non-specialist to understand.

2. We also consider that inexperience may lie at the heart of the examples reported in the consultation document and that as MOD and suppliers become more familiar with the regulatory regime and understanding of its requirements grows, these will not be seen as issues requiring changes to either the Act or the Regulations.

3. Notwithstanding the above, we believe there is merit in exploring the proposal further with a view to identifying the best method of providing guidance that the contracting parties can refer to when establishing the rates to be used for steps 1-6, and determining whether or not a contract is a QDC or QSC.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

1. We disagree with the proposal that the SSRO should be given powers to issue compliance notices or any right to enforce penalties. The Act clearly establishes MOD as the enforcement body and the SSRO as an independent and impartial arbiter that can give opinions and make determinations in a set of clearly defined circumstances. Giving the SSRO the suggested powers would completely undermine its primary function and represent a major shift in policy. It would in effect become the prosecutor, judge and jury whose powers would be asymmetric as it would have no right of sanction against MOD. We support the existing process which we believe is adequate and allows MOD to assess the intent behind any non-compliance and its materiality before issuing a compliance or penalty notice.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

1. We believe the regulatory framework reflects the government's intentions with regards to referrals and enforcement and it is not clear what the problem is that the proposals are seeking to solve. It is appropriate that the SSRO should only give opinions and make determinations when asked to by one or both of the parties. We do not support the proposal that the SSRO should be able to initiate opinions or determinations as this will undermine its impartiality and independence.

2. The proposal(s) to give the SSRO additional powers is based on supposition of what might happen at some future time. We believe this is an insufficient basis on which to proceed, and that the SSRO already has adequate powers to discharge its functions and statutory obligations in a manner that makes single source procurement a credible alternative to competition. Giving the SSRO additional powers in the manner suggested would represent a significant shift in its role and government policy.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

No response

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

Clearly this is not a matter with which we are directly concerned and is strictly an issue for government and the MOD to consider.

17. Issues raised concerning enforcement of price control (section 15).

1. We do not support any assertion that the SSRO has a duty to enforce price controls or that the SSRO has a role in this area. SSRO's functions are stated in paragraph 1.3 of the consultation document (which does not include a reference to a duty to enforce price controls). We would also query the use of the term "price controls": Contracts subject to the regime must be priced using the pricing formula and 'price control' has no meaning in this context.

2. The primary aims of the SSRO given in §13(2) are to ensure:

a. That good value for money is obtained in government expenditure on qualifying defence contracts, and
b. That persons other than the Secretary of State who are parties to the qualifying defence contracts are paid a fair and reasonable price under those contracts.

The Act and Regulations are silent on the need to strike a balance between the objectives given above implying that they have to be achieved simultaneously.

3. We agree with the statement in paragraph 15.3 of the consultation document that the primary responsibility for ensuring that pricing complies with the requirements of the regulatory framework (not with the pricing controls as stated) lies with the contracting parties. It also supports the policy contained within the regulatory framework whereby the SSRO does not have a role to play in setting prices unless there is a dispute between the parties and one or both refer the dispute to the SSRO for an opinion or a determination. If at any time the SSRO believes a price may not have been set in accordance with the regulatory framework, it should refer to MOD in the first instance.

4. We do not support any of the other changes suggested for the Act or Regulations outlined in section 15 on the grounds that the SSRO functions are already adequately described by the regulatory framework and that the powers it has been given are adequate for it to discharge its statutory functions.

18. The proposal for disapplying the price formula (section 17).

1. The issues raised under these headings, together with a number of other issues identified by Industry, have been discussed in detail at recent tripartite meetings. During the course of these discussions a number of items have been identified as priority items needing to be addressed and proposed changes to the regulatory framework made as part the recommendations due to be submitted to Secretary of State in June 2017. Other items have been classed as being of lesser importance or urgency which can be addressed between June and December 2017 by either changes to the Regulations or in Guidance (statutory or otherwise). A small number of items have been discontinued. Although described as lesser important/urgent items, many of which are technical in nature, we believe they do require resolution.

19. Stakeholder proposals supported by the SSRO (section 18).

The issues raised under these headings, together with a number of other issues identified by Industry, have been discussed in detail at recent tripartite meetings. During the course of these discussions a number of items have been identified as priority items needing to be addressed and proposed changes to the regulatory framework made as part the recommendations due to be submitted to Secretary of State in June 2017. Other items have been classed as being of lesser importance or

urgency which can be addressed between June and December 2017 by either changes to the Regulations or in Guidance (statutory or otherwise). A small number of items have been discontinued. Although described as lesser important/urgent items, many of which are technical in nature, we believe they do require resolution.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

The issues raised under these headings, together with a number of other issues identified by Industry, have been discussed in detail at recent tripartite meetings. During the course of these discussions a number of items have been identified as priority items needing to be addressed and proposed changes to the regulatory framework made as part the recommendations due to be submitted to Secretary of State in June 2017. Other items have been classed as being of lesser importance or urgency which can be addressed between June and December 2017 by either changes to the Regulations or in Guidance (statutory or otherwise). A small number of items have been discontinued. Although described as lesser important/urgent items, many of which are technical in nature, we believe they do require resolution.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

The issues raised under these headings, together with a number of other issues identified by Industry, have been discussed in detail at recent tripartite meetings. During the course of these discussions a number of items have been identified as priority items needing to be addressed and proposed changes to the regulatory framework made as part the recommendations due to be submitted to Secretary of State in June 2017. Other items have been classed as being of lesser importance or urgency which can be addressed between June and December 2017 by either changes to the Regulations or in Guidance (statutory or otherwise). A small number of items have been discontinued. Although described as lesser important/urgent items, many of which are technical in nature, we believe they do require resolution.

22. Other suggestions for amendments to the legislation.

No response

23. Alternative approaches to improve the regulatory framework that do not require legislation.

No response

Consultation response - Metasums Ltd

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Terry Hersey***
Organisation: ***Metasums Ltd***
Position: ***Director***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☐	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
☑	Other, please specify: ***Training and consultancy support to defence contractors on UK and USA pricing regulations***

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes.
The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

The SSRO's recommendations to the Secretary of State should prioritise improving the clarity and simplicity of the regulatory framework in its application to prime and sub-contracts. There are many areas of the legislative framework where lack of clarity exists (e.g. responsibility for assessment of allowable costs when pricing a QSC or change to a QSC; application of regulations 5 and 14) or wording is particularly inaccessible (e.g. regulations 31 and 32) or where the desire for brevity has overridden the need to make easily intelligible.
There is much to be improved in the Act and regulations. As I understand things, it is within the authority of the Secretary of State to make changes to the regulations insofar as any changes are within the scope of the Act but that changes to the Act require Parliamentary time which may not be available.
The SSRO's remit should not be expanded to address the areas set out in 1 and 2 above. MoD's governance process on procurement decision for single source or competition lays with MoD and other parliamentary bodies e.g. NAO, Defence Select Committee. Much as everyone wants to make greater use of SMEs MoD does not look to have the capacity to provide the level of support that, I know, many need in complying with the range of administrative obligations.
SSRO should concentrate on getting the scope that it has fully operational and based upon sound and effective working relationships with MoD and contractors.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

This is a very bad idea.
It undoes the deal that was agreed at placement and contract acceptance and consequently there will a winner and a looser. Work would continue on the unrevised SoW as it would take some time to agree an AAR compliant price. It would represent

significant risk to the parties if the change was implemented without an AAR compliant price being agreed If the revisions to the SoW were able to stand alone (not be dependent upon the performance of the pre-existing contract) then a new contract, on a stand alone basis should be awarded rather than a pre-existing contract amended.
Contractors will want to deliver to MoD's evolving requirements and therefor reasonably expect to incorporate change by way of an equitable price adjustment (based upon agreed estimates of the additional costs estimated less any costs avoided). This is what the USA does and as far as I am aware every other OECD nation. Pre-existing contracts may contain DEFCONs that give MoD right to impose certain changes to the SoW and for these changes to be priced on an incremental basis. Pre-existing contracts could have been priced by reference to market prices or competition. There is, as far as I can see, no merit in the proposal
For sub-contracts the idea is wholly risible. Many will have been awarded following a competition (the change would not have been competed) and may even (as things stand today) be for; indirect goods, works or services or direct goods, or services where the expected usage on qualifying contracts is >50%.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

The idea should be rejected on two counts (1) it undoes, for no good reason, prices that were previously agreed, (2) the arrangement is not deliverable on other than the most simple of MoD contracts.
This proposal would still cause previously agreed prices to alter for no good reason. Prices established through competition still become undone; prices established which utilised ASG supported policy of application of market prices for proprietary items still become undone; prices established using equality of information and the GPFAA in place at date of contract award still become undone.
I have no idea what 'committed by reason of performance should be taken to mean' but fully expect that the expression would lack sharp edges required when undoing the price of part of a contract. Purchase orders commitments made with the supply chain, including requirements that are anonymised as a consequence of the use of MRP systems; production orders for anonymised requirements, non recurring costs in progress. What profit rate to apply. I strongly suggest that the SSRO explore with MoD CAAS what difficulties lay in the way of implementing such a hybrid.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

Devil lays in the detail. What happens if the 'proposed' QDC is not awarded. Will the QSC cease to be a QSC. I can only see the proposal as reasonable when it is applied to a sub-contract where 100% of the cost of the goods, works or services are to be allocated to a qualifying contract.
Proposed QDC would also need to be a defined term.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

The reference to top 20 is only in regard to contract reports. SSRO should confirm that with MoD that they have utility in knowing all sub-contractors >£1m and this is more than any additional reporting costs.
The reasons for a negative assessment are set out in regulations 58 through 63. Again

the SSRO should confirm that with MoD that they have utility in knowing and are willing to pay for any increased costs to know when an assessment was made and the assessment outcome was negative which element of regulations gave rise to that conclusion. This could be a simple tick the boxes that apply (on the standardised report).

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

Not unless MoD has the capacity to support. Only MoD has access to a sub-contractors company confidential information, only MoD under the Act and regulations is able to exercise that right. Accordingly only MoD is able to assess if costs included within its overall cost estimate are AAR compliant or not. This needs to be done pre-contract award or pricing of contract change.
The £25m threshold was established because MoD had limited capacity to undertake obligations to price qualifying sub-contracts. It is unacceptable and unreasonable for assessment of allowable costs used in pricing of a qualifying sub-contract to be conducted by other than MoD. I'd be very surprised if MoD said it had the capacity to support a lowering of the threshold.
Any lowering of the threshold should consider a higher threshold for '50%' and 'enabling the performance' indirect costs.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

You can't be half pregnant. Contracts that are made within the framework of an international cooperative defence programme have another government as a party to the contract. For this reason they need to be excluded. It is easy to find out if a contract is within the framework of an international cooperative defence programme as there is a framework that says it is. If MoD lets a contract that is half in and half out then the other government is party to the part of the contract SoW. One should not cause an agreement between governments to become undone because the whole contract was not within the framework. MOUs are established for phases of a programme and contracts are awarded for these same phases e.g. development, production, support
I understand the exclusion of intelligence activities to relate to those contracts MoD wants to keep exposure minimised. If MoD mixes intelligence activities within a contract for non intelligence activities then it may still need to be kept outside of the scope. The Secretary of State could always exempt and not say why etc; this just makes it easier for him.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

These proposed amendments would bring the SSRO onto the field of play and undermine the authority of the MoD. They are excessive for a regulations office to be able to perform its duties.
Threatening contractors to supply information that MoD does or has not supported places SSRO in a position contrary to that which was communicated to defence contractors during senior discussions prior to December 2014.
SSRO's position as independent and impartial is incongruent with such a proposal. The SSRO is not a Regulator there to protect the man on the street who purchases

water supply to his house, the is no Samson and Goliath here; the SSRO is a Regulations Office. SSRO needs to overcome its poor relationship with contractors, Rolls Royce reference and much besides has done a great deal of damage to the willingness of contractors to engage with the SSRO. The SSRO needs to repair and I believe that this is best achieved through dialog and meaningful consultation with trade groups. Issue of legislation and threat of penalties is not the way forward. For the framework to work SSRO needs to understand. Failure to engage will lead to industry seeking ever closer policy relationships with MoD and development of agreed commercial guidance for publication on the ASG.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

These proposed amendments would bring the SSRO onto the field of play and undermine the authority of the MoD. They are excessive for a regulations office to be able to perform its duties.
Threatening contractors to supply information that MoD does or has not supported places SSRO in a position contrary to that which was communicated to defence contractors during senior discussions prior to December 2014.
SSRO's position as independent and impartial is incongruent with such a proposal.
The SSRO is not a Regulator there to protect the man on the street who purchases water supply to his house, the is no Samson and Goliath here; the SSRO is a Regulations Office. SSRO needs to overcome its poor relationship with contractors, Rolls Royce reference and much besides has done a great deal of damage to the willingness of contractors to engage with the SSRO. The SSRO needs to repair and I believe that this is best achieved through dialog and meaningful consultation with trade groups. Issue of legislation and threat of penalties is not the way forward. For the framework to work SSRO needs to understand. Failure to engage will lead to industry seeking ever closer policy relationships with MoD and development of agreed commercial guidance for publication on the ASG.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

Get a better working relationship with MoD, understand more and threaten less.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means

that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

I see this as uncontentious if the right to referral is restricted to MoD and the parties to a contract.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

These proposed amendments would bring the SSRO onto the field of play and undermine the authority of the MoD. They are excessive for a regulations office to be able to perform its duties.
Threatening contractors with fines that MoD does not seek places SSRO in a position contrary to that which was communicated to defence contractors during senior discussions prior to December 2014.
SSRO's position as independent and impartial is incongruent with such a proposal. The SSRO is not a Regulator there to protect the man on the street who purchases water supply to his house, the is no Samson and Goliath here; the SSRO is a Regulations Office. SSRO needs to overcome its poor relationship with contractors, Rolls Royce reference and much besides has done a great deal of damage to the willingness of contractors to engage with the SSRO. The SSRO needs to repair and I believe that this is best achieved through dialog and meaningful consultation with trade groups. Issue of legislation and threat of penalties is not the way forward. For the framework to work SSRO needs to understand. Failure to engage will lead to industry seeking ever closer policy relationships with MoD and development of agreed commercial guidance for publication on the ASG.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

Get a better working relationship with MoD and contractors through dialog, consultation and most of all listening.
SSRO looks to have very few ideas beyond those of extending its authority. The SSRO should learn through dialog so that it can make expert determinations and develop reporting to satisfy the objectives. Listen more and take action after a full understanding is developed.
It is not single source procurement that lacks credibility but rather the SSRO.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO’s recommendations.

I believe I have covered this elsewhere. The exact question being asked is unclear.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

The USA let FMS contracts using the Federal Acquisition Regulations (FAR), Defense Supplement (DFAR), Cost Accounting Standards Boards Regulations (CASB), Joint Travel Regulations (JTR) to name but a few. US Defence contractors embed the US regulations into their business processes, FASB has an IFRIC for Government Contractors. Sub-contracts issued by defence contractors undertaking FMS contracts are also subject to the same US federal regulations.
It's a government to government contract, the US Government will use their systems Even if the Government stood to one side and let the contractor decide if he wanted to sell using UK legislation I can't see much grounds for optimism or access.

17. Issues raised concerning enforcement of price control (section 15).

The SSRO is not alone in making recommendations to the Secretary of State
The SSRO's independence and impartiality is completely undermined if they act as pricing authority on matters other than where there is a within scope reference.
15.10 I believe you are wrong where you state that you may have the authority today.
15.12 I despair at SSRO lack of understanding. MoD is the pricing authority and the party with whom contractors engage in pricing matters. SSRO wandering in at will undermines MoD and increases uncertainty.

18. The proposal for disapplying the price formula (section 17).

The pricing formula should not be applied when market forces show the reasonable price. Prior competitions held by companies should be good to show market prices (there are permitted in the USA when circumstances support the same); verifiable market prices for non-developmental items should be used when there is adequate evidence.
It should be for MoD to disapply the price formula.

19. Stakeholder proposals supported by the SSRO (section 18).

All look fine on a quick read except the suggested amendments to regulations 34 and 36
Cost allocation methodology is the Q-MAC. Does the SSRO seek a copy of the contractor's QMAC? Overseas contractors may have their own nations version of the same e.g. CASB DS-1 for US contractors.
Apportionment is set out in the development of the rate claim numerators and should therefor be self evident. Recovery should be set out in the rate claim denominators and should also be self evident. No harm in including within the words but watch the language to ensure clarity of understanding

20. Stakeholder proposals not presently supported by the SSRO (section 19).

Negative incentive adjustments should be incorporated as a pre-determination of LDs

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

I believe that SSRO's thinking in 20.5 is muddled or unrealistic. The consequences of its position is that agreed contract prices would routinely be subject to wholesale price redetermination as many changes to the SoW are 'do this instead of that' or 'incorporate this in addition before you supply the article' rather than 'I'd like a bag of carrots in addition to the cabbages I ordered'. Also when there is an agreement to change the allowable cost included within an agreed price. This price (as is MoD practice) used 'actual' labour and overhead rates as calculated by the contractor for the financial year before the contract was awarded. These rates were included in the basis of estimate and were included within the CPS submitted to MoD and SSRO on contract award. On post award audit MoD found that the 'actual' labour and overhead rates for the Lofting Department' used in estimating the contract included some costs which the contractor has subsequently accepted were not AAR compliant. The rate for later years was therefore established on a false base and should have been £0.10 per hour less. There were 10,000 hours included in the estimated cost using this rate. Should the contract price be re-established as a non-severable amendment rather than the price be adjusted by £1k plus profit?
20,6 is misses the point , it is not the difficulty in estimating but rather retention of the profit motive. If contracts are subject to price redetermination the failures and achievements to date are unwound as costs and performance to date fall to no cost plus. Contract are awarded as fixed and firm because MoD wants them that way.

