SSRO

Single Source
Regulations Office

Assuring value, building confidence

Monitoring the impact and performance of the single source regulatory framework - July 2016

Contents

Introduction

1. Introduction

1.1 The regulatory framework for single source defence contracts was introduced by Part 2 of the Defence Reform Act 2014 (the Act) and the Single Source Contract Regulations 2014 (the Regulations). The scheme of regulation[1] (the 'regime') aims to strike a balance between value for money for the taxpayer and fair prices for contractors.

1.2 The SSRO's statutory functions include keeping Part 2 of the Act and the Regulations under review. The *SSRO's Corporate Plan for 2016 to 2019* sets out requirements for it to collect quantitative and qualitative evidence about the regime, and identify positive and negative elements in the way it is operating.

2. Approach

2.1 This report further develops the SSRO's approach to monitoring the impact and performance of the regime. The approach is based around ten factors that the SSRO has identified as relevant.

2.2 The SSRO considers that, to assist it in carrying out its statutory functions, it needs to have a set of measures to help monitor the success or otherwise of the regime. This will be particularly helpful for keeping the Act and the Regulations under review, but should also inform other functions, such as giving statutory guidance and providing reporting templates.

2.3 The SSRO intends that its monitoring of the adopted measures should be transparent. Publishing the monitoring will provide a means of further engaging with stakeholders and generate an important evidence base to assist the SSRO in carrying out its statutory functions.

2.4 In order to select a set of indicators to monitor the impact and performance of the regime, the SSRO has taken into account the objectives of the regulatory framework. The Act and Regulations overall aim to ensure good value for money for the taxpayer and fair and reasonable prices for defence contractors by:

- controlling the pricing of contracts;
- providing transparent access to information held by defence contractors which can be analysed and reflected in improved contracting; and
- giving the SSRO oversight of the regime.

2.5 The approach looks at the whole regime, and does not aim to assess the SSRO's own performance. However, the SSRO will take into account the information it gains from carrying out the monitoring in considering its own approach to, and performance in, regulating the regime. An important part of any system is to gain regular feedback to allow improvements to be made where required.

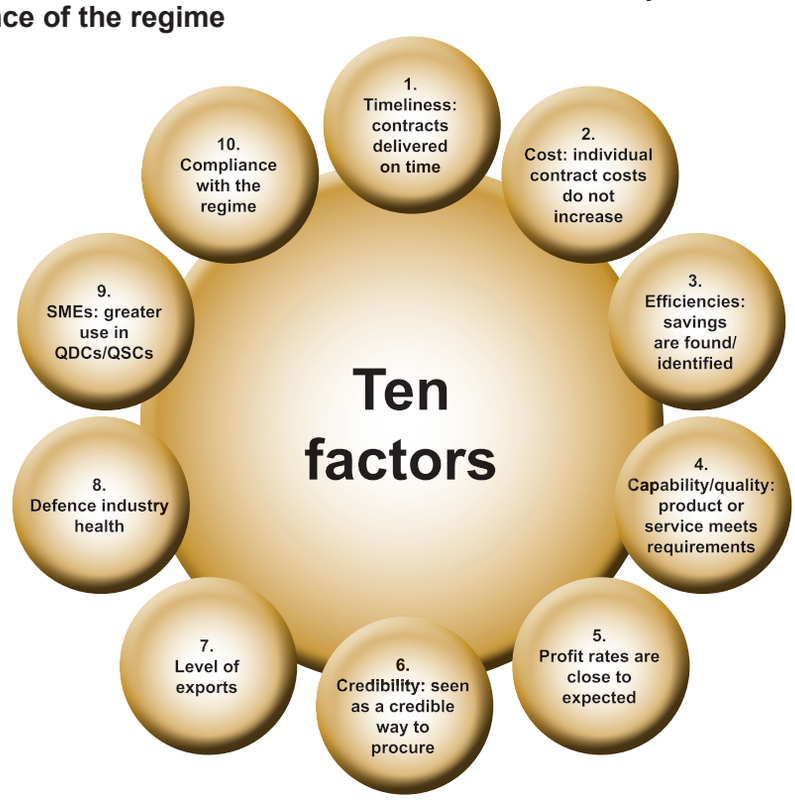
1 For further information see the SSRO's Review of the Single Source Regulatory Framework: Call for input: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/524530/SSRO_Review_of_the_Single_Source_Regulatory_Framework_-_Call_for_input_Final.pdf

Monitoring the impact and performance of the regime

3. The ten factors and their measurement

3.1 The SSRO has identified ten factors that it will consider when monitoring the impact and performance of the regime (Figure 1).

Figure 1: Ten factors the SSRO will use to monitor the impact and performance of the regime



3.2 The following tables set out why the SSRO considers each factor important in monitoring the impact and performance of the regime. The tables also set out what the measure is that the SSRO intends to use, including lead indicators, and the data sources.

