VALUE FOR MONEY AND PUBLIC PRIVATE PARTNERING – THE UK MOD EXPERIENCE

NEIL V DAVIES
Managing Director
DAVIES ECONOMIC CONSULTANCY LTD and
Director and Chief Economist,
DEFENCE ECONOMICS LTD

Former Chief Economist
UK MINISTRY OF DEFENCE 1996-2012

DAVIES ECONOMIC CONSULTANCY LTD

defence economics

SLIDE 1 – OUTLINE OF PRESENTATION

-The drive to improve value for money through private sector involvement in defence and reform of procurement

-Lessons learnt

-Criteria for deciding whether and which form of private sector involvement to adopt

SLIDE 2 - FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

1) Privatisation -

Selling state owned assets and undertakings

Examples –

Royal Ordnance Factories; British Aerospace (now BAE Systems) and Rolls Royce in 1980s

Sales of (part of) Defence Evaluation and Research Agency (QINETIQ) in 2003

SLIDE 3 - FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

2) Contractorisation/Outsourcing

– Procuring services from private sector instead of through state managed activity

Examples – property management, cleaning, catering

SLIDE 4 - FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

3) Government Owned/Contractor Operated Undertaking

– Transfer management of undertaking and employment of staff to private sector while retaining ownership of assets

Example – Naval dockyards in early 1980s.

SLIDE 5 - FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

4) The Private Finance Initiative

-Involves Private Sector investing in, managing, operating and maintaining assets and service delivery; while Public Sector pays through long term contract covering standards and charges

SLIDE 6 – FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

5) Prime Contracting

– arrangement for procurement with a single contractor who then manages all the subordinate supply contracts

Examples – all major equipment acquisitions since late 1980 and now applied to MOD estate maintenance and capital works

SLIDE 7 – FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

6) Contractor Logistic Support (CLS)/Integrated Operational Support (IOS)

– arrangement with single contractor for logistics support for set period or life of equipment.

– Examples – Sea King helicopter Integrated Operational Support

SLIDE 8 – FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

7) Wider Markets Initiative/Marketing Partnerships

– Generation of revenue, from commercial exploitation of irreducible spare capacity in public sector assets;

– Examples – mostly small scale including use of MOD facilities for films

SLIDE 9- FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

- 8) Executive Agencies And Accruals Accounting
- - Executive Agencies run on quasi-commercial lines by Chief Executives responsible for delivering specified targets.
- - accruals-based accounting introduced in 2001 to provide public sector managers with incentives to manage assets and stocks efficiently