22. Other suggestions for amendments to the legislation.

SSRO should take the opportunity to review contract and contractor reports to ensure they provide utility e.g. the use MoD make of estimated rates is limited for a number of wholly understandable reasons.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

SSRO's statutory guidance on reporting is little more than a repeat of the regulations and has advanced little from the unsatisfactory status developed by MoD 18 months ahead of the formation of SSRO before it gave up and left it to SSRO to develop (engaging in dialog with contractor working parties.

MOD RESPONSE TO SSRO REVIEW OF THE SINGLE SOURCE REGULATORY FRAMEWORK: PUBLIC CONSULTATION ON RECOMMENDATIONS

Proposal	MOD Comments
Proposed Amendment 6.12 pp11	**Not supported** The decision whether to treat an amendment as a new contract or to become a QDC should be one which is driven by the benefits which will be achieved. MOD commercial policy already places the onus on the Project Team to push for the placement of QDCs and conversion to QDC status on amendment, and has mechanisms in place to support teams in this. However, the general assumption that QDC status will always be better than the extant position is not always the case, particularly where there contract is substantially complete and has limited cost and schedule going forward. Any decision on whether to convert on amendment should be subject to a review at the point of change to assure that best value for the Department is obtained. This may not be monetarily related, it could be benefits regarding transparency however the case needs to be made contract by contract rather than the adoption of a general assumption of benefit and a legal requirement
Proposed Amendment 6.13 pp11	**Supported** Insofar that the change is applicable once the decision to convert a contract to QDC on amendment is made, then this proposal is very welcome. It would provide clarity when in the position where part of the contract has already been performed and commitments made on costs and profit. But this is just one of a number of types of cost where we believe the pricing formula should be dis-applied. *MOD has expressed comprehensive views on this during tripartite (MOD/ADS/SSRO) workshops.*
Proposed Amendment 7.20 pp16	**Supported** But only in relation to situations when a sub-contract is signed in the knowledge that it is intended to be part of a proposed QDC. This will be necessary to prevent gross avoidance. However, a statutory requirement for *all* contracts entered into before a QDC leads to a risk of an infringement of the principle of a party entering knowingly into a contract with legal obligations.
Proposed Amendment 7.22 pp17	**Not Supported** The proposal to require the details of all subcontracts £1m+ in the contract reports appears too burdensome to suppliers on a framework which is still developing. A better option would be to set a different value for which those assessments are required for example, if set at £20m, this will provide visibility of contracts close to the threshold. **Supported** The recommendation to complete a QSC assessment within 30 days of the agreement of the contract does not appear unreasonable. Reasoning for negative assessments may not be unreasonable providing there is a suitable materiality threshold for those contracts. Neither of these requirements should result in significant additional costs for contractors.

	Not supported The requirement to notify Secretary of State and SSRO regarding the outcome of a QSC assessment within 30 days is less persuasive and appears to set up another ad hoc reporting mechanism. Notification of the assessment should be included in the next standard report.
Proposed Amendment 8.5 pp19	MOD is not averse in principle to the lowering of the QSC threshold. However, currently there is not enough data to support the requirement for the change in legislation. The changes discussed as part of proposed amendment 7.22 may provide a stronger dataset to allow a better judgement to be formed as to whether the threshold should be lowered and, if so, to what level. It is also necessary to consider the practical consequences of lowering the threshold and at what sub-level it will impose obligations on and whether they would have the required familiarity with the legislation. Lowering the threshold is likely to pull in a larger number of sub-contractors, many of which will not be familiar with SSCRs.
Proposed Amendment 9.7 pp23	**Not supported** To allow exclusion only where a contract is wholly within an international agreement is too restrictive. There are almost certainly going to be instances where part of a contract, perhaps only for a small part of the overall value, is not tied up with an international co-operative arrangement but the remainder is part of such an arrangement. In these circumstances it would not be practical or make sense to treat the contract as a QDC as the legislation would not be enforceable on much of the contract. MOD would like to look into the possibility of amending the exclusion to allow for carving out the aspect of the contract that is made within the framework of an international defence programme and making the rest of the contract subject to the regulations. We would also like the SSRO to consider the option of both parties being able to agree to the whole contract becoming a qualifying defence contract regardless of the fact that some element of it may be within the framework of an international defence programme. The MOD position on exclusions for international collaborative contracts was dealt with at the Tripartite (MOD/ADS/SSRO) Workshops. **Partially Supported** MOD supports the conclusion that clarity is required on the exclusion and that a definition needs to be developed which recognises that there needs to be an exclusion for contracts, where outside knowledge of the nature or/and the timing of a defence procurement activity could cause a risk to national security. We thought it may be useful to link the definition to the information that would need to be provided in the Contract Pricing Statement and whether outside knowledge of any of the information required to be provided would cause a risk to national security. The MOD position on exclusions for international collaborative contracts was dealt with at the Tripartite (MOD/ADS/SSRO) Workshops.

Proposed Amendment 10.15 pp28	**Not supported** MOD do not believe it would be reasonable to give the SSRO such unrestricted powers to compel industry to provide such information. The Act and Regulations already set out the information that the SSRO requires to undertake its main statutory duties. There may be merit is revisiting these requirements, but a blanket, self-determined right of the type described seems disproportionate and is unlikely to be supported by Parliament.
Proposed Amendment 11.15 pp32	**Supported**
Proposed Amendment 12.12 pp35	**Not supported** The proposal to allow the SSRO to issue compliance and penalty notices is inconsistent with their role as a body of arbitration. It is for the MOD to issue these notices and for the SSRO to offer advice and an appeals route to suppliers. The MOD position on this issue was dealt with at the Tripartite (MOD/ADS/SSRO) Workshops. The SSRO has offered to make arrangements (proposing the establishment of a separate body within the SSRO to look at appeals) but we do not believe that this will have credibility with industry as this internal body (set up entirely by the SSRO) will be asked to arbitrate on decisions made by the SSRO. There will be a clear conflict of interests which have not been addressed by the SSRO's proposals. Moreover, having both MOD and SSRO issuing these notices is confusing and also raises questions regarding what happens to the receipts which are generated.
Proposed Amendment 14.4 pp38	**Not supported** The value for money that MOD seeks is achieved through a Government-to-Government arrangement where best value is obtained through a price negotiated by the overseas Government and, in most circumstances, the MOD simply does not have the option or the leverage to negotiate a better deal with another sovereign government. The MOD position on exclusions for Government-to-Government agreements was dealt with at the Tripartite (MOD/ADS/SSRO) Workshops. The Act was not intended to replace established arrangements such as these. Moreover, MOD does not have the means to enforce the Act upon foreign Governments. MOD does however think that there may be merit in look looking into other ways of the SSRO getting more transparency about the frequency of and reasons for the use of Government-to-Government contracts. We have already shared these thoughts with the SSRO and industry.
Proposed Amendment 15.8 pp40	**Not supported** This would put the SSRO in the position of being able to make legally binding changes to single source contract prices at will. Suppliers would then be unlikely to sign contracts unless the SSRO had agreed that the price is AAR. This would mean that, in effect, the SSRO would negotiate contract prices. Apart from the resource implications, the MOD would still own the risks to military capability of a failure to agree. Moreover, the SSRO could not act as an arbiter on prices that it had already approved, and so it would be necessary to establish an additional body to take on this role.

Proposed Amendment 17.16 pp44	*MOD has expressed comprehensive views on this during tripartite (MOD/ADS/SSRO) workshop.* MOD supports the proposal that the legislation needs to allow for disapplication of the pricing formula, but not that all such cases be referred to the SSRO
Proposed Amendment 18.4 pp45	**Supported**
Proposed Amendment 18.6 pp46	**Supported,** subject to further detailed consideration
Proposed Amendment 18.10 pp46	**Supported** The suggested application of the Final Pricing Adjustment to only the relevant proportion of the contract that has been priced on the Firm, Fixed or Volume Driven methods is appropriate to ensure that the correct FPA is applied.
Proposed Amendment 18.12 pp47	**Supported** The approach set out to enable a direct payment between MOD and the subcontractor as a result of an allowable cost adjustment, to avoid impacting on wider arrangements, looks reasonable.
Proposed Amendment 18.14 pp47	**Supported** The requirement to include the cost allocation methodology is welcome; preferably a formal cost allocation statement should be required (in MOD referred to as the QMAC).
Additional Amendments	In addition, the MOD has asked the SSRO to consider the following proposed changes: (a) options for widening the Cost Risk Adjustment applied to the Baseline Profit Rate; (b) considering a process to allow for the application of different profit rates within the same overall contract; (c) disapplication of the price formula to part of a price of contract, while maintaining a structured set of criteria for demonstrating that they are AAR; and, (d) Clarification of the exclusions, especially on international collaborative agreements.

Consultation response - Real Safety Today Limited

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Peter Hanley***
Organisation: ***Real Safety Today Limited***
Position: ***Managing Director***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☑	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☑	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
☑	Other, please specify: ***Independent Researcher***

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes.
The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

1. ***Yes. Public money spend and outcomes of spend always need to be explored. Proper investigation of where money is going and what it has achieved is as vital as the amounts involved. This helps form better policy and improve engagement of meaningful projects, and make it more difficult for money-spend focused activities to simply absorb money for low value outcomes. This ultimately helps the nations economy thrive and grow and support its citizens.***
2. ***As the SSCR2014 regulatory framework seems to be focused on failure of qualifying contractors to limit profits, it's not clear how this framework would seek to promote competition and innovation. Any monitoring of SMEs under these conditions would likely increase their costs for no meaningful gain, and worsen their Annual Reporting of 'Going Concern'. This would have an adverse impact on the economy.***

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

3 to 8 No comment

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

SSCR2014 doesn't have a definition of "good value for money", nor one for "fair and reasonable prices for contractors"? Without these critical definitions, even with the SSCR2014 regime, no judgement can reasonably be met. So it is unlikely that a judgement on value can be reached outside the regime. This is a simple logical conclusion which needs no further discussion on evidence, reasons, benefits or impacts. It simply remains for the regulator to decide whether these definitions are to be provided and used in decision making or not.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

RE para 10.13 second sentence: "Disclosure of the information would be a criminal offence, except in the limited circumstances provided in that Schedule." The logic of this disclosure arrangement may well lead to violation of security. The Purpose and legitimacy needs to be established first before SSRO ask for the information. The respondent organisation is not in a position to second guess where the SSRO's investigations are going at any one time; therefore in the interests of avoiding penalties and charges, respondents may overstep the mark.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

For a regulation that is only 2.5 years old, it's not clear why SSRO should need alternatives for accessing data. Surely the logic and system design has been developed robustly before these regulations were put into force.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

12 & 13 No comment.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

The Act [and Regulations] can't truly be considered 'self regulating' as this term usually applies to an industry or body being trusted to manage all its affairs, with little or no intervention from say a regulator. The Act [and Regulations] have effectively determined that intervention in the industry activities is required, and enforcement powers have been provided to SSRO. The activities described in the regulation and consultation papers, largely revolve around the contractors managing the risk of being prosecuted by SSRO; this is not a 'self regulation' situation. Question 14 hits the nail on the head when it refers to "make single source procurement credible". This seems to be a far more meaningful overall purpose for SSRO. Other measures could be the clarification of the Defence Reform Act 2014 and SSCR2014 to state that this Act and Regulations are made to "make single source procurement credible". This would be better than the phrase at beginning of DRA2014 ".. to make provision relating to defence procurement contracts awarded …". The beginning of SSCR2014 has no introductory purpose statement. Thus these instruments can become to mean anything that people wish, and miss the objective the legal drafters had in mind. As an example the Health and Safety at Work etc Act 1974 says in its opening words: " … to make … provision for securing the health, safety and welfare of persons at work …". It's purpose is clear. This could be a good model for SSRO to consider.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

RE "15.3 The primary responsibility for ensuring compliance with price control rests with the contracting parties. They are required to ensure that the price of a QDC or QSC conforms to the formula. If they cannot agree, or if some matter requires clarification, then the Act provides for referral to the SSRO for an opinion or determination."
This introduces a root cause of an issue; that "price is a formula". The chances are that all parties will have in mind what has gone before. Human beings are often creatures of habit, and often adopt a precautionary principle. The mere fact that there is a formula to be met, AND that if the Contractor gets that wrong they will maybe fail at some degree, creates a perverse incentive to keep the costs and prices as high as possible; until it is seen how things pan out. I note already elsewhere that SSRO is aware that QDC [?] pricing is retrospective.
The next 15.4 follows on from issue raised in 15.3: "The SSRO is charged with keeping under review the provision of Part 2 of the Act and the Regulations. As the application of the price formula is a key feature of the regulatory framework, the SSRO considers the reports it receives on QDCs and QSCs to keep under review whether the price formula is being applied. The SSRO will also take into account other information of which it is aware."
This shows that SSRO itself will get caught in the Preferential engineering of Price controls as it is dependent on those it is regulating for its data, as input to its decisions. Again this can have the adverse effect of locking a system of contracts into a long term cycle of behaviour which preserves inefficiencies rather than encouraging real innovations.
The regulatory control issue further emerges in 15.7: "The SSRO accepts that it may be difficult for the MOD to take action in cases where it has already agreed particular terms with the contractor. However, this creates the real possibility that contracting parties may agree a price in circumstances where that is not in compliance with the price formula and the MOD may subsequently pay that price."
Here we now see that the very regulations for achieving the order desired, may get subverted for some undisclosed reason. If the price control formula is so important, then some practical research is needed into how this works in practice where human beings are managing large amounts of money for large project outcomes.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

In systems engineering terms the last line of 14.2 "In such cases the other government is effectively an agent, standing between the Secretary of State and the defence contractor that supplies the equipment." Creates a wholly different arrangement to the one that SSRO and SSCR2014 are devised to manage. Clearly there is an issue, to be addressed, which may benefit from some systems design input before the application of regulation is considered or reconsidered.

17. Issues raised concerning enforcement of price control (section 15).

15.5 first sentence hold the key to the effectiveness of SSCR2014 "If the SSRO has any concerns as to whether the price formula has been correctly applied .." In similar fashion to the response at Comment 16, a systems engineering approach, coupled with Clean Language interviews with SSRO and its stakeholders, could reveal the granularity and detail behind this concern. When a human being expresses concerns in this way there is usually something worth exploring. It is suggested that this is a critical area for SSRO to get clarity on. This will be helped with diagrams rather than relying on words alone to express and understand the issues and dynamics, and achieve success.

18. The proposal for disapplying the price formula (section 17).

No comment.

19. Stakeholder proposals supported by the SSRO (section 18).

No comment.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

No comment.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

No comment

22. Other suggestions for amendments to the legislation.

"The purpose of this regulation to limit excessive profit is understood. This means that this regulation has been designed with the familiar purpose in mind of 'avoiding failure', where the failure in this instance is deemed to be excess profits of single source contractors. Sadly, experience shows that the attempts to control failure with constraints, doesn't address the failure, and leads to other unintended adverse consequences. In the long term the economic activity and productivity of organisations declines. This wouldn't be in the interests of the UK economy for its performance to be degraded or suppressed in any way.
It is suggested that there is an alternative strategy which could liberate the Productivity powerhouse of the UK economy, and remove the need for costly failure avoidance regulation. The suggestion is that the SSRO investigates the possibility of developing and deploying "Success seeking regulation". This type of focus would encourage organisations and contractors to generate successful outcomes. As success by way of better outcomes in less time and for less cost became the norm, there would be less need for profit margins to be pushed up to maintain the contractor cost base.
The above suggestion for "success seeking regulation" would support the SSRO's two statutory aims of obtaining good value for taxpayers' money and a fair and reasonable return for industry, albeit in a logically different way to the current enforcement model. The reason for suggesting a different approach to regulation is that Single Source Contracts involve more than 'spending', and so would produce a wider scope of scrutiny than the SSRO's first recommendation: "ensuring single source spending is fully covered by the legislation". For Contract organisations to be truly successful, whether large or small, they need to ensure the spending is appropriate, and deployed effectively in order to achieve a project outcome which is worth more than the spend. It is well known that focusing the human mind on remaining within set constraints [in this case spending] that the activities are designed to meet the constraint; the truly desired outcome cannot receive the attention it needs. The human mind cannot both be avoiding failure and seeking success. At the very basic level of survival, when any of us is threatened by an event, our mind-body systems are designed over thousands of years of evolution to protect us. Whilst that threat is still present, we are not able to simultaneously sit down and calmly plan how we would exploit that situation for maximum gain at least cost.

The unstated desire of SSRO regulations is likely to be deriving maximum gain from a procured project, for the least cost. This is best achieved in conditions which encourage people to be calm and fully engaged in an appreciative activity. When financial resources are put under tight constraint, this initiates a condition of fear and threat in the project team. They won't perform as well as desired. Neuro-economics shows that the fear of loss creates a disproportionately disruptive effect on people. The study by nobel laureate Daniel Kahneman, shows that for each £100 loss [or constrained spend] then in order to create a calming balance in the human mind, £300 gain has to be generated. So tightening the constraints on profits, will create a drive three times as strong against that constraint, just simply so that the project team can regain their minds so they can think. Hence why a change of strategy at national level towards success seeking regulation, can deliver significantly better outcomes for less cost than currently believed.
As an indication of the focus of the regulations themselves [The Single Source Contract Regulations 2014] there are nine instances of 'failures' and no instances of 'success'. There is one instance of a 'successful contractor' but there is no evidence of a focus on the higher goal of a 'successful project or contract'.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

No comment.

RESPONSES TO CONSULTATION

Keith Hartley
Emeritus Professor of Economics
University of York
21st March, 2017

My comments are:

1. **Para 5.9. Pricing single source contracts**.
SSRO expresses concern at single source contracts which should have been competed. This is an important topic which requires further detailed and critical study focusing on analysis and critical assessment.

2. **Allowable costs (para 6.8).**
SSRO needs to recognise that allowable costs are not necessarily efficient costs. The definition of allowable costs could be funding considerable inefficiencies.