3.3 Defence suppliers are required to submit data about qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs) to the SSRO, along with supplier reports including those on qualifying business units (QBUs). Five of the ten factors rely on this data that is returned to the SSRO by defence suppliers, while the other five draw on data collected by the SSRO or that is publicly available.

Timeliness

Why it matters	What is measured and how
Delivering contracts on time matters because it helps ensure that requirements are available to front line commands when needed and costs do not increase significantly. Reports from contractors will identify whether planned contract milestones are being met or not. Delays in delivery may also lead to an increased gap between estimated and actual costs. Learning from contractor reports could lead to future contracts for the same or similar output being able to be delivered in less time and/or at reduced cost. The single source procurement framework must not act as a barrier to contracts being delivered in a timely manner.	The proportion of QDCs[2] experiencing slippage, measured through the difference between contracted and actual / forecast milestone completion dates. **Data sources:** Contract completion reports, but with lead indicators from quarterly reports for larger QDCs and interim reports for smaller QDCs.

Cost

Why it matters	What is measured and how
Cost control is a key component of the single source procurement framework and it is important to understand whether this control is being successfully maintained.	The proportion of QDCs experiencing cost growth / reduction, and total cost change as a percentage of overall cost. Measured through the variance between the cost estimate in the latest version of the contract, and the current total forecast cost to completion in QDC reports. Excludes profit. **Data sources:** Contract completion reports. Lead indicators from quarterly reports for larger QDCs and interim reports for smaller QDCs.

2 Where QDCs are referred to in this document, this also applies to QSCs.

Efficiencies

Why it matters	What is measured and how
The SSRO is charged with ensuring value for money for the taxpayer is obtained in government expenditure on QDCs and that contractors are paid a fair and reasonable price. Any efficiencies that can be identified through the work of the SSRO will be an important measure of whether these objectives are being achieved. The single source procurement framework allows use of different pricing methods and incentives to encourage efficiency. The impact assessment for the Defence Reform Bill[3] calculated that the long run annual average savings to be achieved from the Act, Regulations and the SSRO would be approximately £200 million.	The confirmed savings identified by the SSRO, the total under investigation by the SSRO and the potential savings identified by the SSRO. The first two are measured against those QDCs received in each year (and so figures for previous years can change if further issues are identified). Savings confirmed can be from different areas of the SSRO's work, including compliance work and referrals. Potential savings can be from different areas of the SSRO's work, including value for money studies[4]. **Data sources:** SSRO analysis of savings from compliance, referrals and other work. The SSRO reviews QDC submissions for compliance with the Act and Regulations. Where non-compliance is identified this results in further challenge by the SSRO. If these are confirmed as being erroneous, either by the contractor or the MOD, this results in confirmed savings.

Capability / quality

Why it matters	What is measured and how
Important indicators are whether capability requirements are met and quality achieved. Requirements flow down from the Strategic Defence and Security Review and are set by the MOD. The regime needs to support delivery of these requirements and they should be as capable of being delivered through single source suppliers as they are following a competition.	The SSRO receives information at the start of a contract on the deliverables in a contract, and metrics associated with these. The metrics associated with the deliverables are not updated in the quarterly reports, and so changes in these are not captured until interim or contract completion reports. The measure would be the proportion of contracts where metrics associated with deliverables are met. **Data sources:** Contract completion reports. Lead indicators from interim reports.

3 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/210533/Defence_Reform_Bill-_Impact_Assessment-_MOD0002.pdf

4 For more information on the SSRO's programme of value for money studies please see: https://www.gov.uk/government/consultations/programme-of-value-for-money-studies

Profit rates

Why it matters	What is measured and how
Profit control is a key component of the single source procurement framework and it is important to understand whether this control is being successfully maintained.	The proportion of QDCs from a financial year that achieve a final profit on completion that is five percentage points[5] above or below the expected rate, and the numbers higher or lower than expected. (Excluding any incentive adjustment). **Data sources:** Contract completion reports, with lead indicator data from quarterly reports for larger QDCs and interim reports from smaller QDCs.

Credibility

Why it matters	What is measured and how
A regime that strikes the right balance between value for money for the taxpayer and a fair and reasonable return for industry should be received positively and encourage engagement. It should lead to single source procurement being seen as a credible alternative to competitive procurement in the right circumstances. The SSRO must ensure that it remains transparent, professional and independent in all of its work in order to develop as a trusted adjudicator and the accepted expert on single source procurement.	Specific measures would be the number of, and where relevant, proportions of those positive, neutral and negative for: • number of referrals; • engagement from stakeholders, including queries, letters; • number of Parliamentary references to the SSRO or the regime; and • number of significant other references to the SSRO or the regime including in the media. The assessment will also be qualitative rather than a simple quantitative measure. The proportion of the total value of new MOD contracts that is non-competitive would also be a measure. **Data sources:** The SSRO's monitoring during each financial year and MOD published statistics.