SLIDE 10 – FORMS OF PRIVATISATION AND OTHER INVOLVEMENT OF PRIVATE SECTOR

9) Strategic Private Sector Partnerships

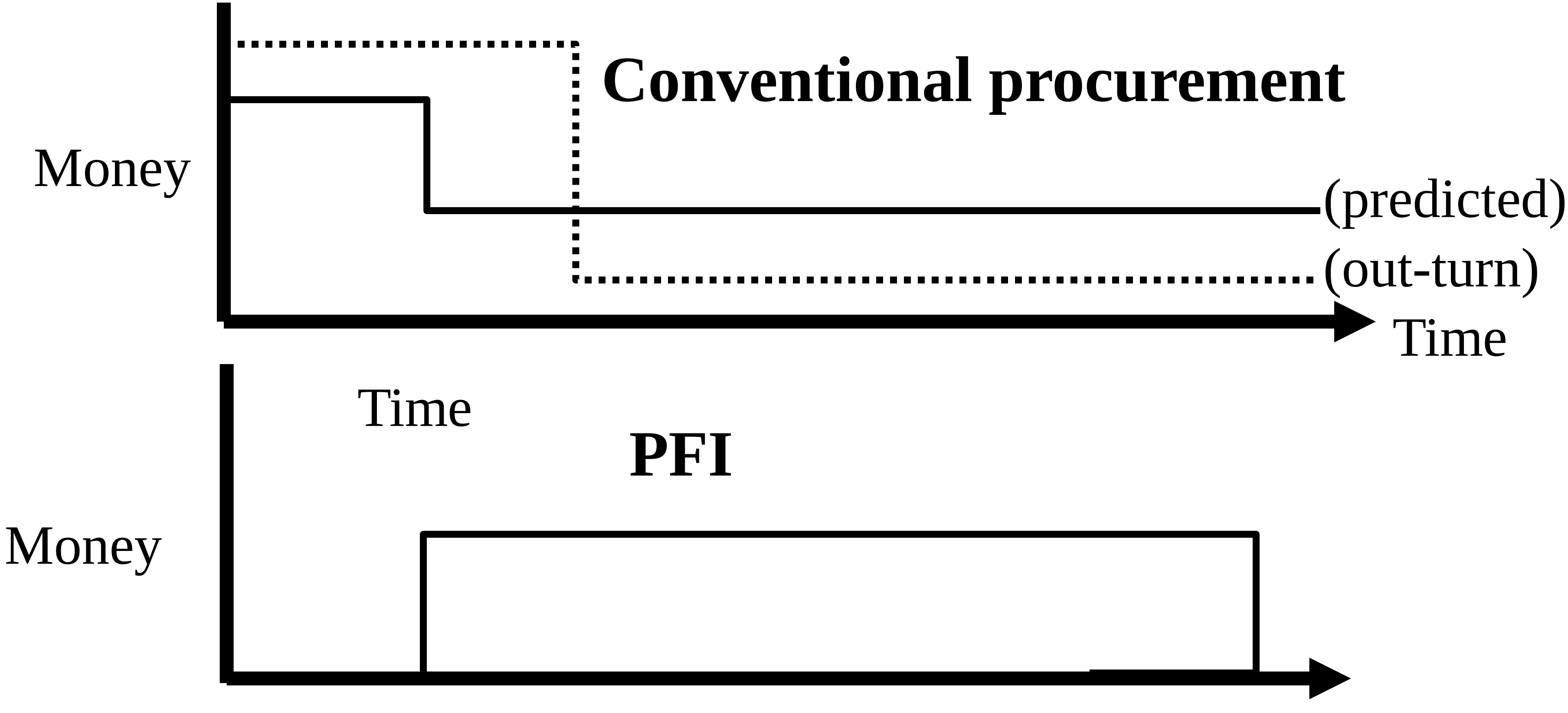
– Enter into partnership with private sector organisation for management of Core support function

Examples – Partnership with Serco and Accenture for senior management of Defence Business Services in March 2012