3. **QSCs and supply chains (para 7.7).**

The focus on defence industry supply chains is welcome but problematic, mainly because supply chains are complex and relatively unknown for defence industries. They differ between types of equipment (air, land, sea).
I have three further comments on supply chains:

a) Need to define competition for supply contracts: what is competitive and non-competitive? How practical is competition in supply chains (e.g. for nuclear submarines, there might be monopoly suppliers where competition is determined/limited by the provisions of the US-UK nuclear agreement).

b) How far will you proceed into the supply chain? First tier suppliers can be identified by primes; but there are second and third tier suppliers which are difficult to identify and require substantial research (probably not worthwhile to include, say, third tier suppliers?).

c) I was surprised by the estimated total value of QSCs – the figure seemed low?

4. Other Proposals? Recommendations

I found most of these reasonable and sensible, especially on Amendments and Proposal (para 6.13); on Excluded Contracts; and on Access to Information.

Consultation response - QinetiQ Ltd

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

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Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Graham Brown***
Organisation: ***QinetiQ Ltd***
Position: ***Group Commercial Director***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☑	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
	Other, please specify:

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

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- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

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1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

At this time, we do not believe that the regulatory framework requires to be expanded to achieve the original aims of the DRA in order to improve its effectiveness. Industry is adapting to the DRA regime. However, the experience of industry and the SSRO and the MOD is limited to the two years since its introduction and the data that is available to the SSRO derives mainly from the initial contract reports which have been submitted.

We agree that the regulatory regime would benefit from review in areas representing either fault lines or gaps in the regulations reflecting the operational experiences of the SSRO, MOD and defence industry over the last two years. One of the key parameters that the regulations needs to re-enforce is the incentivisation axis that encourages Industry to manage their cost base in an efficient manner, releasing funds for growth. This is a really important alignment between industry and the SSRO as it targets the circa +90% (which is the cost base) rather than focus on the profit which has a single digit effect. It also important to align the regulations with the key business drivers of business investors, the shareholders. We believe that this would be consistent with the Regulators Code. (Para 1 (Regulators should carry out their activities in a way that supports those they regulate to comply and grow)).

As defined in the DRA, the SSRO's aim is to ensure that good value for money is obtained for the UK taxpayer in expenditure on qualifying defence contracts and that single source suppliers are paid a fair and reasonable price under those contracts. The DRA does not require a 'balance' to be struck between these two objectives; rather, it requires both to be achieved.

The value delivered by a feature of the regulations needs to be at least commensurate with the cost of its implementation, and any future change needs to be evaluated in this context and to meet this test.

In respect of a) above, with reference, in particular, to greater transparency regarding single-source procurement decisions, the MoD is the best-qualified and most appropriate authority to decide on value for money when it comes to military capability and operational need, and to decide on the optimal procurement strategy as between single source and competition. If MoD has agreed a single-source contract that it believes represents value for money, with the price determined in accordance with the regulations, and the contractor is satisfied that it has a fair and reasonable price, then the DRA tests (and the SSRO's aims) should be assumed to be met. The SSRO's role is assuring value and building confidence and it discharges this by monitoring compliance with the regulations which provide the framework for value for money and

a fair price to the contractor. It should also be duly recognised that MoD does have considerable buying power in its relationship with industry.
In respect of b) above, we do not believe that promotion of competition by the SSRO is necessary to achieve the DRA aims. We consider that it would be inconsistent for the SSRO to assume such an objective as the DRA's aims are defined specifically in relation to qualifying defence contracts (i.e. single-source contracts) where there is not a competitive market. Our view is, therefore, that it is unnecessary for the regulatory framework to be amended to promote competition, as the existing framework is premised on the basis of a lack of competition.

Additionally, we are aware that the MOD has its own policy regarding the monitoring of SME engagement prompted by wider government policy, and that 'innovation' is a key element on the agenda. Whilst recognising that it is necessary to ensure that the DRA and SSCR regime are not inadvertently stifling any of these wider government policy objectives in the promotion of competition, innovation and the involvement of SMEs, we feel that the need for the goals set out in (b) above are being adequately addressed by government more generally. Also, to put the case for increased transparency into a business context, contractors are already motivated by consideration of shareholder value to manage their cost-bases more efficiently, and promote growth, which automatically supports the generation of value for money to the MoD, and lines up with HMG "better regulation" approach, which is, as stated above, for Regulators to carry out their activities in a way that supports those they regulate to comply and grow.

The interactions between transparency, the promotion of competition, and promotion of innovation would need to be thoroughly evaluated and analysed, as it does not follow that they reinforce each other. In fact, there are often tensions between these different factors. For example, it is noted that the DRA already provides significant requirements regarding transparency. While the imposition of a greater level of transparency on contractors is unlikely to promote a more competitive environment of itself, it may often have the opposite effect. It may even lead to a reduction in participation in the marketplace or weaken a pro-competitive dynamic. A lighter touch to transparency under the regulations could promote competition and innovation.

To promote innovation, the regulatory framework needs to uphold the principle of a fair and reasonable price for contractors. We believe that some of the suggested changes may have the opposite effect but there are other clarifications/suggestions that might be made that we believe would help. These are set out in our response to question 21.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

We believe that conversion of a non-QDC contract to a QDC contract should remain by mutual consent and not happen automatically when a non-QDC contract is amended. We have set out our reasons below.

We understand the SSRO to have acknowledged the logic of preserving a contract's pre-amendment "backstory" or history at the point of the amendment (see question 8). In practice, from a business perspective, this will be underpinned by decisions that the contractor has made, for example, affecting returns on investment, and risk profile, that are embodied in the contract price agreed at the outset and which have enduring validity, as pricing assumptions and dependencies, beyond the amendment date. We therefore believe the regulations should also support the maintenance of these business underpinnings. Automatic conversion and a requirement to re-price the entire 'contract in accordance with the formula and prevailing regulations remove a key ability of management to forecast and plan for essential matters on which investment business cases are founded. We note also that this situation, as described above, is equally applicable where Regulation 14 applies (i.e. the need for re-pricing when amending an existing QDC).

If investment returns (and other equivalently important commercial considerations) are not within a contractors' reasonable control, this will influence contractors' willingness to invest in the contract, limit innovation and research, limit the contractors willingness to invest in capability development and affect MoD affordability. It could also have implications for industry which is driven to achieve efficiency by shareholder demands for returns. Furthermore, it could impact on the MOD's ability to secure essential scope and contract change if, as a consequence of investor pressure, contractors become cautious about accommodating MOD requests for change.

We would also recommend that the term "new contract" be avoided. This is because a "new contract", as opposed to an existing contract converting to a QDC, imports a different meaning. A "new" contract would be subject to the requirement under the DSPCR to be put out to tender. This is clearly not what is required under the DRA. An alternative would be to use the term "converted contract".

When considering when a contract should convert to a QDC, we believe that it is impractical to prescribe a single threshold to apply to all contracts. For example should a contract automatically convert to a QDC where the contract's overall value is high in comparison to the amendment (i.e. a £5M amendment to a contract of value £1Bn?). Automatic conversion based on threshold would also fail to take account of other matters (for example contracts with a limited remaining term, such as 6 months to go. There would need to be clarity over the timing and measurement of the conversion (for example, if the aggregate value of a number of small value changes was in excess of the threshold that would not mean that the contract converted). To avoid such anomalies, it is important for conversion to continue to be the subject of mutual agreement on a case-by-case basis.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

We support disapplying the price formula to committed costs when a contract becomes a QDC by amendment, as outlined in paragraph 6.13. Thus, where a contract becomes a QDC by amendment, we concur that neither the price controls nor the transparency obligations under the DRA should apply to costs and associated profit committed by reason of performance of the contract. We would, however, welcome clarification that

the reference to 'committed costs' is intended to include costs incurred and other financial commitments in place prior to the amendment.

As discussed in our response to question 3, and for the reasons described therein, we believe this principle of recognising and preserving the 'history' of a contract should be extended to include other business and pricing assumptions and dependencies, the prices themselves, and incentive arrangements agreed prior to the conversion date that have a validity beyond that date. If adopted, this would require a change to the proposed new section 15(6) to the DRA, as quoted in the consultation document.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

The concerns that are described in the responses to Questions 3 and 4 above extend to the proposals for QSCs. We would also note the risk of "hair-trigger" conversions, as, in contrast with the consultation's proposal for QDCs, the SSRO does not propose that a QSC conversion should only follow where there has been an agreed amendment to a QSC.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

As a fixed threshold would be subject to the vagaries of escalation (e.g. VOP), parties would potentially not know until well after contract signature whether they had crossed a QSC threshold. Likewise, the test of a 50% contribution to the QDC opens up a major area of uncertainty.

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

Please refer to the general comments regarding transparency in our response to question 1 and 2.
QinetiQ feels that it is too early to consider changes in this area. There does not appear to be any evidence at this stage to merit reduced QSC threshold.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

We believe that the MoD would need to have the final say on both issues, and that the current level of flexibility should be retained, because these matters have the potential to directly concern national security and the maintenance of sovereign capability, and also because the MoD is best placed to determine the value for money aspects associated with international cooperative defence programmes.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

At one level, we believe this is not an appropriate question for the SSRO because the DRA defines (through threshold levels, circumstances such as those described in question 4, etc.) which contracts the government believes should be subject to the regulations and be tested against the objectives of value for money for MoD and a fair and reasonable return for the contractor.

As described in our response to question 1 and 2, the DRA does not require a 'balance' to be struck between these two objectives; rather, it requires them to be achieved simultaneously, so any lack of coverage under the regulations is of equal interest to industry. We have no reason to propose any alteration to the coverage - subject to our response to question 8 - that is currently defined under the DRA, and note that the DRA allows very few exemptions for new contracts.

For any non-QDC contracts that do not convert on amendment, we have explained in our response to question 3 why we believe such conversions to a QDC should continue to be by mutual consent. We have also explained how the regulations might be clarified/changed to make conversion more acceptable.

Although probably not intended to be part of this question, we also note that MoD policy now adopts almost entirely the approach of the regulations for single-source contracts underneath the £5M threshold.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

It is noted that the DRA already provides significant requirements regarding transparency. We are mindful that, whilst the SSRO already pays careful attention to holding competitively sensitive confidential information securely, employees and contractors of the SSRO, who are entrusted with such sensitive information, carry a significant legal obligation in respect to such information in their possession, which continues after they have left the SSRO's employment. This will be for periods of varying duration, depending on the quality of the information. The inadvertent dissemination of information will in many circumstances be sufficient to facilitate or even establish an information exchange leading to conscious or unconscious acts of anti-competitive behaviour. Inadvertent release would have potentially serious consequences for the competitive marketplace.

We note the reference in the Consultation to the OECD's 'Regulatory Enforcement and Inspection' publication. Specifically, the SSRO's proposals should align with the following principles:

- ***'Selectivity'; which encourages leaving compliance to market forces.***
- ***'Risk focus and proportionality'; which require intervention to be proportionate to the level of risk.***
- ***'Transparent governance'; whereby the operations of the regulator itself should be transparent.***
- ***'Clear and fair process'; which requires Governments to ensure coherent legislation and clarity of rules concerning the process for inspections and enforcements.***

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

We believe the regulations are already adequate to enable the SSRO to oversee credible single-source regulation. Furthermore, as noted above, the regime as a whole, including the role of the SSRO, has only been functioning for a limited period of time. We are of the view that is too early to be making changes to the current regime, which requires further time to properly "bed in".

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

Such an extension would be likely to strongly encourage referral to SSRO prior to contract agreement (with the consequence of there being three parties to a contract negotiation). Without such prior engagement with the SSRO and the MoD, neither the contractor nor the MoD would be certain of its commercial position (on which, for example, from the contractor's perspective, investment decisions and an assessment of a reasonable return will be based, and from MOD's perspective, value for money and affordability will be assessed). The consequences will be a far more cumbersome process to agreeing contracts and a disincentive to those in the industry to seek out these contracts.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

We believe it is too early to consider a change at this stage in the application of the regime. For example, that the new statutory guidance on compliance reporting has only recently been issued.

Also, we believe that MoD is best placed to assess whether the issue of compliance and penalty notices requires change, as it is in the best position to assess all of the facts in individual cases. If this is lost, there will be implications for the relationship between MoD and industry. This is a particular example of a provision that, in our view, Parliament did not intend to be reviewed at such an early stage in the life of the regime. Other examples would be the responsibility for QSC assessments, QDC exemptions, and the QSC threshold.

As MOD also has buying power, and is an intelligent customer, it is best placed to influence behaviours of suppliers in the defence community.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

QinetiQ does not support the proposal that the SSRO should be able to initiate opinions or determinations as this would severely undermine the SSRO's independence.

We would welcome an independent appeal panel with OECD "Best Practice Principles for Regulators" and would suggest that the remit of the panel include other areas where the SSRO is entrusted to make a determination of an issue.

QinetiQ does not see any evidence to suggest that the SSRO's powers are insufficient to discharge its functions as intended in the regulations.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

No response.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

No response.

17. Issues raised concerning enforcement of price control (section 15).

No response.

18. The proposal for disapplying the price formula (section 17).

Please refer to our response on question 21.

19. Stakeholder proposals supported by the SSRO (section 18).

Please refer to our response on question 21.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

Please refer to our response on question 21.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

These issues have been the subject of recent tripartite discussions and the outcome that QinetiQ supports is captured in the ADS responses together with the proposed actions for each item identified in the 92 issues.

Re-pricing contract amendments: see responses to questions 1, 2 and 21. The five bullets in paragraph 20.6 appear to be related to costs rather than the profit rate used to calculate the price where the issue arises.

Figure 11 (4) 'relating' has application potentially wider than the contract itself whereas 'concerning' limits the application to the contract which is understood to be the intention.

Figure 11 (6) might include consideration that the contractor be made whole or put back to the position it would otherwise have been as an alternative to compensation.

22. Other suggestions for amendments to the legislation.

Flexibility to look beyond the six regulated pricing methods, and incentive models, at the discretion of MoD and the defence industry, on a case-by-case basis, would help promote innovation and potentially offer opportunities to improve value for money and the management of affordability.

***As discussed in our response to questions 3 and 4, if the regulations recognised that the 'history' of a contract prior to the date of a conversion to a QDC by agreement - or the date of the amendment, where a QDC is amended in accordance with regulation 14 - covered business aspects that have validity beyond the date the contract converts, this would support contractor investment decisions, innovation, flexibility around contract change, and increase the acceptability of a conversion*.**

We would support greater flexibility and the potential to increase the percentage adjustment permitted at step 5 of the profit rate calculation (as mentioned to in item (10) of figure 11) in support of innovation.

We seek clarity on the practical application of Step 2 - (cost risk adjustment to determine the contract profit rate) - in particular on how a calculated risk adjustment value is intended to translate to the plus or minus 25% range of baseline profit rate.

The absolute value for risk and reward should be expanded to allow and incentivise more creative risk transfer which would create increased value for money opportunities.

It is important for the SSRO to be effective from and Industry perspective. It will therefore be important for the SSRO to continue to demonstrate that they are transparent and efficient as an organisation. This would also consistent with the Regulatory Code, para 6, "Regulators should ensure that their approach to their regulatory activities is transparent".

We seek confirmation that contractually mechanistic price adjustments implemented in accordance with agreed contract terms, for example, under an agreed VOP formula, do not constitute an 'amendment' either to a QDC contract (in the context of Regulation 14) or in respect of conversion of a non-QDC contract to a QDC.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

We believe that it would be advantageous for MoD to aggregate its requirements to increase contract size.

Response from the TaxPayers' Alliance to the Single Source Regulations Office consultation on the review of the single source regulatory framework

Submitted on behalf of the TaxPayers' Alliance by
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Summary

The TaxPayers' Alliance (TPA) has longstanding concerns regarding the procurement of defence equipment – something which has long been a challenge for British governments. We appreciate that it can be an extremely complex process but given the large amounts of taxpayers' money at stake it's vital that the government learns from past mistakes.

Given that around half of new MoD HQ contracts placed by both number and value are non-competitive, a robust regulatory framework for such contracts is essential in ensuring taxpayers get value for money.

Therefore we welcome this consultation but feel unable to address all the questions given the high degree of specificity and our organisation's reticence to comment on issues of security and international diplomacy.

Recommendations:

Coverage

Lowering the price threshold for QSCs from £25 million to £10 million removes an unjustifiably large discrepancy between the thresholds for QDCs and QSCs.

We agree with the SSRO's rationale to set the threshold for a QSC at £10 million compared to £5million for a QDC given that a minimum of 50 per cent of the value of a sub-contract's obligations must be for a QDC or QSC for that contract to become a QSC.

The fact that there is no evidence of the proportion of subcontracts with value contributions to QDCs or QSCs of as little of 50 per cent means we cannot see how another threshold could have been proposed.

We do not feel that we are able to comment on the exclusions where intelligence activities and international cooperative defence programmes are a factor.

Transparency

We are concerned that there have been instances in which the SSRO has not been able to carry out its statutory duties as contract reports have failed to provide adequate information.

We therefore feel that the proposal to amend the Defence Reform Act 2014 to empower the SSRO to require contractors to provide it with the necessary information to carry out its statutory duties are fair and reasonable. If enacted, these proposals would bring the powers of the SSRO more into line with those of Ofcom, the CMA and other statutory regulators and we see no good reason why this should not be the case.

We also welcome the SSRO's proposal to publish an annual account of how it has exercised its functions in this section so that a value judgement can be made as to whether these powers are being used proportionately.

Referrals and enforcement

We agree that these proposals will sharpen incentives for improvements in record keeping and reporting. We also note that the SSRO's proposal to amend the Act to empower it to issue compliance and penalty notices is consistent with the OECD's best practice principles and again brings its powers into line with other statutory regulators in the UK. Again, we do not see why this should not be the case.

Consultation response - Thales UK LTD

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Alison Hexter***
Organisation: ***Thales UK LTD***
Position: ***Finance Director HQ***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☑	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
	Other, please specify:

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes.

The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

Before any modification of the framework to extend its powers, the added benefit to that of the existing arrangements needs to be explored the cost and admin burden of any modifications must be understood.