5 The level at which a final pricing adjustment would apply as explained in Regulation 17.

Exports

Why it matters	What is measured and how
The Minister for Defence Equipment, Support and Technology has explained that "making industry more efficient should … also lead to a more competitive role for the UK industry in the export market".[6] The regime should help to deliver this efficiency through encouraging different behaviours as it embeds over time. Export potential is also important as it can reduce the cost to the taxpayer through additional benefit to the MOD.	The value of UK defence exports. UKTI / DSO publish annual statistics on the value of new orders from a survey of companies. The statistics do not cover whether the exports are linked to a single source procurement by the MOD. **Data sources:** UKTI / DSO published statistics.

Defence industry health

Why it matters	What is measured and how
The SSRO has a duty to ensure that contractors are paid a fair and reasonable price, therefore contributing to the financial health of the defence sector. A strong defence sector sustains employment, retention of specialist skills and economic benefits through a widespread supply chain. It also ensures that there is ample opportunity for competition because a number of suppliers, including small and medium sized enterprises, are available to compete for government contracts.	The SSRO intends to carry out analysis on the health of the defence industry in autumn 2016, which will be used to set the right measure or group of measures to consider. This would look at financial health indicators for the MOD's top UK suppliers, and track changes over time. Indicators could include, for example, credit ratings, dividends and shareholder returns.

6 Foreword to Review of Single Source Pricing Regulations, Lord Currie, October 2011

Small and medium sized enterprises (SMEs)

Why it matters	What is measured and how
The regulatory framework helps to deliver the government's policy objectives around promoting business for SMEs by monitoring the extent to which SMEs are involved in qualifying contracts and requiring information from suppliers as to their actual and planned engagement of SMEs.	The value of spending with SMEs by suppliers (across all defence contracts, not just QDCs), from annual SME reports. Lead indicator: number and value of SMEs in top 20 subcontracts (having a value of not less than £1 million) for each QDC, and number and value of QDCs let to SMEs. **Data sources:** Annual supplier SME reports and contract notification reports, quarterly contract reports for larger QDCs, interim contract reports for smaller QDCs and contract completion reports.

Compliance

Why it matters	What is measured and how
An important test of the single source regulatory regime is whether the MOD and industry are complying with the Act and the Regulations. Our compliance indicators, published in the SSRO's compliance reports, will allow us to measure increases in compliance over time. Contractors should also become more familiar with the regime requirements and processes for reporting should become embedded within their organisations.	The SSRO has eight compliance indicators to measure compliance. Three apply to contractors, three to the MOD and two apply to both parties. The assessment is whether the party has complied or not. The MOD compliance is measured through indicators that relate to notifying the SSRO of any QDCs, to notify the SSRO of verification within 30 days, and having regard to the SSRO's statutory guidance on Allowable Costs and contract rate requirements. Contractor compliance is measured through indicators relating to submitting accurate reports, their compliance with the statutory guidance on Allowable Costs and contract profit rate requirements. Overall percentages for the MOD and contractors will be considered here. Full details of compliance are published separately by the SSRO in its published reports on compliance. **Data sources:** SSRO's compliance reports.

3.4 The SSRO will use 2015/16 as a baseline year in order to monitor emerging trends. Where data is made available to the SSRO on single source contracting in earlier time periods then this may also be used to set a baseline. The SSRO will also look to use external comparators in assessing the regime.

3.5 Where appropriate, the SSRO may also choose to make qualitative judgements about each factor, and provide explanations for its view. The SSRO will take into account any other information that it deems relevant in making judgements on each factor, and also in making any overall judgement about the regime.

Next steps

4. Annual publication

4.1 The SSRO will publish, each year, its monitoring of the impact and performance of the regime. This will be a backward-looking assessment, and will include data on the measures in the most recent year. For measures based on QDC reports, it will also include updated figures for previous years, as contracts from those years continue or reach completion.

4.2 The first publication of the monitoring will be in June 2017 along with the SSRO's formal review of the Act and the Regulations, covering data for 2015/16 and 2016/17. The SSRO considered publication of 2015/16 data. However, only six QDCs / QSCs had reports beyond the original set provided at the start of the contract[7]. Therefore the numbers were too small to make any monitoring meaningful for 2015/16 at this point in time.

4.3 The SSRO will look to continue to improve the data and measures that it uses to monitor the impact and performance of the regime. It will consider in its work on reviewing the Act and Regulations, and in considering its reporting templates, whether the right data is being collected. Any future changes to the measures set out here will be explained in the annual monitoring reports.

7 As at end May 2016.