SLIDE 11 – BENEFITS OF PFI

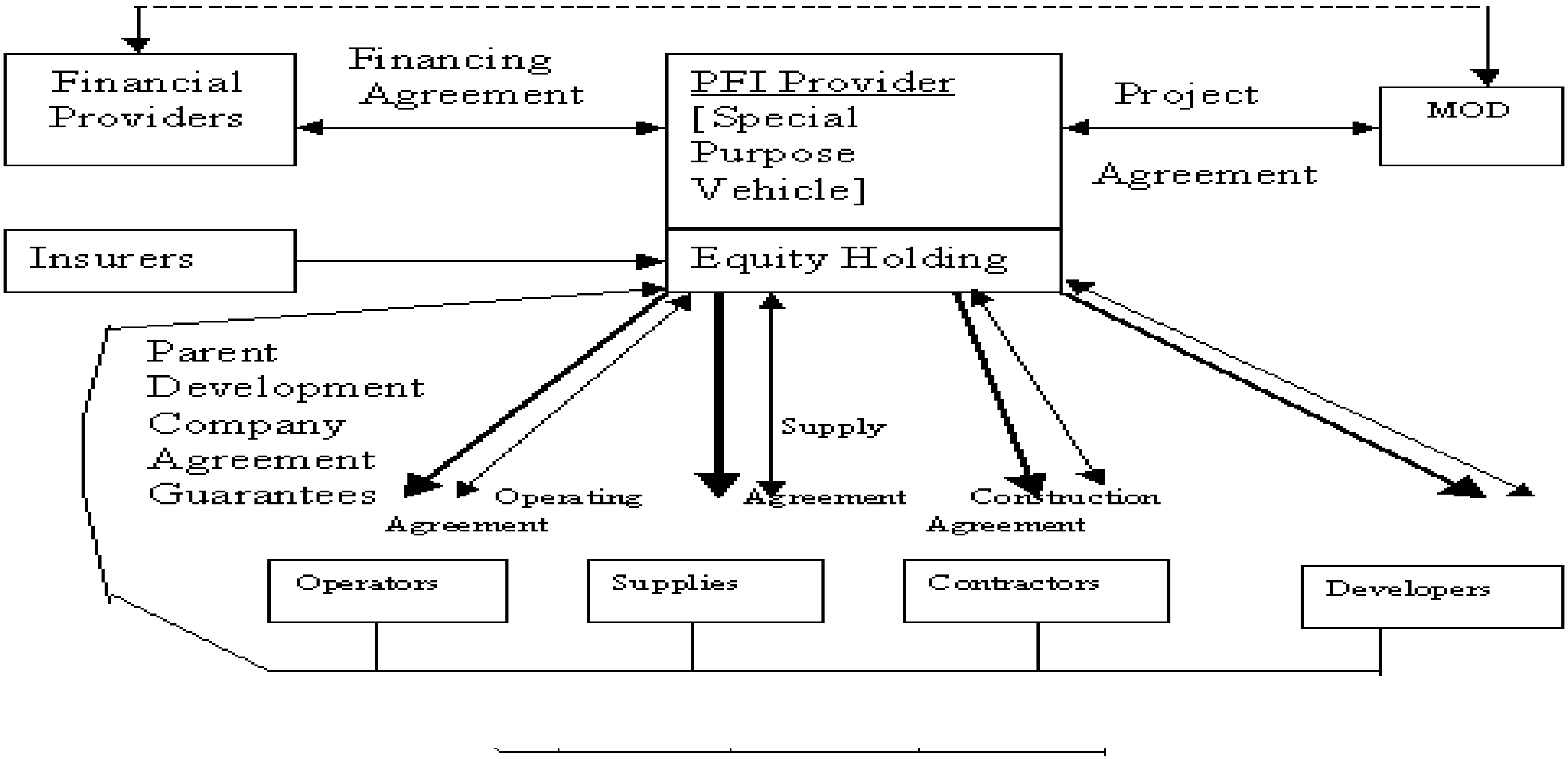
- Explicit requirement definition – delivers what's in contract
- More innovative approach to service delivery
- Incentivises to deliver to time and cost
- Greater transfer of risks to private sector
- Affordability - avoids up front Public investment