The SME's are not well placed for this burden and more than likely may look elsewhere for business which will be to the detriment of the UK Defence industry.

Competition not single source should be promoted as Industry would then set a price that could recover all of its costs.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

It is worth ensuring the existing regime is delivering the benefits it desires before extending the scope or enhancing the provisions in the current legislation.

This change is not supported as amendments are not ' new contracts'.

Amendments to be a QDC have to be agreed by both parties and a change to legislation to a £5m amendment threshold amendment to an initial contract award under a fair process is not supported.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

If a contract is agreed to become a QDC by amendment, then the costs incurred prior to the agreement of the amendment need to be segregated.

Agree in principle but we need to ensure 'commitment' is clearly understood as there may be for example prices agreed for quantities with subcontractors who do not wish to become QSC's.

The reporting requirements will need to be understood and it should only include the costs and price covered by the amendment - a different performance obligation.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

There needs to be more work done on this. There is an issue of uncertainty. Where negotiations have already been made with a subcontractor who then becomes a QSC this will present problems. Further uncertainty could be an issue with timing as there potentially could be a QSC in existence prior to the QDC let.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

We recommend not making any changes to QSC assessments until the existing system has been in operation for about three years. There is no point in change without defining the value of the change.

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

My concern is that this threshold reduction may cause difficulty in agreeing contracts with subcontractors especially those that provide a product with an external market value and this may cause a detriment to the quality of the end supply.
The current threshold should remain.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

This could cause issues with security of information across country borders.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

Contracts and subcontracts which are not priced directly under the regulatory framework are subject to the provisions of certain DEFCONs.

There is a need to ensure the value of the current regime for QDCs actually works and is demonstrated before adding any new contracts into the regime as it may be very damaging to the UK Defence Industry. Suppliers (QDCs and QSCs) may consider they

will not undertake work that does not give the margin they require especially if they are part of an International group and need group approval for a required margin.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

The comparison to powers given to other regulators is not appropriate as the SSRO is not a regulator in the same sense. The SSRO should not need more information than is already stipulated . The powers given to the SSRO by the Act and Regulations provide access to information sufficient to enable it to perform its statutory obligations. MOD has open book access for all other requirements.
There is a big danger in gathering data which is not appropriate.

Focus should be on ensuring that the information currently collected is of value and working with industry and the MOD rather than just giving more 'power'

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

If access to a contractor's private information is essential for a task being performed, the SSRO should canvas MOD to use its Open Book rights to obtain the information. SSRO should gain and use information that is already accessible in the public domain.
There is a danger that the SSRO will have data and not information.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

Again this may not be what the spirit of the legislation intended .There is concern that there may be a lack of knowledge within the SSRO on this topic especially where specific contract and program knowledge is required for example in respect of risk and incentive for the contract profit rate.
There could however be some benefit in establishing workshops with finance reps from Industry to ensure clear guidance for all other steps of the profit rate calculation
Some allowance should be made for disallowed costs as the Baseline profit rate does not take this into consideration.
Where a business unit is part of a Group and assets are used but are not specifically owned by a specific business unit (eg if a Separate Properties legal entity exists) there may need to be an adjustment to a local business unit balance sheet to recognise the use of Capital assets.

No agreement on extending the grounds for referral for whether the contracts should be a QDC or QSC.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

The Act clearly establishes MOD as the enforcement body and the SSRO should be at arms length and can give opinions and make determinations in a set of clearly defined circumstances. This authorisation for the SSRO to issue compliance notices is not necessary and may preclude the ability of Contractors to work with the SSRO to ensure the regime is supported , The existing process is adequate and allows MOD to assess the intent behind any non-compliance and its materiality before issuing a compliance or penalty notice.

We would support Industry working with MOD and the SSRO to ensure the benefit of the reports and reporting is understood and to understand if there are any gaps and questions - issuing compliance and penalty notices without understanding may be a bit like getting a speeding fine when you have no speedo in the car.

The new DEFCARS reporting seems initially to be working and it is by working together we will make progress not by further powers for penalties.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

The regulatory framework states the SSRO should only give opinions and make determinations only when asked to by one or both of the parties. We do not support other measures as any SSRO additional powers are not necessary.
We need to ensure the current regime works without extending further powers.
Any measures take time to implement and understand for both MOD SSRO and the supplier so a cost benefit analysis should be undertaken before any change is recommended.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

We appreciate that the government needs to obtains good value for money in its expenditure on qualifying defence contracts but recently with the reduction in the profit rate and disallowed costs this could mean contractors do not consider they are paid a fair and reasonable price under these contracts and anything that widens the scope of the current legislation needs to be carefully considered especially in respect of qualifying subcontractors and the onus of reporting and pricing that would be placed on them. The cost and burden of complying with the current regulations must not be underestimated.

We need time and experience and for the MOD and its suppliers become more familiar with the regulatory regime and understanding of its requirement.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

There needs to be consideration for Companies that are part of a Group and incur costs from overseas. Where costs are allowed by the HMRC there should some trust between department that costs are appropriate.
The Memorandum of Understanding agreements that exist need to be reviewed.

17. Issues raised concerning enforcement of price control (section 15).

Price control compliance is agreed between the 2 contractual parties.
Both the MOD and the Contractors can be trusted to follow the pricing rules.
Any recommendation on this front would damage the 'independence' of the SSRO - it would not be independent as it would be involved in price setting.

The possibility for a contractor to make a case for deviation from the formula is welcomed especially when this concerns products that have a proven market value.

18. The proposal for disapplying the price formula (section 17).

No further comment.

19. Stakeholder proposals supported by the SSRO (section 18).

Agree that regulation 52(2) could be amended to measure the six months from the "time of agreement" of a QDC, as defined in regulation 2, rather than the date of entry into the QDC.

Agree that Regulation 2 could be amended by adding a new paragraph to specify that reference to a report under Part 6 of the Regulations includes a reference to an estimated rates agreement pricing statement.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

Records kept for HMRC purposes should be sufficient. Records normally retained in the accounting ledgers should be sufficient.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

The whole issue regarding price determination and profit rate timing needs to be clearer - the profit rate is that in force when you start work on the initial contract and any price re determining is possibly confusing
With IFRS 15 Contractors need to have certainty regarding contract values.

22. Other suggestions for amendments to the legislation.

It is very important that we all understand the existing legislation and make amendments based on facts rather than change for changes sake. We need time to really understand any issues and we have not experienced problems that may arise later when we execute and complete existing QDC's.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

At all times workshops should be held with industry to ensure their voice is heard. In this way industry will feel part of the process.

Consultation response - Transparency International Defence & Security

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Eva Anderson***
Organisation: ***Transparency International Defence & Security***
Position: ***Barrister and Senior Legal Analyst***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☐	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☑	Academic, think tank or similar
	Other, please specify:

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes. The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

Transparency International (TI) is the leading non-governmental organisation improving transparency and reducing corruption in the defence and security sector. Wasteful, corrupt and fraudulent spending inhibits the ability of the defence sector to respond effectively to national threats. Nearly all of the UK MoD's largest single source suppliers have been investigated for bribery in recent years, as have the MoD's two government-to-government sales agreements with Saudi Arabia. For this reason TI supports enhancing the SSRO's powers to ensure that single source spending is more transparently and effectively monitored.

UK Defence Sector Corruption Risks: A Global Comparison

A 2015 assessment by TI's Government Defence Anti-Corruption Index (GI) found lack of transparency and oversight of single source procurement to be amongst the UK defence sector's highest corruption risks. The GI is an international benchmark that assesses the quality of political oversight and accountability mechanisms, the integrity of personnel, procurement, and finance systems, as well as an evaluation of how militaries behave on operations in over 120 countries. The GI is based on detailed research requiring a network of experts in around 100 countries. Each assessment involves an evidence-based analysis, normally by a country-based academic, which is then subject to intensive peer review, including by representatives from Ministries of Defence. Our team of experts draws together evidence from a wide variety of sources across 77 indicators to provide a detailed assessment of the integrity of each country's defence institutions.

The UK scored high overall in the GI, gaining an A – placing it in the low risk of corruption category, one of only two countries to attain this score worldwide. But the UK gained low scores for transparency and oversight of single sourcing, making this area one of the MoD's highest corruption risks. The UK scored equally low in two other procurement risk indicators: transparency of financial packages and standards expected of companies, subsidiaries and sub-contractors.

Single Source Procurement: Appropriate Checks and Balances

UK single source defence procurement is higher than most European countries. In the Netherlands, less than 10% of the total value of defence contracts is single-sourced. Yet in the last three years the percentage of non-competitively sourced new defence contracts has averaged 53-56% in the UK. This figure does not include the total value of new non-competitive contracts entered into, which increased by almost 60% from £3.4bn to £5.4bn, as a result of a number of large value contracts, with a total spend of £8.3bn on all single source defence contracts in 2014/15.

Unjustified use of negotiated or single source procedures increases the risk of corrupt practices. Most European countries have independent institutions such as a

Court of Audit to scrutinise the choice of procurement procedure. However the SSRO does not have the power to reject the choice of procurement procedure, nor does it have sufficient information to scrutinise whether the use of non-competitive procurement procedures and exemptions is appropriate.

In 2016, TI was invited by the Cabinet Office to review the UK's implementation of its anti-corruption strategy. TI submitted two principal observations regarding the SSRO:

1) The SSRO's role is somewhat constrained. Although the SSRO receives reports on single source defence contracts, this only applies above a certain threshold (£5 million for qualifying defence contracts and £25 million for qualifying sub-contracts), contracts can be exempted by the Secretary of State. Existing contracts that are extended also fall outside the reporting regime. Therefore, not all single source procurement contracts are subject to the price control and transparent open book reporting which the new regime has introduced, serving to limit the SSRO's ability to maintain a complete overview of the total scale of single source defence procurement and apply controls to it.

2) The SSRO's powers are also limited when it comes to oversight over individual procurement decisions. Although the MoD's investment approvals process requires a "strong justification" for the use of single sourcing, this justification is not publically reported and nor does the SSRO have the power to scrutinise or reject the choice of procurement procedure; summon witnesses from government or the private sector and require them to provide information; investigate or follow up on malpractice (malpractice cases are referred back to the ministry; and, in the cases we have been made aware of, appear to lead to no subsequent action by the ministry). Nor does the SSRO have powers to require access to other information held by contractors and enforcement of non-compliance with the regime's requirements sits with the Ministry of Defence. Such powers would lead to greater transparency and accountability amongst suppliers and procurement authorities tendering very high value contracts – giving greater assurance of value for money.

TI recommended two key changes be implemented:

1) A summary of single source procurements and tender justifications should be available to the public.
2) It would be preferable to allow the SSRO, as the regulator, to determine and specify what information needs to be included in the reports it receives. Where information is not reported by contractors, the SSRO should have the powers to require it. The Cabinet Office should consider giving the SSRO powers to seek reports from stakeholders, scrutinise or reject the choice of procurement procedure, approve business cases for single source procurement as in Canada, investigate on the basis of reports, summon witnesses from government or the private sector and require them to provide information, and investigate or follow up on malpractice.

Since that review, the National Audit Office has announced that it will no longer validate the annual performance of the MoD. Meanwhile the MoD is currently embarking on some of its biggest procurement programmes in recent history. This current lack off oversight over secretive defence spending makes it even more vital that an active, independent supervisory body such as the SSRO be given sufficient powers to hold contractors and public officials to account.

A copy of TI's July 2016 submission to the Cabinet Office is attached.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

No response.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

No response.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

No response.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

No response.

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

No response.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

No response.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

No response.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

No response.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

No response.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

No response.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

No response.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

No response.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

No response.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

No response.

17. Issues raised concerning enforcement of price control (section 15).

No response.

18. The proposal for disapplying the price formula (section 17).

No response.

19. Stakeholder proposals supported by the SSRO (section 18).

No response.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

No response.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

No response.

22. Other suggestions for amendments to the legislation.

No response.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

No response.

Attachment: Annex to Transparency submiss

August 2016 Submission to the Cabinet Office on the UK's Anti-Corruption Strategy: *Procurement and Trade*

Part I: Exclusion of corrupt companies/individuals from UK public procurement

The UK Anti-Corruption Summit communiqué made a very strong commitment that "*corrupt bidders should not be allowed to participate in public procurement tenders*" and committed signatories to:

> a) find ways of ensuring that relevant information such as final convictions is made available to contracting authorities; and
>
> b) sharing that information across borders.

A meaningful system of excluding corrupt bidders has two key functions:

> a) it protects the integrity of and public trust in the public procurement process; and
>
> b) it serves as a crucial incentive for enhancing good corporate governance and as a deterrent from engaging in wrongdoing among companies/individuals that wish to bid for public contracts.

The 2009 OECD Recommendations for Further Combating Bribery calls for "*concrete and meaningful steps*" to be taken by signatories to the Convention to ensure that public subsidies, licences, public procurement contracts, contracts funded by official development assistance, officially supported export credits and other public advantages be denied as a sanction for bribery in appropriate cases. In 2014, the OECD Working Group on Bribery stated that the UK had not implemented its recommendations from its Phase 3 report with regard to:

1. establishing a national exclusion register;
2. training public contracting authorities on due diligence with regards to convictions of companies; and
3. providing public Cabinet Office guidance on exclusion, including factors to be considered when deciding whether to convict a company of section 7 of the Bribery Act.

These issues are therefore likely to resurface during the Phase 4 review of the UK's implementation of the OECD Anti-Bribery Convention.

The United States government's experience of procurement exclusion over the last three decades has proven that active and meaningful implementation of a UK exclusion regime would encourage greater self-reporting of economic crime violations by companies at an earlier stage, create a greater incentive for companies to seek a Deferred Prosecution Agreement, and motivate a stronger internal commitment by the company to prevent corrupt activity, in order to avoid exclusion. The new self-cleaning provisions of the 2015 Public Contract Regulations allow companies that can prove that they "*actively collaborated*" with law enforcement authorities, paid compensation and have taken concrete organisational measures to prevent reoffending, to tender for contracts despite conviction for economic crimes.[1]

[1] A similar self-cleansing provision does not exist in the parallel legislation for defence procurement, the Defense and Security Procurement Contract Regulations (DSPCR). Chapter 14, section 18 of the DSPCR includes a derogation authoring procurement authorities to disregard the exclusion of a supplier where there are "overriding requirements in the general interest" which justify doing so, but that the derogation must

If companies knew that there exists a real risk of exclusion from public contracting if they fail to engage in these self-cleaning steps, then they would be more likely to take such steps, including actively collaborating with law enforcement authorities. In essence, the self-cleaning provisions meet the same standards that are set out in a Deferred Prosecution Agreement (which is only available to a company that collaborates with law enforcement, and which requires compensation and remedial organisational measures to be taken). The United States experience suggests that allowing companies offered DPAs to tender, and excluding those that have not, for the set period of time, would significantly increase the number of self-reports made by companies to the SFO. This would in turn lead to improved detection and sanctioning of economic crime by corporations in the UK, as well as helping reduce enforcement costs for the SFO.[2]

For this to have real effect, companies would have to face a real risk of discretionary exclusion for a gross violation of section 7[3] of the Bribery Act. Currently, the UK government has not actively implemented either mandatory or discretion exclusion for companies convicted of any Bribery Act, or equivalent offence.

Mandatory exclusion from public procurement

The UK Defence Ministry has never imposed mandatory exclusion, though it has advised some suppliers not to prepare or submit bids for tenders. This is despite the UK's transposition of 2004, 2009 and 2014 EU Procurement Directives all of which include a provision on mandatory exclusion from procurement where a company, or persons with "powers of decision, representation or control" over the supplier, is convicted of corruption and other economic crimes.

In fact, no UK company/individual appears to have been excluded from procurement by any UK procurement authority. Rather than incentivising good practice by creating penalties for illegal practices, the legislation appears to be effectively ignored. However, even this is hard to assess as no central data appears to be collected which would enable policy makers to determine whether companies have been excluded and whether there is consistency, fairness and predictability in the way the rules are being applied.

Discretionary exclusion for grave professional misconduct and offences such as failure to prevent bribery (s7. Bribery Act 2010)

Similarly, UK procurement authorities do not appear to have used their discretionary exclusion powers to review any contractor who has been convicted of s7 Bribery Act offence or is party to a Deferred Prosecution Agreement. This seems to be the case however severe the economic crimes involved, and without any additional checks taking place to ensure that the company has put in place sufficient measures to mitigate against a reoccurrence of the violations that led to the original criminal investigation. This practice is in direct opposition to the intended objectives of the legislation, which grants greater discretionary exclusion powers than before to procurement authorities to exclude suppliers that undermine public procurement integrity:

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only be used "in the most serious of circumstances...such as a crisis". The factors listed for consideration, such as "the nature and seriousness of the case," could arguably be construed to favour active collaboration. In theory, the wording of the DSPCR provides an even stronger incentive for companies to avoid conviction and seek a Deferred Prosecution Agreement, as the avenue for disregarding exclusion is narrower, but as the UK government has not actively implemented the exclusion regime, the low threat of exclusion currently provides no incentive for companies to collaborate (whether the contractor is governed by the DSPCR or the 2015 Public Contract Regulations). For analysis and data see Transparency International, Evaluation of the functioning and impact of the EU Defence and Security Public Procurement Directive (2009/81/EC) across 20 states, July 2016, http://ti-defence.org/publications/evaluation-eu-defence-security-procurement-directive/

[2] Ibid.

[3] S.7 failure to prevent bribery

a) Sweett Group PLC pleaded guilty in December 2015 to a charge of failing to prevent bribery intended to secure and retain a contract in the UAE. Despite this the company has continued to win multi-million pound contracts from UK public procurement authorities during the investigation and immediately after the conviction;[4]
b) In 2014, AgustaWestland's UK subsidiary entered into a settlement in Italy and was fined €300,000. The parent company, AgustaWestland SPA was fined €80,000 and had €7.5 million confiscated to settle an Italian bribery investigation into the sale of 12 helicopters to the Indian military.[5] Yet –according to articles in The Hindu newspaper and Italian court documents – the scale of the alleged bribery was vast and Indian authorities are investigating whether AgustaWestland paid €60 million in bribes to Indian officials to secure the sale. The strength of the evidence has so far resulted in two senior executives –the former CEO of AgustaWestland and the former CEO of Finmeccanica –being convicted of bribery and sentenced jail for paying bribes to Indian officials to secure the deal.[6] Yet the company's annual report stated that AgustaWestland's settlement "was neither an affirmation of liability, nor an acknowledgment of guilt." The company and its subsidiaries have continued to win defence contracts across Europe, including in Italy and the UK. In recent months Swedish and South Korean enforcement agencies have launched two new bribery investigations into AgustaWestland's sales operations in those markets;
c) In 2010, BAE Systems was ordered to pay £500,000 and £250,000 costs to settle a corruption probe into a £26 million contract for the sale of a radar and air traffic control system to Tanzania. BAE was also ordered to make nearly £30 million of ex-gratia payments to Tanzania. BAE pleaded guilty to one charge of failing to keep proper accounts. The judge said he was "surprised" the SFO had offered BAE "a blanket indemnity for all offences committed in the past", and added that he was "astonished" that the SFO agreed that none of the funds paid by BAE to third parties had been used improperly. The judge said it was "naïve in the extreme" to think that BAE's agent in Tanzania, who was paid more than $12 million via offshore companies, was simply "a well-paid lobbyist";
d) In 2010, BAE Systems settled another bribery investigation with the US Department of Justice and the UK SFO – which had investigated allegations of substantial secret payments made to secure plane leases to the Czech and Hungarian governments, as well as bribes to the Saudi government. BAE pleaded guilty to one charge of conspiring to make false statements to the US government and paid a $400 million fine. This settlement has also allowed BAE to avoid criminal corruption convictions and mandatory exclusion from US and European public contracts. Mike Turner, then CEO of BAE Systems, said in August 2005 that BAE and its predecessor had earned £43 billion in twenty years from the Saudi Al-Yamamah contracts and that it could earn £40 billion more. The DoJ gave a damning condemnation of BAE, which it said had "intentionally failed to put appropriate, anti-bribery preventative measures in place", despite telling the US government that these steps had been taken.

Despite having discretionary exclusion powers, no UK procurement authority has conducted additional checks to ensure that these companies have put in place sufficient measures to mitigate against a reoccurrence of the violations that led to these criminal investigations.

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[4] See Sweett Group News section on Homepage, Civil Service Government Hubs Programme, Brixton Town Centre regeneration prject, London Bridge redevelopment, Public Health England transformation porgramme etc. http://www.sweettgroup.com/news/

[5] Finmeccanica Press Release, 28 August 2014, http://www.leonardocompany.com/en/-/finmeccanicaaccolte-gip-richieste-agustawestland

[6] Both individuals have appealed their sentences to the Italian Supreme Court.

Our research also uncovered a number of European public sector suppliers that have been investigated and convicted of bribery or corruption by European enforcement agencies in the last 3 years, but no evidence that they have subsequently been excluded from public contracts. Many of these suppliers are listed as winning public contracts in the Tenders Electronic Daily (TED) European database. By failing to apply the legislation and allowing companies to evade the possibility of exclusion, the UK government is undermining the exclusion regime by neutralising its intended goal as a deterrent against corruption. Failure to use these legislature powers further removes any incentive for companies to deal promptly and openly with instances of corruption, cooperate with criminal enforcement agencies in the investigation and prosecution of corrupt acts, or implement effective anti-corruption policies.

Discretionary exclusion: The contrasting case of the United States approach to suspension and debarment

Over the last three decades the US debarment system has taken a more risk-based approach to these issues and evolved from a purely mandatory exclusion framework to one that places greater emphasis on discretionary suspension and debarment tools. The US does not seek to punish contractors for past wrongdoing, such as where a company has been convicted of bribery, though this is one of a range of risk factors that is considered. Instead, by authorising procurement officials to analyse a range of factors such as a contractor's control systems, honesty, integrity, ethics, responsibility, competence and what remediation steps the contractor has taken since any malpractice was discovered, the system seeks to give procurement officials (also referred to as suspension and debarment officials) a wide margin of discretion to decide whether to suspend or debar an entity based on the current risks that a contractor poses to the federal government (defined as "present responsibility").

Crucially, United States' procurement officials are not bound to only consider mandatory exclusion factors such as criminal convictions, but can act on the basis of "adequate evidence"[7] to exclude contractors accused of, or under investigation for, misconduct. Only in extreme cases, if a contractor is judged to have taken insufficient steps to remedy the malpractice and therefore represents a continuing risk to US public procurement is an entity or individual debarred. This approach incentivises companies to self-report and demonstrate effective remediation. The most recent annual report from the Interagency Suspension and Debarment Committee (ISDC) indicates a significant increase in the number of contractors self-reporting incidences of malpractice to procurement authorities, in the hope of avoiding more serious penalties such as debarment.

The US approach encourages companies to take responsibility for their own risk management and remediation efforts, in order to demonstrate present responsibility. As a consequence, this limits the government resources required to monitor and investigate malpractice.

In line with this discretionary power, US procurement officials have developed a range of proactive engagement tools, such as pre-notice engagement letters, which give contractors an opportunity to discuss the steps they are taking to address issues, that if left un-remediated, would likely result in suspension and debarment. For example, United States agencies reported a nearly 30 per cent increase from FY 2014 to FY 2015 in the use of show cause or other pre-notice investigative letters. Finally, use of administrative agreements (settlements) increased by 25 per cent from FY 2014 to FY 2015, with

[7] US preponderance of the evidence is equivalent the UK burden of proof in civil trials, judged on the balance of probabilities, as opposed to the criminal burden of proof — beyond reasonable doubt. There is nothing in the wording of the European Directive, or the UK implementing legislation, that suggests discretionary exclusion need be on the basis of the criminal burden of proof, indeed the case of Forposta specifically mentions gross breach of contract as a potential trigger for discretionary exclusion.

companies seeking to settle criminal investigations. The ISDC devotes significant resources to regulatory development support and training, with a particular emphasis on promoting greater procedural consistency, transparency of practice, and fairness in suspension and debarment programs across the Federal Government.

Discretionary Exclusion: weaknesses in the UK's approach

The UK seems to have created a hybrid regime, mixing elements of discretionary and mandatory exclusion provisions, without clarifying its objectives for doing so. The UK discretionary exclusion provisions apply to instances of "grave professional misconduct" on the part of the contractor, and appear to grant broadly similar powers to procurement authorities as the United States discretionary model.

In a recent ruling, the European Court of Justice clarified that the concept of "grave professional misconduct" gives procurement authorities a wide margin of interpretation, and can be applied to "any wrongful conduct which has an impact on the professional ethical standards established by a disciplinary body or for gross breach of contract.[8]

There is nothing in the wording of the Directive that would preclude UK (and European) procurement officials from analysing a range of factors beyond a conviction, such as a contractor's control systems, honesty, integrity, ethics, responsibility, competence and what remediation steps the contractor has taken since the malpractice was discovered, in a similar fashion to US suspension and debarment officials. This discretionary aspect is particularly important given the very low criminal conviction rates in Europe and the increasing number of settlements. However these additional powers are also not being used by the UK government to exclude contractors for cases involving bribery and corruption. Many of the commercial staff we interviewed felt no government pressure to implement the exclusion regime, were unclear on how or when they could apply the provisions and were concerned about potential legal action by suppliers.

Overall, research and interviews indicate four main factors limiting the implementation of the exclusion provisions, which are discussed in more detail below:

a) lack of guidance for procurement officials on exclusion framework objectives, interpretation and implementation including for issues such as derogation and self-cleaning;

b) lack of a robust self-cleaning provision for defence and security procurement. It is possible that this can be elaborated on in the implementing policies and procedures, without requiring legislative change.

c) significant weaknesses in due diligence and information sharing procedures on entities and individuals;

d) lack of political will to exclude (or threaten exclusion) for domestic providers.

[8] C-465/11 Case of Forposta, European Court Justice, 2012 http://curia.europa.eu/juris/liste.jsf?num=C- 465/11&language=EN

Guidance for procurement officials on exclusion framework objectives, interpretation and implementation including for issues such as derogation and self-cleaning

There appears to be no specific or detailed public guidance for contracting authorities on how to interpret the mandatory and discretionary exclusion clauses of the UK Public Contracts Regulations. Contracting authorities are therefore left to determine crucial questions such as, in what circumstances a company convicted under Section 7 of the Bribery Act should be excluded for "grave professional misconduct"; whether a company has self-cleaned adequately (including whether they have cooperated with law enforcement authorities and undertaken necessary corporate reforms) and whether and when a derogation in the national interest can be applied, in a way that is not inconsistent with the bar for self-cleaning. These questions however need legal and specialist advice in order that they can be properly assessed.

For example, the legislation does not stipulate if a derogation should be interpreted as a blanket derogation allowing the company to continue bidding for all public procurement tenders, or if the derogation should be considered on a tender-by-tender basis, depending on whether the required equipment or services can be adequately provided by another supplier.

Because the derogation allows suppliers to escape exclusion and fails to stipulate any remediation or self-cleaning requirements, the existence of the derogation in its current form undermines the goals of the exclusion framework. It also creates a disparity between SME suppliers who will face a greater risk of exclusion for criminal offences than large, single source suppliers, which governments depend on to fulfil single source contracts.

Mabey and Johnson for instance, was the first company to plead guilty to overseas corruption in September 2009, after which it changed its name to Mabey Bridge. Within eight months of being sentenced, the company had won a single source contract through the Department for International Development to provide emergency bridges following an earthquake in Pakistan and another contract in Austria. It went on to win further contracts in Slovenia and Scotland, and was a subcontractor on the building of the East London Line.

It is not clear from our research if all incidences of procurement authorities continuing to trade with convicted companies are being approved internally as a derogation, or if procurement authorities are just ignoring/unaware of the exclusion requirements. To avoid continued abuse, the circumstances in which the derogation can be applied should be clarified, limited and made more consistent with the aims of self-cleaning.

Provisions for ending exclusion if a supplier effectively "self-cleans"

UK defence procurement

The EU recently updated the Public Contract Directive (2014/24/EU) to include a "self-cleaning" provision. In order to prove it has "self-cleaned", a company needs to prove that

a) it has paid or undertaken to pay compensation in respect of damage caused;

b) it has actively collaborated with investigating authorities; and

c) it has taken concrete organisational steps to prevent further criminal offending or misconduct.

This clause grants public procurement authorities and suppliers who have been excluded from public procurement a remediation mechanism, giving the possibility of an end to exclusion for suppliers who are judged to have effectively "self cleaned" –a similar process to that undertaken by US suspension and debarment officials in their decision-making. A company's "self-cleaning" measures must be evaluated against the gravity and nature of the offending. Defence procurement though is explicitly excluded from the directive, and the Defence Procurement Directive lacks this provision.

A senior European defence commercial official flagged the lack of a self-cleaning provision as an inconsistency between two parallel procurement directives – one framework which gives convicted non-defence sector suppliers an opportunity and incentive to remediate, and a separate framework which mandates that governments exclude defence suppliers whatever actions they may have taken to remediate. This current legal inconsistency may give defence sector suppliers legal cause to challenge the Defence Directive as "disproportionate".

UK non-defence procurement

As UK has implemented the latest EU Procurement Directive in the form of the Public Contract Regulations 2015 and the self-cleaning provisions detailed within. Unlike the defence regulations, these are proportional and allow for rehabilitation, but they fail to establish where the bar for integrity lies.

The regulation leaves it to the discretion of contracting authorities to determine whether a company is reliable or has "self-cleaned", and no guidance exists across government to help inform such a judgement. The danger of course is inconsistent implementation, with some authorities accepting a companies' declaration of "self-cleaning" while others don't. Authorities may also feel under pressure to accept companies' assertions of self-cleaning, particularly in the absence of in depth knowledge about compliance and enforcement. Smith and Ouzman is a case in point. The company attended the Association of Electoral Administrators conference, which raised the possibility that a company convicted of corruption may well bid or have bid for contracts to print ballot papers for the last UK General Election and other by-elections. Since many of these contracts would be below the threshold at which the EU Directives apply (£170,000 for central government and its administrative agencies, and £111,676 for all other authorities), Smith and Ouzman are unlikely to run foul of the EU regulations. However, if they were to tender for contracts over that threshold anywhere in the EU, the company would have to prove that it has self-cleaned.

Smith and Ouzman have been trying to establish itself as a company that has self-cleaned: the company has got a BS10500 certificate for Anti-Bribery Management systems. It also claims on its website that it cooperated with the SFO. "The extent of our cooperation", the company claims, "was acknowledged in court on a number of occasions and has not been disputed". The danger is that Smith and Ouzman may be using assertions by their defence counsel in court that they cooperated as official court acknowledgement of their cooperation. Public definitions of the SFO's concept of cooperation by David Green, its Director, require a company to have made an admission of guilt, a prompt notification of the offending to the prosecutor, full disclosure of wrongdoing, compensation to victims and disciplinary action against wrongdoers. If Smith and Ouzman can successfully present itself as a self-cleaned company, despite having contested the charges against it, despite having kept its Directors until a month after they were convicted of corruption, and despite having failed to date to make any compensation to victims, then the objectives of UKs exclusion regime will be rendered meaningless.

UK Procurement Authorities Due Diligence on Supply Chain Corruption Risks

Due diligence checks in the UK are comparatively weak and appear to rely solely on statements made by companies in Pre-Qualification Questionnaires, without further checks. This amounts to a form of self-certification. There are several means through which due diligence procedures could be strengthened:

Widening the net: While authorities could approach the Disclosure and Barring Service for further due diligence checks, it is not clear that this Service would provide useful additional information, given they would likely draw only on information in the Police National Computer. Convictions by the SFO and FCA, the main white collar crime prosecuting bodies, are not automatically entered in to the police national computer and there is no requirement for them to do so. And nor would this provide detail of relevant convictions or current investigations occurring in comparable legal jurisdictions in the European Union and the United States.

Better information sharing across jurisdictions: In February 2016, an EU funded report from Conflict Armament Research investigated the supply chain of weapons in armed conflicts and named 51 commercial entities from 20 countries, including Belgium, the Netherlands, Austria, that are involved in the supply chain of components used by IS to create improvised explosive devices (IEDS).[13]

A lack of information sharing across jurisdiction on relevant convictions is a significant factor limiting the effectiveness of exclusion framework. Our research found no evidence that procurement authorities proactively conduct due diligence on domestic as well as non-domestic entities to check whether suppliers, senior management and sub-contractors have a conviction for corruption, bribery, collusion, money laundering, fraud, terrorist financing or other offences detailed in the procurement legislation. Nor do authorities proactively conduct their own due diligence checks on suppliers' ultimate beneficial ownership, for for links to organised crime or terrorist groups, which are grounds for exclusion in the legislation.

Proactive integrity checks: All UK Defence Ministry prime level contractors must sign a "Statement in Relation to Good Standing" and in some cases a "Dynamic Pre-Qualification Questionnaire" before signing a contract. These are designed to ensure that neither the organisation nor its representatives have a criminal conviction for the offences stipulated in the procurement directives. Defence contractors must then pass Security Clearance. The UK Defence Ministry reserves the right to request further information from the UK Criminal Records Bureau, but this process does not appear to include integrity or due diligence checks on a supplier or on the sub-contractors.

For non-UK suppliers, commercial staff are directed to consult the competent authority of the relevant EU member state. A number of defence ministries including Belgium, Latvia, Lithuania and Greece reported that they ask suppliers to provide a criminal record certificate from their domestic Ministry of Justice but that this procedure differs between countries and it can take considerably longer to receive confirmation from some countries, particularly France. The Belgium Defence Ministry reported that it has no formal proactive due diligence protocol, but that it can request the Intelligence Services to investigate.

Reaching out to additional sources is vital first step. The United States is the most active global enforcer of anti-bribery and economic crime, but the Department of Defense's General Counsel, and most senior suspension and debarment official, Rod Grandon, informed us that no UK procurement authority has ever requested information on US convictions, settlements or entities listed on the US debarment

blacklist prior to awarding UK defence contracts. Current vetting procedures are inconsistent across UK procurement agencies and do not systematically include checks for non-conviction relevant risks such a ultimate beneficial ownership, links to organised crime or terrorism, current investigations, settlements or senior management convictions.

Subcontractors: Beyond the prime contractor level, our research indicates that no due diligence is undertaken of sub-contractors or third parties. While the UK MOD, like other European defence ministries, reserves the right to check and refuse subcontractors and third parties, none systematically do this or could give examples of having done this. In many cases evidence suggests that defence ministries are not aware of which subcontractors or third parties they are contracting with, nor do they require a contractor to confirm that sub-contractors and entities involved in the contract have not been convicted of corruption.

Improving collection and access to enforcement or other relevant information on suppliers: As discussed above procurement authorities' ability to use the mandatory and discretionary provisions depends upon easy access to information from enforcement bodies in all European/comparable legal jurisdictions on current investigations, court cases, judgments and settlements against contractors, their senior management, and subcontractors. Spain operates an Official Register of Debarred Tenderers and Companies.[9] The UK however does not have a consolidated, publicly available list of convictions imposed on individuals or companies for bribery, or other relevant convictions or information.

The SFO's website lists very basic details on the companies and individuals currently under investigation or convicted by the agency. The Crown Prosecution Service does not list any of the investigations or convictions it has secured on its website.[10]

In contrast, all United States procurement authorities, including the US Department of Defence, use a countrywide consolidated electronic database - the Excluded Parties List System – with information on all companies or individuals excluded from receiving Federal contracts. American procurement officials must check the database to ensure they do not award a contract to an excluded bidder. The system is accessed via the System for Award Management, which includes information of various sensitivity levels, depending on the user's level of security access. For members of the public, assessed as having the lowest level of security access, the information that is publicly available includes company name, DUNS unique company identifier, address, whether the entity is currently debarred, and expiration of debarment period.