SLIDE 12- COMPARISON OF CONVENTIONAL AND PFI PROFILES



DAVIES ECONOMIC CONSULTANCY LTD

SLIDE 13 - TYPICAL PFI CONTRACT STRUCTURE



DAVIES ECONOMIC CONSULTANCY LTD

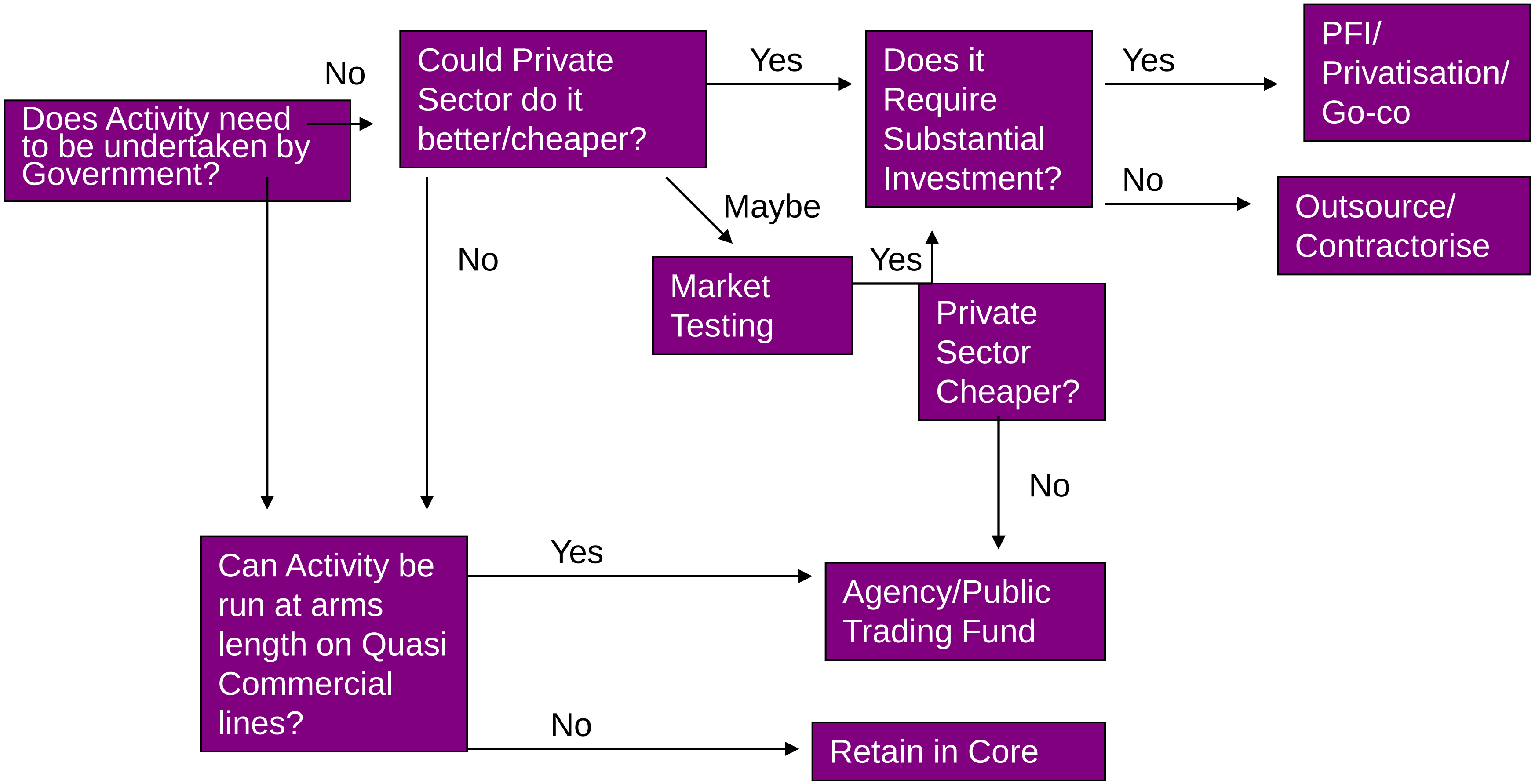
SLIDE 14 – OVERALL LESSONS LEARNT

A) Financial Saving

- Early benefits from market testing MOU in-house activities delivered savings of 20-30% over period 1983-89, even when task kept in-house
- Subsequent savings smaller in region of 10-15%

B) Delivery

- PFI has ensured delivery of required outputs to teams and bases but process substantially longer (at least 12 months longer)
- Even in operational areas – Balkans, Iraq contracted out services have met requirements in full


Does Activity need to be undertaken by Government?
No
Could Private Sector do it better/cheaper?
Yes
Does it Require Substantial Investment?
Yes
PFI/ Privatisation/ Go-co
No
Outsource/ Contractorise
Maybe
Market Testing
Yes
Private Sector Cheaper?
No
No
Can Activity be run at arms length on Quasi Commercial lines?
Yes
Agency/Public Trading Fund
No
Retain in Core

SLIDE 16- REFORM OF DEFENCE PROCUREMENT

- Smart Acquisition (1998) just 2 Approval Points & Empowered Integrated Project Team
- Defence Procurement Agency and Defence Logistics Organisation merged in 2007
- CAAS restructured in 2009 to provide central cost assurance
- Gray Report found endemic weaknesses of perverse incentives and optimism bias.
- In 2010 Gray appointed Chief of Defence Material

SLIDE 17- Reform of Defence Headquarters

- Successive Attempts to Restructure, Retrench and simplify Defence Headquarters
- “Streamlining” initiative in 2009 sought to simplify processes and structure
- Latest attempt involves 25% cut in senior military and civilian posts at 1* level

SLIDE 18- CONCLUSIONS

- Greater Involvement of Private Sector as MOD could no longer carry out full range of functions efficiently with reduced resources.
- Private Sector has delivered greater efficiency and economy but subject to appropriate contract design.
- Now being taken into Core functions.
- Successive Reforms of Defence Acquisition and Headquarters largely unsuccessful due to reluctance to accept required simplification of processes.