The benefits of a centralised approach to exclusion decision-making: The US excluded parties list forms the basic infrastructure for keeping excluded contractors from participating in US Government acquisitions. However the decision-making authority to exclude contractors is decentralised, with decision-making authority being vested in suspending and debarring officials across the various federal departments and agencies (Environment, Defence, Health procurement authorities etc.). The activity

9 The OECD Working Group on Bribery has recommended in some country reviews, e.g. Germany, that a national register be established for the purpose of ensuring exclusion of convicted companies from public procurement.

10 According to our research, Italy lacks any accessible central database of investigations and cases. German authorities maintain details of investigations, charges, judgments rendered and other terminations of proceedings, but they anonymise case information and never disclose the names of the defendants nor of the countries involved. This practice is implicitly confirmed by a Federal Administrative Court decision based on the principles of privacy and data protection, notwithstanding the fact that cases are tried in open court and judgments are pronounced in public. In Belgium and Greece even a basic level of statistical data collection concerning bribery enforcement is missing. Similarly in Bulgaria, France, Portugal and Spain the systematic collection and publication of enforcement data has serious shortcomings. See http://ti-defence.org/wp-content/uploads/2016/07/160728-EU-Commission-Defence-Directive-Evaluation-Paper.pdf

levels and effectiveness of the debarment regime varies considerably between agencies, some such as the Department of Defence and Environment, are recognised as being particularly active and effective, other agencies significantly less so. For this reason a decentralised model is generally viewed as less successful than a centralised exclusion model, although the establishment of a central committee, known as the Interagency Suspension and Debarment Committee –responsible for taking steps to promote consistency and best practices across the various decentralized federal agency suspending and debarring officials—has helped to ameliorate some of this issues.[11]

For countries lacking such a long history of suspension and debarment precedents however, a decentralised model would likely lead to duplication of personnel, increased resourcing requirements, and inconsistency in interpretation by different procurement authorities, as well as confusion for contractors. In recent comments, Rodney Grandon, and head of debarment for the US Air Force, argues that a country seeking to establish a new exclusion regime should consider a more centralised model, as such a model promotes from the outset the consistency and predictability necessary to establish credibility and confidence in the exclusion regime by government and industry stakeholders.

The World Bank exclusion system, which based itself on lessons learnt from the US framework, has opted for a centralised model. This allows for a very small unit of experienced, highly trained personnel thereby increasing uniformity, certainty and limiting the financial resources required from the World Bank. With an annual operating budget of over $60 billion – broadly equivalent to the UK's defence budget - the World Bank's Suspension and Debarment Office publishes a similarly transparent information database to that made accessible by the US Federal Government.

Its website lists the firms and individuals that are ineligible to be awarded a World Bank-financed contract, because they have been sanctioned under the Bank's fraud and corruption policy. Details available to the public include the firm's name, address, country, period of ineligibility (date starting and ending) and grounds for sanction. The list also includes other sanctions such as conditional non-debarment, broadly similar to a UK Deferred Prosecution Agreement and imposed when companies have demonstrated to the World Bank that they have taken comprehensive corrective measures and that other mitigating factors apply, so as to justify non-debarment.

Recommendations

The Cabinet Office /Crown Commercial Service should produce for public consultation written guidance for procurement officials on how to interpret exclusion from public procurement (this was done with the 2006 Regulations by the then Office of Government Commerce). This guidance should cover:

the objectives of the UK's exclusion framework and how it will deter companies from committing corrupt acts, encourage companies to implement effective anti-corruption policies, deal promptly and openly with any instances of corruption and cooperate with the authorities in the investigation and prosecution of corrupt acts;

11 Section 4 of Executive Order 12549 on Debarment and Suspension directed the establishment of the Interagency Suspension and Debarment Committee (ISDC) to monitor implementation of the Order. This Order mandates Executive departments and agencies to: Participate in a government-wide system for debarment and suspension from programs and activities involving Federal financial and nonfinancial assistance and benefits; Issue regulations with government-wide criteria and minimum due process procedures when debarring or suspending participants, and Enter debarred and suspended participants' identifying information on the General Services Administration list of excluded persons, now known as the System for Award Management (SAM). Information placed on SAM is the responsibility of the Agency issuing the suspension or debarment action.
The ISDC also facilitates lead agency coordination, serves as a forum to discuss current suspension and debarment related issues, and assists in developing unified Federal policy. When requested by OMB, the ISDC serves as a regulatory drafting body for revisions to the government-wide nonprocurement suspension and debarment common rule.

how authorities should deal with contractors, agents and sub-contractors under investigation for offences listed in the Regulations in the UK and comparable legal jurisdictions;

how authorities should determine whether a contractor or sub-contractor has self-cleaned and produce clear and independent criteria upon which this determination could be made, and what similar provisions and incentives can be extended to defence contractors;

how authorities should determine whether a company that has been subject to a Deferred Prosecution Agreement, or a conviction for a Section 7 offence under the Bribery Act, has effectively implemented sufficient measures to no longer represent a risk to public procurement, with clear and independent criteria for how to determine these cases;

in what circumstances authorities can apply a derogation in the national interest from the exclusion clauses, and how to ensure such derogations do not undermine the purpose of the regulations and the benefits they bring to improved corporate governance;

how authorities can access information on convictions, settlements and current investigations into domestic/foreign contractors, their senior management and relevant group/parent entities bidding for contracts or being awarded sub-contracts.

2. The Cabinet Office should ensure that the CCS collect centralised data on exclusion of contractors and sub-contractors, ensuring that reasons are given for where exclusions are applied or not, and for derogations. The CCS should publish such data on an annual basis, we recommend that the Cabinet Office considers the exclusion databases published by the United States government and the World Bank.

3. Real consideration should be given to setting up:

a) a national exclusion register which can act as a one-stop shop for procurement officials to go to for information on exclusions (such a register should include both convictions, settlements, current investigations as well as decisions made to exclude), which, like the US database, could have varying levels of information tailored to security access i.e. the public, UK/European and US procurement officials, intelligence officials in five eyes defence ministries; and,

b) a central unit to offer specialist advice to procurement officers, collect centralised data and to make a determination regarding under what circumstances companies should be excluded on a mandatory/discretionary basis, the application of a derogation and self-cleaning. Close consideration should be given to the World Bank's centralised decision-making model.

Both of these steps would significantly improve implementation of the exclusion provisions of the Regulations as well as ensuring consistency, fairness and predictability.

4. To ensure that steps taken in the UK on excluding corrupt companies are part of a multilateral approach which creates a level playing field internationally, the UK should take two steps:

a) the Cabinet Office should work with the new Brexit trade team to ensure that public procurement exclusion clauses are included at the very least in trade deals made with signatories to the UK Summit Communiqué to ensure implementation of the Summit Commitment; and

b) work with the OECD Working Group on Bribery to ensure that Phase 4 reviews specifically look at whether countries are abiding by their OECD commitment to ensure exclusion of convicted companies

from public procurement and other public advantages, and develop consistent recommendations on the setting up of national registers and the need for guidance to procurement officials.

Part II: UK Model Contracts for Public Procurement

The Model Contract terms issued by the Cabinet Office, Crown Commercial Service (CCS) and the Government Legal Service in April 2014 have specific provisions, including contract cancellation, to deal with corruption and related issues. This is a promising step, and gives greater clarity to suppliers and procurement authorities on the standards of behaviour expected, and the conditions in which discretionary debarment might be imposed, or a contract can be cancelled. What is not clear is if the use of model contracts is mandatory for procurement authorities, or what sectors they apply to. We have found no evidence for example that model contracts are being used by the MOD's commercial department, or that procurement officials are even aware of their existence.

There is also room for improvement in the drafting of the Model Contracts. Provisions are currently somewhat vague, too narrowly defined, and do not adequately reflect UK and European procurement and bribery legislation. Nor do they clarify to procurement authorities and suppliers what actions constitute breach of contract and may therefore trigger debarment. Finally, there may be merit in tailoring model contracts for specific types of procurement such as defence and pharmaceuticals.

The Current Approach: Large value contracts

The Model Services Contract has been developed for services contracts with a value over £10 million. We have identified several areas where contract could be improved or strengthened:

Clarity on penalties: neither section 39.6, nor any part of the contract, stipulates that the penalty for breach would trigger a process that may lead to discretionary exclusion from public procurement, as previously highlighted discretionary exclusion was explicitly designed for breach of contract.[12]

The scope of application: The definition of 'government' in section 39.1 (b) of the Model Services Contract is not clear, it seems likely it is only intended to apply to the UK government. It should be broadened to include equivalent legal jurisdictions such as the USA and European Union member states:

"*The Supplier represents and warrants that neither it, nor to the best of its knowledge any Supplier Personnel, have at any time prior to the Effective Date: (a) committed a Prohibited Act or been formally notified that it is subject to an investigation or prosecution which relates to an alleged Prohibited Act; and/or (b) been listed by any government department or agency as being debarred, suspended, proposed for suspension or debarment, or otherwise ineligible for participation in government procurement programmes or contracts on the grounds of a Prohibited Act.*"

The use of agents: Section 39.2(b) is rather narrow, and does not include the supplier's agents, one of the highest risks in procurement. In 2013 for example, more than 90 per cent of reported US foreign bribery cases involved third party intermediaries.[13] If it is found, as currently alleged, that Rolls Royce did use agents abroad to pay bribes to secure contracts, this would fall outside of the terms of this contract:

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[12] In a recent ruling, the European Court of Justice clarified that the concept of "grave professional misconduct" gives procurement authorities a wide margin of interpretation, and can be applied to "any wrongful conduct which has an impact on the professional ethical standards established by a disciplinary body or by a judgment which has the force of res judicata", including "breach of contract". C-465/11 Case of Forposta, European Court Justice, 2012 http://curia.europa.eu/juris/liste.jsf?num=C- 465/11&language=EN

13 http://ti-defence.org/agents-pose-major-corruption-risks-arms-deals/

"*The Supplier shall not during the term of this Agreement: (a) commit a Prohibited Act; and/or (b) do or suffer anything to be done which would cause the Authority or any of the Authority's employees, consultants, contractors, sub-contractors or agents to contravene any of the Relevant Requirements or otherwise incur any liability in relation to the Relevant Requirements*."

Encouraging the use of compliance programmes: Our research has identified that improvements in anti-corruption controls are driven primarily by both governments and contractors engaging in a self-assessment that assesses and seeks to mitigate their risk exposure. The companies and governments that score highest in the Transparency International Government Defence Anti-Corruption Index and the Defence Companies Anti-Corruption Index share one approach to best practice – a requirement that suppliers put in place a robust compliance or business conduct program that adheres to minimum standards established by the government.

For higher value procurement contracts over $5 million, the United States government requires that suppliers conduct a corruption risk assessment and put in place robust compliance program together with training for all employees and subcontractors. These provisions apply equally to subcontractors and agents of the main contractor. The compliance program must adhere to minimum standards stipulated by the US government in the Federal Acquisition Regulations.[16] To ensure corporate responsibility and adherence to the rule of law, the Cabinet Office might consider a similar requirement for UK higher value procurements.[14] This would ensure that the UK's prosperity agenda is not undermined by malpractice.

The threshold for application: seems unnecessarily high, in the United States for example, including for defence procurement, model contracts are mandatory and the provisions apply to tenders over a value of $5 million. We were unable to find any evidence in our research the section 39.3 is being followed by procurement authorities, indeed anecdotal evidence suggests the contrary:

"*The Supplier shall during the term of this Agreement: (a) establish, maintain and enforce, and require that its Sub-contractors establish, maintain and enforce, policies and procedures which are adequate to ensure compliance with the Relevant Requirements and prevent the occurrence of a Prohibited Act; and (b) keep appropriate records of its compliance with its obligations under Clause 39.3(a) and make such records available to the Authority on request*."

Enforcement: We were unable to find any evidence in our research the section 39.4 is being enforced by procurement authorities, our evidence suggests the contrary:

"*The Supplier shall immediately notify the Authority in writing if it becomes aware of any breach of Clause 39.1 and/or 39.2, or has reason to believe that it has or any of the Supplier Personnel have: (a) been subject to an investigation or prosecution which relates to an alleged Prohibited Act; (b) been listed by any government department or agency as being debarred, suspended, proposed for suspension or debarment, or otherwise ineligible for participation in government procurement programmes or contracts on the grounds of a Prohibited Act; and/or (c) received a request or demand for any undue financial or other advantage of any kind in connection with the performance of this Agreement or otherwise suspects that any person or Party directly or indirectly connected with this Agreement has committed or attempted to commit a Prohibited Act*."

14 This is not a significant burden to require of UK companies bidding for larger contracts. Due to the global nature of defence (or pharmaceutical) sales, many trade with the United States and are already required to have an ethics and anti-corruption program in place. Harmonising this requirement would help to improve standards internationally by aligning UK practices with current global best practice.

Regulating illegal behaviour: We also assessed the extent to which UK and European defence ministries use model contracts to regulate illegal behaviour and notify bidders of their legal obligations. According to the European Court of Justice's interpretation of the discretionary exclusion provisions for "grave professional misconduct" this can include a gross "breach of contract". Breach of a contractual clause gives procurement authorities the power to terminate a contract or act immediately to exclude a contractor in the event of misconduct. For example, the United States' model contract terms require contractors, including subcontractors, above a certain threshold to:

1. Prohibit kickbacks (applies to all contracts exceeding the simplified contract threshold)
2. Provide for the Cancellation, Rescission, and Recovery of Funds for Illegal or Improper Activity (applies to all contracts except commercial purchases)
3. Allow for Price or Fee Adjustment for Illegal or Improper Activity
4. Require certification and Disclosure Regarding Payments to Influence Certain Federal Transactions. (Applies to contracts above $100,000)
5. Require a Contractor Code of Business Ethics and Conduct 52.203-13 (applies to contracts above $5 million)
6. Require display of a Hotline Poster(s) (52.203-14, applies to contracts above $5 million)
7. Require whistleblower protections Under the American Recovery and Reinvestment Act of 2009 (52.203-15, applies to all contracts above the simplified contract threshold).

Breach of contract: The UK's position on gross breach of contract and violations of the law is not clear and seems to be inconsistent between sectors. In contrast, the United States Federal Acquisition Regulations formally require that the main contractor adopts a comprehensive compliance and ethics programme for tenders over $5 million, together with training for all employees and subcontractors, within 90 days of the contract award. It also stipulates that these provisions apply equally to subcontractors and agents of the main contractor. The main contractor is also obliged to self-report any ethical and compliance violations committed by it or by a subcontractor to the manager of the Contractor Disclosure Program at the DOD Inspector General's office, or face the risk of debarment.

The Current Approach: Lower value contracts

According to the Cabinet Office's website, the short form terms and conditions developed by the Crown Commercial Service and the Government Legal Service is for general goods and services contracts with a value below the procurement thresholds set out in the Public Contracts Regulations 2015. The documents are designed to ensure that procurement authorities are able to use appropriate and proportionately 'light touch' contract terms for low value procurements. It is unclear why these do not cover defence procurement, and this may suggest the Cabinet Office is settling a lower bar for integrity and compliance for SME defence suppliers.

Similarly, as with the Model Service Contract above, no mention is made in the contract that breach of contract or failure to self-report would trigger a process that may lead to discretionary exclusion. Section 1.1 is also too narrow a definition of fraud and corruption, and does not extend to supply chain sub-contractors. It should match the procurement directives implemented into UK law, for example including offences such as money laundering, collusion, bribery of foreign officials etc. Finally, section 1.1 refers to "*good industry practice to prevent fraud*", but gives no guidance on what this might be.

Recommendations

The Cabinet Office should review the contractual provisions in the Model Contracts to ensure that they reflect both the needs of different sectors, as well as the current legislation regulating economic crimes, exclusion and procurement, and set the bar for integrity sufficiently high across different sectors.

For high value procurements, real consideration should be given to making a comprehensive compliance and ethics programme, that adheres to minimum standards established by the Cabinet Office, a formal requirement for prime contractors, together with training for all employees and subcontractors. These provisions should apply equally to subcontractors and agents. The main contractor should be obliged to self-report any ethical and compliance violations committed by it or by a subcontractor, or face a risk of discretionary exclusion for gross breach of contract.

Part III: Bilateral Trade Agreements and Government-to-Government Defence Sales

The UK's 2014 Anti-Corruption Strategy made a strong commitment to "*raise global standards, build prosperity, and promote sustainable global growth, open markets and fair access to resources. The UK's leading role in the global trade and financial systems, and our commitment to international aid places a particular responsibility on government to lead the response to business-related bribery and illicit financial flows.*" The prospect of bilateral trade negotiations with the European Union, United States, China and Commonwealth states such as India, Canada, Nigeria, Kenya, and others, will be a test of the UK's commitment to put this commitment into practice.

Transparency International consistently ranks corruption in procurement as the highest corruption risk facing governments.[15] A meaningful trade policy, and in particular bilateral trade agreements and government-to-government defence sales, should be aligned with international anti-corruption frameworks to ensure that all parties adopt and actively implement global anti-corruption conventions, and that corrupt contractors are not allowed to prosper in domestic or international markets, thereby contributing to sustainable, positive growth and increased prosperity.

The Cabinet Office should take heed of recent public protests during negotiations for the Transatlantic Trade and Investment Partnership (TTIP) and ensure transparency at each stage of negotiations for both bilateral trade agreements and government-to-government defence sales. Opacity in bilateral trade generates and amplifies serious risks of undue influence and policy capture by well-connected, well-resourced interests to the detriment of SMEs, consumers and the public. Studies have shown that aligning policies that enhance transparency in regional trade agreements increases bilateral trade by more than 1 per cent.[16] A meaningful system to ensure increased prosperity from trade should guarantee greater transparency at each stage of the trade and government-to-government sales agreement process. This will help ensure that all relevant interests can be articulated and considered, and deliver the best possible outcomes for society.[17]

Increasing prosperity and removing obstacles to global trade and foreign investment are the primary objectives of trade agreements. Corruption, on the other hand, is a major obstacle to achieving those goals; it distorts the fair awarding of contracts, reduces the quality of basic public services, limits opportunities to develop a competitive private sector and undermines trust in the rule of law. Analysts estimate that corruption generates trade costs equivalent to those rising from trade tariffs.[18] Transparency International and Corruption Watch UK have highlighted the poor record of procurement malpractice enforcement worldwide, particularly where it relates to the sale of defence and security materiel.[19]

15 See for example http://ti-defence.org/publications/evaluation-eu-defence-security-procurement-directive/ and http://government.defenceindex.org/#close
16 Iza Lejárraga and Ben Shepherd, Quantitative Evidence on Transparency in Regional Trade Agreements, Trade Policy Paper no. 153 (Paris: Organisation for Economic Co-operation and Development, 2013). Lejárraga and Shepherd further note that the expected increase in intraregional trade could be over 15 per cent: see page 5.
17 Cary Coglianese, Heather Kilmartin and Evan Mendelson, 'Transparency and Public Participation in the Rulemaking Process: Recommendations for the New Administration', George Washington Law Review, vol. 77 (2009), 924–72.
18 James Anderson and Douglas Marcouiller, 'Insecurity and the Pattern of Trade: An Empirical Investigation', The Review of Economics and Statistics, vol. 84 (2002):
19 http://www.transparency.org/exporting_corruption see also http://ti-defence.org/publications/evaluation-eu-defence-security-procurement-directive/

The European Union estimates that corruption costs its economy €120 billion per year[20] - slightly less than the entire yearly EU budget and the same amount that an EU-commissioned Centre for Economic Policy Research study[21] estimates as a one-time potential gain for the European Union, once the TTIP is fully implemented. Measures to safeguard and promote the integrity of business in bilateral trade and government-to-government sales agreements should therefore be given equal attention as the potential benefits that each could release.

According to the European Commission's own analysis, public procurement is an area particularly prone to corruption. A 2013 EU Anti-Corruption Report on corruption relevant to business found that more than three out of ten European companies participating in public procurement cited corruption as the reason they were unable to win a contract. Indeed, more than one-half of all companies viewed corruption as widespread - 56% in procurement managed by national authorities and 60% in regional or local procurement – with little evidence of active criminal enforcement against corrupt actors.[22]

Similarly, the SFO's current investigations for example into allegations of bribery at Rolls Royce in its business dealings in Nigeria, India, Brazil, Indonesia, China and South Korea, highlight the very real risks to both SMEs and large, sophisticated companies in their dealings with public officials abroad. To address these risks, the UK should include strong and effective anti-corruption provisions in bilateral trade and government-to-government agreements.

A meaningful anti-corruption trade policy should also reflect the specific types of corruption risks associated with specific trade partners and business sectors. The EU Anti-Corruption Report for example, diagnosed some of the most frequently occurring types of corrupt practices including: drafting of tailor-made specifications to favour certain bidders; splitting of public tenders in smaller bids to avoid competitive procedures; disproportionate and unjustified selection criteria; unjustified exclusion of bidders; unjustified use of emergency procedures and unjustified exceptions

from publication of bids.[23] Other methodologies exist for a sectoral risk assessment using qualitative and quantitative data, such as Transparency International's Government Defence Anti-Corruption Index,[24] which has subsequently been developed by NATO into the Self Assessment Questionnaire for current and prospective member states.

The current approach

The revised World Trade Organisation's Government Procurement Agreement (GPA),[25] recognises in its preamble the importance of avoiding conflicts of interest and corrupt practices, in accordance with applicable international instruments, such as the United Nations Convention Against Corruption. However, the text of the GPA only includes a general admonition to procuring entities to conduct their procurement in a transparent and impartial. Overall it is insufficient to address corruption in the life cycle of an actual procurement process.[26]

20 http://ec.europa.eu/dgs/home-affairs/e-library/documents/policies/organized-crime-and-human-trafficking/corruption/docs/acr_2014_en.pdf
21 Centre for Economic Policy Research, Reducing Transatlantic Barriers to Trade and Investment: An Economic Assessment (London: Centre for Economic Policy Research, 2013), available at http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc_150737.pdf
22 Transparency International's most recent reports on the enforcement of foreign bribery legislation and malpractice in defence procurement showed that 11 EU countries – Belgium, Bulgaria, Czech Republic, Denmark, Estonia, Ireland, Luxembourg, Poland, Slovenia, Slovak Republic and Spain – have shown evidence of little or no enforcement of obligations under the OECD convention prohibiting bribery of foreign officials. Only two EU countries – UK and Germany – are considered to be actively enforcing the convention.
23 http://trade.djaghe.com/
24 https://government.defenceindex.org/#close
25 https://www.wto.org/english/tratop_e/gproc_e/gp_gpa_e.htm
26 Transparency International Working Paper 02/2016, Transparency and Corruption: A Role In Mega Trade Deals

Globally, the USA sets the current standard for anti-corruption provisions in trade and investment agreements. More recently, the European Commission has pledged to include "ambitious" anti-corruption provisions and to increase transparency in all future trade deal negotiations, including the proposed TTIP.[27] Previous bilateral agreements with major trading partners, South Korea for example, have not included these provisions.

To date, the most advanced anti-corruption trade agreement is the Trans-Pacific Partnership (TPP), which, at the end of 2015, included a specific chapter devoted to transparency and anti-corruption.[28] This includes provisions for the exclusion of corrupt contractors from public procurement, whistleblower protection, no impunity for officials charged with corruption offences, steps to reduce the secrecy and abuse of anonymous shell companies, and the requirement for governments to consult with civil society on their anti-corruption commitments – a position that is increasingly being reflected by the EU and Canada. The TPP has set an important precedent, but its contribution to prosperity will be determined by its actual implementation and enforcement.[29]

It is expected that in the TTIP, the European Union and the USA will go beyond the provisions that are typically found in US free trade agreements (FTAs) –the UK should aim to meet that higher bar. Those FTAs generally include a provision on Ensuring Integrity in Government Procurement Practices that requires the parties to ensure that criminal or administrative penalties such as discretionary and mandatory exclusion from public procurement are available to sanction malpractice. The use of administrative penalties alone is not ideal for discouraging criminal behaviour, but their inclusion does gives parties flexibility to incentivise integrity, in circumstances where a trade partner's criminal enforcement institutions may lack the independence or resources to mount a successful criminal prosecution as often as they should.

Since the release of confidential negotiation documents in TTIP Leaks[30], and other public protests, the European Union has stated to publish online all position papers submitted to the United States in the framework of TTIP negotiations, and has made efforts to explain the content of the agreement to less well represented groups such as SMEs, consumers and the general public. The EU Commission has started to hold regular stakeholder briefings after each negotiation round, as well as what it calls 'Civil Society Dialogues.'[31] The UK should ensure that it, as well as any bilateral trade partners, follows a similar process for their citizens. This should include the removal of legal provisions that limit access to information. Our view is that freedom of information restrictions should be aligned with international best practice,[32] which suggests that there has to be a 'pressing social need' for the information restriction.[33]

27 http://www.transparencyinternational.eu/2015/10/press-release-eu-trade-deals-to-include-ambitious-anti-corruption-proposals/
28 The European Union has announced that it intends to advocate in favour of such a chapter in TTIP as well, but no draft text has yet been published. CETA includes corruption provisions only in its chapters on government procurement and on ISDS.
29 http://www.transparencyinternational.eu/wp-content/uploads/2014/03/2014-03-07_TI_Letter-to-Karel-de-Gucht-FINAL-doc.pdf
30 https://www.ttip-leaks.org/
31 See http://trade.ec.europa.eu/civilsoc/meetdetails.cfm?meet=11411 (first meeting: 16 July 2013) and http://trade.ec.europa.eu/doclib/docs/2016/june/tradoc_154661.pdf (30 May 2016).
32 This is in line with how article 19 of the International Covenant on Civil and Political Rights is interpreted by the UN Human Rights Council, as in the Report of the United Nations High Commissioner for Human Rights and Follow-up to the World Conference on Human Rights: Addendum, A/HRC/10/31/Add.3 (New York: United Nations, 2009), 7; and how article 10 of the European Convention of Human Rights is interpreted by the jurisprudence of the European Court of Human Rights, as in Freedom of Expression in Europe: Case-Law Concerning Article 10 of the European Convention on Human Rights, Human Rights File no. 18 (Strasbourg: Council of Europe Publishing, 2007).
33 Agnes Callamard, Expert Meeting on the Links between Articles 19 and 20 of the ICCPR: Freedom of Expression and Advocacy of Religious Hatred that Constitutes Incitement to Discrimination, Hostility or Violence (Geneva: Office of the United Nations High Commissioner for Human Rights, 2008), 5, available at www2.ohchr.org/english/issues/opinion/articles1920_iccpr/docs/experts_papers/Callamard.doc.

Government-to-government defence and security sales

Government-to-government defence sales are conducted in complete secrecy, legally exempt from any freedom of information requirements,[34] and in the absence of any anti-corruption provisions.[35] They can therefore pose a particular set of corruption risks. Government-to-government defence sales with Saudi Arabia are the most striking example of the UK's failure to include appropriate anti-corruption provisions in bilateral trade agreements and the potential for these shortcomings to actively undermine the UK government's prosperity agenda and global reputation. The SFO is currently investigating allegations that the UK government's prime contractor to Saudi Arabia, GPT Special Project Management, now a subsidiary of Airbus, bribed officials to secure a GBP1.5 billion contract, SANGCOM, to design, operate and maintain communications systems to the Saudi National Guard.[36]

The heightened risk of corruption in UK government-to-government sales with Saudi Arabia is reinforced by an earlier SFO investigation into the Al-Yamamah case, which included near identical allegations that the UK government's prime contractors for the project – in that instance BAE Systems – had paid hundreds of millions of pounds in bribes to Saudi officials.

Government-to-government sales: are lessons being learnt?

The 2015 Transparency International Government Defence Anti-Corruption Index ranked the Saudi Arabia Ministry of Defence in Band E, the second highest risk of corruption category, Saudi Defence sector procurement risks scored in Band F, the highest risk category.[37] Yet despite a widespread awareness of these risks, government-to-government defence sales are negotiated without any meaningful assessment of the corruption risks to the UK government and its contractors, and seemingly without any meaningful attempts to mitigate those risks. Little seems to have been learnt through either the GPT or Al-Yamamah case.

As far as we are aware, there has been no internal MOD review, or independent external review to identify any institutional failings.[38] This is in stark contrast to the response by BAE Systems in the wake of Al-Yamamah, which set up a transparent and independent ethics committee, headed by the former Lord Chief Justice, Lord Woolf, to investigate the way it does business and ascertain whether its practices conformed with the highest ethical standards. A criminal investigation by the SFO is not sufficient for this purpose –its objective is to identify criminal liability, not to identify the strengths or weakness in the MOD's internal checks and procedures. Criminal investigations take many years to conclude, leaving the MOD and UK government meanwhile at a continued risk of exposure to the same failings.

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34 Financial Times, UK-Saudi contract details can stay secret, tribunal rules, 24 July 2015, https://next.ft.com/content/cd7b0b3e-31f5-11e5-91ac-a5e17d9b4cff

35 The EU Directive 2009/81/EC on defence and sensitive security procurement sets very broad exclusions to transparency, reporting and competition such as government to government sales.

36 SANGCOM: The Saudi Arabia National Guard Communications Project (SANGCOM), The SFO is examining whether GPT bribed individuals in connection with its contract to supply communications equipment to the Saudi national guard.
Details about gifts allegedly given to Saudi generals, and payments made to a Cayman Islands bank account, were passed to the SFO by Ian Foxley, a former Saudi-based employee of GPT. GPT has a contract to design, operate and maintain communications systems to the Saudis under a government-to-government programme called Sangcom. The Ministry of Defence is GPT's sole customer under the contract.
https://next.ft.com/content/c930e308-06ba-11e4-b0d3-00144feab7de

37 http://government.defenceindex.org/countries/saudi-arabia/ and summary of scores and recommendations http://government.defenceindex.org/downloads/docs/saudiarabia.pdf

38 In 2012 the enforcement agency allowed Airbus to carry out an internal inquiry into the whistleblower allegations. https://next.ft.com/content/c930e308-06ba-11e4-b0d3-00144feab7de

One obvious area for examination is the mandate and role of British officials in such contracts. According to the current Minister of Defence more than 53 UK MOD staff continue to be employed by SANGCOM, the Saudi National Guard communications project.[39] The SFO has questioned several UK MOD officials in connection with its investigation, as the UK MOD is GPT's sole customer under the contract, and is supposed to approve GPT's expenditures. Project personnel have the following defined roles:[40]

a) facilitate contact between the Saudi Armed Forces and the prime contractor, thereby helping to define programme requirements and to expedite the resolution of problems;

b) ensure equipment and services provided to the Saudi Armed Forces are as contracted and that all supporting training is carried out to an acceptable standard;

and c) endorse claims for payment when properly supported and submitted in accordance with the payment schedules in the relevant agreement.

The Saudi Arabian Government reimburses the UK MOD for these staff costs, which could serve to discourage UK staff from robustly and independently overseeing contracts, or feeling sufficiently empowered to raise issues.

UK Ministry of Defence Employees employed by SANCOM[41]

Manpower as at 1 April 2016	SANGCOM Project
UK-based Civilian Staff	2
UK-based Military Staff	0
Saudi Arabia-based Civilian Staff	31
Saudi Arabia-based Military Staff	20

The Ministry of Defence Saudi Armed Forces Projects, MODSAP,[42] which oversees Al-Yamamah, employs an even larger number of MOD staff than SANGCOM. Project personnel roles are as defined above.

UK Ministry of Defence Employees employed by MODSAP[43]

Manpower as at 1 April 2016	MODSAP

39 http://www.parliament.uk/business/publications/written-questions-answers-statements/written-question/Commons/2016-06-28/41412
40 http://www.baesystems.com/en/our-company/our-businesses/bae-systems-saudi-arabia/our-partners/modsap
41 http://www.parliament.uk/business/publications/written-questions-answers-statements/written-question/Commons/2016-06-28/41412
42 The Ministry of Defence Saudi Armed Forces Project (MODSAP) covers the Saudi British Defence Co-operation Programme, formerly known as Al Yamamah (sale of Tornado, Hawk and PC-9 aircraft to the Royal Saudi Air Force) and the Al Salam programme (sale of Eurofighter Typhoons to the Royal Saudi Air Force).
43 ibid.

UK-based Civilian Staff	73
UK-based Military Staff	31
Saudi Arabia-based Civilian Staff	37
Saudi Arabia-based Military Staff	68

The UK government also failed to conduct an independent inquiry into the UK MOD's part in Al-Yamamah, and narrowed the SFO's criminal investigation into Al-Yamamah on national security grounds in 2006, despite a public appeal from the Directors of Transparency International UK, Global Witness and Corruption Watch UK to the Attorney General urging no interference in the SFO investigation.

BAE eventually paid $400m to US authorities in order to settle the bribery allegations. In 2007, BAE earned 12.6% of its revenues from MODSAP, increasing to 20.2% in 2013.[44] Prior to the settlement, Mike Turner, then CEO of BAE Systems, said in August 2005 that BAE and its predecessor had earned £43 billion in twenty years from the Al-Yamamah contracts and that it could earn £40 billion more—highlighting the limits of to ensuring corporate responsibility and adherence to the rule of law through fines alone. The DoJ gave a damning condemnation of BAE, which it said had accepted "intentionally failing to put appropriate, anti-bribery preventative measures in place", despite telling the US government that these steps had been taken. Criminal investigations are too few, and fines too low, to act as an effective deterrent to corporate malpractice on their own – the UK's SFO is one of the most active enforcement agency outside of the USA but has never successfully prosecuted a defence company for corruption. To be truly effective criminal enforcement needs to be combined with a real risk of exclusion from public contracting.

BAE's motive in settling the case, and agreeing to conditions such as payment of a fine and remediation, was strongly influenced by a desire to avoid the risk of exclusion from public contracting. A criminal conviction would have triggered mandatory exclusion from European Union public procurement contracts and potential debarment from all US federal contracts. Rodney Grandon, Deputy General Counsel and chief suspension and debarment official in U.S. Department of the Air Force, has argued that the threat of debarment from all US Government agency tenders during the period of exclusion has driven deep and positive changes affecting internal controls, compliance and ethics in many contractors that compete for or perform contracts worldwide. The US record of discretionary debarment over the last 30 years has shown that one of the most effective ways of ensuring that companies act responsibly, ethically and adhere to the rule of law when participating in the government marketplace is by establishing legal authorities that align responsible corporate behaviour with a corporation's financial interests. The threat of mandatory or discretionary exclusion from public contracting is the most effective way of ensuring that a company's financial rewards (maintaining access to public procurement) are aligned with the company's own efforts in ensuring that its personnel do not break the law.

44 https://deceptioninhighplaces.com/arms-trade/summary-of-britains-biggest-arms-deals-with-saudi-arabia/

Recommendations

1. Set up a transparent and independent ethics committee review to investigate the way the UK MOD does business and ascertain whether its practices in Saudi Arabia conform with the highest ethical standards.
2. Include a solid anti-corruption framework in bilateral and regional trade agreements, and government-to-government sales that aligns with global standards:[45]
    a. include a general commitment to fighting corruption, with explicit reference to both the UN Convention against Corruption and the Organisation for Economic Co-operation and Development's Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (usually referred to as the OECD Anti-Bribery Convention), ensure that all non-parties join the two conventions;
    b. include robust anti-corruption provisions in all the chapters of a trade agreement that are potentially exposed to corruption - serious consideration should be given to those proposed by Transparency International for inclusion in TTIP[46] - this should also reflect the specific types of corruption risks associated with that trade partner or business sectors;
    c. require the exclusion of suppliers that have engaged in corruption, fraud or other illegal acts from participation in public procurement, also requiring the parties to take measures to combat corruption in matters affecting trade and investment;
    d. these provisions should include whistleblower protection, no impunity for officials charged with corruption offences, steps to reduce the secrecy and abuse of anonymous shell companies, and the requirement for governments to consult with civil society on their anti-corruption commitments;
    e. focus attention on enforcement implementation: monitor and publicly report on the implementation of anti-corruption commitments in bilateral and regional trade agreements and government-to-government defence sales by building on the parallel monitoring use by Transparency International and others of international anti-corruption instruments;
    f. require companies seeking to participate in procurement to provide "documentation from competent authorities". The required documentation includes certifications that companies have paid taxes and social security obligations and have not been in bankruptcy, and that their managing directors and board members have not engaged in fraud, money laundering or criminal activity.[47]

3. Establish clear and transparent accountability channels for all stakeholders in the implementation of the agreement:
    a. establish a common, mutually agreed disclosure policy;
    b. ensure that all relevant domestic institutions and actors – particularly Members of Parliament and their advisers – have timely and complete access to negotiating documents;
    c. limit confidentiality between parties as much as possible throughout the negotiation process;

45 These recommendations are based on Transparency International's WORKING PAPER #2 2016: TRANSPARENCY AND CORRUPTION – A ROLE IN MEGA TRADE DEALS, July 2016, www.transparency.org/whatwedo/publication/working_paper_2_2016_transparency_and_corruption_a_role_in_mega_trade_deals
46 http://www.transparencyinternational.eu/2015/10/press-release-eu-trade-deals-to-include-ambitious-anti-corruption-proposals/
47 A US proposal in TTIP, see http://trade.djaghe.com/?p=2806

d. foster participation by different stakeholders throughout the regulatory process and set up a common website for easy access to all regulations;
e. adopt good-practice policies for lobbying transparency;[48]
f. avoid 'forum shopping' and 'policy capture' and ensure that all parties trading or investing in one of the partner states are subject to the same legal system and are treated equally (the principle of non-discrimination).

48 Transparency International, Lobbying in Europe: Hidden Influence, Privileged Access (Berlin: Transparency International, 2015), available at www.transparency.org/whatwedo/publication/lobbying_in_europe .

Part IV: UK Single Source Procurement and Poor Procurement Practice

Our research has highlighted a positive example of the Cabinet Office proactively investigating poor procurement practice: in 2011, the UK government launched a 'Mystery Shopper Scheme' to address poor public procurement practice and receive complaints against procurement authorities, as well as from subcontractors against prime contractors.

In the first 3 years of the scheme, the Cabinet Office received 580 cases, reporting that 79% of cases reached a positive outcome; for example live changes made to procurement tenders, recommendations to procurers to change behaviour, and shared examples of good practice.

In 2014, this was expanded to include 'spot checks': each month 20 sets of online tenders are selected at random to ensure they comply with best practice. In one of these checks the UK MOD was reported for illegible contract documentation. All case results are published online at www.gov.uk. In an annual report the UK Cabinet Office compares the data to previous years to identify positive and negative trends and issue guidance to procurers. For example, one trend analysis highlighted an increase in the number of complaints relating to specifications that did not allow for equivalents, an increase in bureaucracy, as well as complaints from suppliers that they did not have sufficient time to respond to lower value tenders.

This initiative should be continued, but with further attention given to increasing transparency and oversight of single source procurement.

Single source procurement: the issue

Greater transparency and oversight in procurement, including the advertisement and publication of awarded contracts, discourages opportunities for corruption and malpractice. Despite recent reforms, there is still limited transparency about the scale and nature of single source defence procurement and how this stymies competition both within the UK and internationally.

UK government departments are not currently required to justify the reasons for selecting non-competitive tender procedures (single source or negotiated procedure) to an independent external oversight body with the power to scrutinise and reject the elected procedure, and access sensitive information. This is somewhat out of step with international best practice,[49] and the Cabinet Office should consider exploring the merits of giving this power to the SSRO. We also recommend that a summary of single source procurements and tender justifications should be available to the public.

Key statistics:

- The number of new single source Ministry of Defence (MOD) contracts decreased from around 1,300 in 2013/14 to around 1,050 in 2014/15.
- The proportion of new defence contracts which were single source or non-competitive also decreased slightly – from 56% in 2013/14 to 53% in 2014/15.

However the total value of new non-competitive contracts entered into increased by almost 60% from £3.4bn to £5.4bn, as a result of a number of large value contracts, with a total spend of £8.3bn on all single source defence contracts in 2014/15.

[49] For example Canada, see http://government.defenceindex.org/generate-report.php?country_id=5570

The Current Approach to Single Source Procurement

The MOD's starting position for defence procurement is that a competition should be held for all requirements, and contracts only awarded to a single source supplier where this is not possible. The MOD has an Investment Approvals process for all significant procurements, which is set out in Joint Service Publication 655, to ensure that there is a strong justification for when single source procurement is being recommended. But the UK's reliance on long-term, high-tech, high-capital investment contracts nonetheless makes it one of the highest single source defence procurers in Europe.

The Defence Reform Act (the Act), Single Source Contract Regulations (the Regulations) and the SSRO as independent regulator were therefore introduced in 2014, following Lord Currie's review[50] in 2011. The aim was to bring greater transparency to single source procurement contracts, and the regulatory framework seeks to deliver value for money for the tax payer and fair and reasonable prices to defence companies by creating a window onto the prices and costs of defence contractors and their associated delivery. The regime requires a number of standard reports to be submitted across single source contracts and by single source contractors, and provides for a form of open book accounting to enable appropriate oversight.

In the absence of market competition, one important function of the SSRO is to recommend to the Secretary of State for Defence the profit margins on single source defence contracts to try to ensure value for money for the taxpayer and a fair and reasonable return for defence companies. According to the SSRO's former chairman, anecdotal evidence suggests that in the past five decades companies have been earning anywhere between 12 and 22 per cent margins on UK defence single source contracts.[51] The current formula, which allows for a baseline profit margin of 8.95 per cent, with a number of adjustments to take the profit margin up or down and averaging 11.7 per cent in 2015-16, is calculated based on a comparison with companies in Western Europe and North America engaging in similar activities to defence companies.

But the SSRO's role is somewhat constrained. Although the SSRO receives reports on single source defence contracts, this only applies above a certain threshold (£5 million for qualifying defence contracts and £25 million for qualifying sub-contracts), contracts can be exempted by the Secretary of State. Existing contracts that are extended also fall outside the reporting regime. Therefore, not all single source procurement contracts are subject to the price control and transparent open book reporting which the new regime has introduced, serving to limit the SSRO's ability to maintain a complete overview of the total scale of single source defence procurement and apply controls to it.

The SSRO powers are also limited when it comes to oversight over individual procurement decisions. Although the MOD's investment approvals process requires a "strong justification" for the use of single sourcing, this justification is not publically reported and nor does the SSRO have the power to scrutinise or reject the choice of procurement procedure; summon witnesses from government or the private sector and require them to provide information; investigate or follow up on malpractice (malpractice cases are referred back to the ministry; and, in the cases we have been made aware of, appear to lead to no subsequent action by the ministry). Nor does the SSRO have powers to require access to other information held by contractors and enforcement of non-compliance with the regime's requirements

[50] Lord Currie Review of Single Source Pricing Regulations (October 2011)

[51] https://next.ft.com/content/63ee7aae-5471-11e5-b029-b9d50a74fd14

sits with the Ministry of Defence. Such powers would lead to greater transparency and accountability amongst suppliers and procurement authorities tendering very high value contracts –giving greater assurance of value for money.

There is though already some potential momentum for reform. The SSRO will be engaging with stakeholders in September 2016 regarding the detailed transparency provisions of the Act and the Regulations. The SSRO has identified instances where information would be useful for analysis but is not prescribed in the Act for inclusion in reports about contracts. A more flexible approach for prescribing information to be included in reports would be beneficial to the SSRO as the independent regulator in fulfilling its value for money obligations. In early 2017, the SSRO will consult on all its proposed recommended changes to the Act and the Regulations before submitting final proposals to the Secretary of State in June 2017.

Recommendations

A summary of single source procurements and tender justifications should be available to the public.

It would be preferable to allow the SSRO, as the regulator, to determine and specify what information needs to be included in the reports it receives. Where information is not reported by contractors, the SSRO should have the powers to require it. The Cabinet Office should consider giving the SSRO powers to seek reports from stakeholders, scrutinise or reject the choice of procurement procedure, approve business cases for single source procurement as in Canada, investigate on the basis of reports, summon witnesses from government or the private sector and require them to provide information, and investigate or follow up on malpractice.

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Consultation response - UK Regulators Network

1. INTRODUCTION

The SSRO invites submissions from interested persons regarding its proposed recommendations to the Secretary of State for review of:

- Part 2 of the Defence Reform Act 2014 (the Act); and
- the Single Source Contract Regulations 2014.

The SSRO has proposed recommendations in three key areas: ensuring single source spending is fully covered by the legislation; enhancing transparency; and providing effective enforcement of the regulations. The SSRO is also calling for views and further evidence in areas where other organisations have suggested changes and where there are issues that may justify making further recommendations.

Details are set out in full in the separate document entitled “Consultation on recommendations”.

The time period for this consultation is eight weeks. Responses should be provided in writing using this form by no later than **5.00pm on 24 March 2017**. We will consider submissions received by the deadline, prior to making and publishing final recommendations to the Secretary of State by June 2017.

Where submissions are made, the SSRO asks that respondents focus on the benefits and impacts of the issues, and provide such evidence and examples as may support their submissions. This will help us to understand the basis for your submission, make a fuller assessment of the effect of the SSRO’s proposals and inform our finalisation of the recommendations.

2. CONSENT TO PUBLISH RESPONSE

In the interests of transparency, we intend to publish responses to this consultation on the SSRO website upon completion of the consultation, but we will take into account your views on publication.

Please note that the SSRO is subject to the Freedom of Information Act 2000 and other information access legislation, which may require us to disclose your consultation response. If you have not consented to publication, we may notify you of relevant requests and seek your views prior to disclosure.

Any information that is deemed official-sensitive and higher should not be submitted via the link.

Do you consent to publication of your response? ***Yes***

3. YOUR DETAILS

Name: ***Barbara Perata-Smith***
Organisation: ***UK Regulators Network***
Position: ***UKRN Manager***
Respondent type:

Please tick one or more boxes from the list of options that best describes you as a respondent. This allows views to be grouped as well as understood individually.

	Please tick all applicable boxes
☐	Central Government
☐	Trade body
☐	Defence contractor with QDC/QSC
☐	Defence contractor with no QDC/QSC
☐	SME
☐	Member of the public
☐	Organisation representing the taxpayer
☐	Academic, think tank or similar
☑	Other, please specify: ***Network of UK regulators***

4. OVERVIEW

The SSRO's recommendations are targeted at enhancing the existing provisions of the regulatory framework so that it is better placed to achieve the underlying parliamentary objectives of better value for money for the tax payer and a fair and reasonable return for industry.

The SSRO has focused its recommendations for change in three key areas:

- ensuring that single source spending is appropriately covered by the regime;
- enhancing transparency; and
- providing effective enforcement of the regime.

The consultation questions in each of these areas are set out below. In each case, the referenced paragraph and section numbers are from the document "Consultation on Recommendations".
The SSRO has indicated in the Consultation on Recommendations that it intends to keep under review the impacts of procurement decisions on the regulatory framework (paragraphs 5.11 and 5.12). This is on the basis that:

- Competition should be the first choice when awarding contracts.

- The regulatory framework is intended to provide a credible alternative in cases where competition is not feasible for some permitted reason.
- Failure to compete may result in pressure on the applicability of the framework.

Single source procurement is high, with at least £8.8 billion spent on single source procurement in 2015/2016. At the same time decisions to single-source are not transparent, which makes it difficult to assess the extent to which it is possible to improve outcomes.
The SSRO invites views on whether there is benefit to modifying the regulatory framework to:

1. expose single source procurement decisions to greater transparency; and

2. promote competition, innovation and monitor the involvement of SMEs.

In each case please provide reasons and evidence and address the benefits and impacts.

1. Transparency is important in building confidence in regulated sectors and ensuring their legitimacy. It drives greater accountability within regulated companies, resulting in better decision making and better outcomes for the public. In relation to the SSRO, greater transparency of single source procurement decisions, including the price and service - for example delivery time - would enable them as the regulator to identify where additional value can be created and efficiencies gained in contracts to the benefit of UK tax payers.

2. In line with other economic regulators, the SSRO would benefit from promoting competition where is it appropriate and in the best interests of UK tax payers. In the case of the defence, this would allow the Ministry of Defence more choice over the suppliers, likely to result in suppliers competing to offer better services and/or prices. Effective markets generate more value for customers, who are empowered through choice over price and service.

5. RECOMMENDATIONS ON COVERAGE OF THE REGIME

The price control and transparency provisions of the regulatory framework are dependent on contracts becoming qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). As the legislation is currently framed, there are a number of restrictions to contracts being brought within the regime and the SSRO has developed recommendations targeted at removing these.
Would you please give us your views on ensuring appropriate coverage of non-competitive spending, including the SSRO's following proposals to remove restrictions to contracts being brought within the regime.
In each case please provide reasons and evidence and address the benefits and impacts.

3. Treating material contract amendments as a new contract and judging materiality by reference to the £5 million threshold (paragraph 6.12).

No response.

4. Disapplying the price formula to committed costs when a contract becomes a QDC by amendment (paragraph 6.13).

No response.

5. Clarifying the timing issue in relation to the QSC definition (paragraph 7.20).

No response.

6. Providing greater transparency on QSC assessments by removing the 20 contract restriction, specifying a deadline, notifying unreported outcomes and specifying reasons for negative assessments (paragraph 7.21 and following).

No response.

7. Reducing the QSC threshold to £10 million (paragraph 8.5).

No response.

8. Limiting the exclusions in respect of contracts under the framework of an international cooperative defence programme and contracts for intelligence activities (paragraph 9.7).

No response.

9. How value for money and fair and reasonable prices may be demonstrated if single-source contracts are not brought within the regime.

No response.

6. RECOMMENDATIONS ON TRANSPARENCY

A key feature of the regulatory framework is the greater transparency it requires on the part of defence contractors to both the MOD and the SSRO. The standardised reports provide the SSRO with a range of information needed to discharge its statutory functions. However, there are circumstances in which the information provided needs to be supplemented; the SSRO proposes means by which this can be achieved.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

10. Granting the SSRO access to information powers (paragraphs 10.12 to 10.15).

Proposals within 10:12-10:13 would bring the SSRO in line with other economic regulators. The challenge with monopolies, where there are single buyers and sellers, is that it is difficult for other parties, including regulators and consumers, to understand if the monopoly is delivering value. This is due to information asymmetries. Hence why all sectoral regulators in the UK have information gathering powers., Access to accurate and up to date information is essential for regulators to discharge their functions effectively and efficiently, supporting risked based regulatory decisions underpinned by evidence – in the best interests of consumers /tax payers. It also is essential in enabling regulators to act in a proportionate and targeted way. In the absence of high quality data and information regulators are restricted in how they identify and drive efficiencies. It is also important in ensuring greater transparency and accountability in regulated sectors. The SSRO currently differs from other regulators in this respect. For example, Ofcom holds statutory

information gathering powers under Part 2 of the Communications Act 2003, the Wireless Telegraphy Act 2006, and the Postal Services Act 2011. Ofcom is required by each of those Acts to prepare and publish a statement of general policy on the exercise of certain information gathering powers and its proposed use of information obtained from stakeholders under those powers. The CAA also has information gathering powers which are set out in the Civil Aviation Act 2012, Part 2 and Part 1 respectively, and ORR has a wide range of information powers it can use in the process of reviewing and monitoring markets.

11. Alternatives to ensure the SSRO can access the data it needs for proper oversight, delivery of its functions and credible single-source regulation.

No response.

7. RECOMMENDATIONS ON REFERRALS AND ENFORCEMENT

The Act relies partly on self-regulation and partly on a system of referrals by contracting parties, and compliance and penalty notices issued by the MOD to ensure that its provisions are complied with. The SSRO may give expert opinions and make determinations, but only if requested by the contracting parties. The nature of the single source defence market means that the SSRO may be better placed to have a role in enforcement and we propose that measures should be implemented to improve the available enforcement mechanisms in line with other regulators.
Please provide your views on the proposal set out below.
In each case please provide reasons and evidence and address the benefits and impacts.

12. Extending grounds for referral to all steps of the contract profit rate calculation and to whether a contract is a QDC or a QSC (paragraph 11.15).

No response.

13. Authorising the SSRO to issue compliance and penalty notices in respect of reporting and QSC assessments (paragraph 12.12).

Enforcement powers are an essential tool within the regulatory toolbox to ensure compliance with legislation, regulations and licence requirements. This includes in relation to the submission of information and data reporting, to ensure the data is accurate and up to date to inform evidenced based regulatory decisions. They are also a valuable lever in supporting softer regulatory tools that can be used to encourage and incentivise companies to deliver better outcomes.

14. Other measures aimed at ensuring the SSRO can properly discharge its functions and make single source procurement credible.

No response.

8. ADDITIONAL COMMENTS

If you have any additional comments, please provide them below. In each case please provide reasons and evidence and address the benefits and impacts.

15. The SSRO's recommendations.

No response.

16. Issues raised concerning exclusion of government-to-government contracts (section 14).

No response.

17. Issues raised concerning enforcement of price control (section 15).

No response.

18. The proposal for disapplying the price formula (section 17).

No response.

19. Stakeholder proposals supported by the SSRO (section 18).

No response.

20. Stakeholder proposals not presently supported by the SSRO (section 19).

No response.

21. Stakeholder proposals where additional explanation or evidences is required (section 20).

No response.

22. Other suggestions for amendments to the legislation.

No response.

23. Alternative approaches to improve the regulatory framework that do not require legislation.

No response.