

<b>Title:</b> Single Source Contract (Amendment) Regulations 2018 <b>IA No:</b> MOD00001  <b>RPC Reference No:</b> N/A <b>Lead department or agency:</b> Ministry of Defence <b>Other departments or agencies:</b> N/A	<b>Impact Assessment (IA)</b>			
	<b>Date:</b> 06/06/2018			
	<b>Stage:</b> Development/Options			
	<b>Source of intervention:</b> Domestic			
	<b>Type of measure:</b> Secondary legislation			
	<b>Contact for enquiries:</b> Single Source Advisory Team (SSAT) - 0207 2188255			
<b>Summary: Intervention and Options</b>				<b>RPC Opinion:</b> Not Applicable

Cost of Preferred (or more likely) Option				
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANDCB in 2014 prices)	One-In, Three-Out	Business Impact Target Status
N/A	N/A	N/A	Not in scope	Qualifying provision

**What is the problem under consideration? Why is government intervention necessary?**

The Defence Reform Act (2014) is intended to improve the procurement and support of defence equipment by the MOD. The Secretary of State for Defence is required to review single source procurement legislation within three years of the new framework coming into force. This was completed in December 2017 and it identified several areas where the existing arrangements could be improved. These proposed amendments to the regulations aim to clarify which single source defence contracts cannot be subject to the legislation (i.e. those contracts which are specifically excluded from the regulations). Government intervention is necessary clarify existng provisions and to prevent contracts being unnecessarily excluded from the regime

**What are the policy objectives and the intended effects?**

The existing regulations currently specify five categories of single source defence contracts which cannot be made qualifying defence contracts. These are commonly referred to as 'exclusions'. Having engaged extensively with stakeholders in industry and the SSRO, experience with implementing the regulations since December 2014 has shown that, while three of the five are working well, two have caused issues and one additional exclusion has been identified as desirable. The Government is therefore proposing to amend the regulations.

**What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)**

The Single Source Contract Regulations (SSCRs) are already in place and are operating effectively – these amendments are intended to clarify aspects of the original legislation and to make the framework more effective. MOD considered a 'status quo' and a non-legislative option (see below) but assessed that neither would achieve the desired policy intent.

The Department is considering other changes to legislation following its review of the single source regulations but these will not be ready before autumn 2018 at the earliest. An additional Impact Assessment will be developed in due course as these proposals mature.

<b>Will the policy be reviewed?</b> It will be reviewed. <b>If applicable, set review date:</b> 12/2020				
Does implementation go beyond minimum EU requirements?			N/A	
Are any of these organisations in scope?			<b>Micro</b> No	<b>Small</b> No
			<b>Medium</b> Yes	<b>Large</b> Yes
What is the CO <sub>2</sub> equivalent change in greenhouse gas emissions? (Million tonnes CO <sub>2</sub> equivalent)			<b>Traded:</b> Nil	
			<b>Non-traded:</b> N/A	

*I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.*

Signed by the responsible Minister: \_\_\_\_\_ Date: \_\_\_\_\_ Guto Bebb  
15 June 2018

# Summary: Analysis & Evidence

# Policy Option 1

## Description:

### FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate:

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional	Optional	Optional
High	Optional	Optional	Optional
Best Estimate			

#### Description and scale of key monetised costs by 'main affected groups'

We assess that the additional monetised costs on defence suppliers and the Single Source Regulations Office (SSRO) resulting from the proposed amendments are negligible.

#### Other key non-monetised costs by 'main affected groups'

The non-monetised costs by defence suppliers and the SSRO resulting from the proposed amendments are assessed as negligible.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional	Optional	Optional
High	Optional	Optional	Optional
Best Estimate			

#### Description and scale of key monetised benefits by 'main affected groups'

We estimate that a small number of additional contracts will be covered by the framework as a result of the proposed amendments, and only with with the consent of the parties affected. This will increase financial and non-financial benefits to MOD, primarily through improving. This will represent a small proportion of the number and value of contracts already covered by the framework, and the additional coverage both in terms of number of contracts and total value will be modest.

#### Other key non-monetised benefits by 'main affected groups'

Both MOD and defence suppliers will benefit from greater clarity in defining which single source contracts are excluded from the framework. This will result in less confusion and a reduction in the administrative burden on MOD and industry suppliers.

Key assumptions/sensitivities/risks  
(See below)

Discount rate

### BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs:	Benefits:	Net:	

## **EVIDENCE BASE – Problem under consideration**

### **Background - MOD use of single source procurement**

1. The MOD's approach to single source procurement was fundamentally altered by Part 2 of the Defence Reform Act (2014) and the Single Source Contract Regulations (2014) which established a new framework for dealing with single source defence contracts. This replaced the previous, voluntary arrangements known as the Government Profit Formula and its Associated Arrangements (commonly referred to as the "Yellow Book").
2. This new Framework (known as the "Single Source Contract Regulations, or SSCRs") was based on the principle that industry gets a fair and reasonable price in exchange for providing the MOD with the protections we need to assure value for money.
3. In designing the new framework, the key principles were to:
  - a) Address issues that arise from single source procurement – for example, supporting the MOD's ability to replicate the missing competitive pressure;
  - b) Focus on areas where standardisation is of value – the framework proposed benefits from wide application and stability over time;
  - c) Be proportionate – higher value contracts carry a greater risk to VFM, so there should be greater protections. We did not want to discourage the greater involvement of Small and Medium Sized Enterprises (SMEs) in defence by a framework that is too burdensome.
  - d) Provide VFM – we took a balanced approach between asking for information we would ideally like, and asking for information that is readily available using current industry systems and processes. We have ensured that the framework is practical by engaging with industry on these proposals.

### **The Single Source Contract Regulations – Key features**

4. The framework has four key features:
  - (a) Increased transparency through open book provision allowing MOD to request access to any information pertinent to the price and outturn performance of a qualifying defence contract;
  - (b) Improvements to the pricing principles including shifting the onus of proof from MOD to the supplier who is required to demonstrate that costs are appropriate, attributable, and reasonable;
  - (c) Suppliers are required to provide MOD with a comprehensive set of standardised reports on costs;
  - (d) Establishment of an effective compliance mechanism and the creation of an executive Non-Departmental Public Body (ENDPB) known as the Single Source Regulations Office to resolve disputes between MOD and suppliers which are referred to it for a decision.
5. The Better Regulations Executive (BRE) at the then Department for Business, Innovation and Skills, was consulted in 2013-2014 concerning the new legislation. It advised that because suppliers would be reimbursed for costs incurred complying with the new requirements, and because single source procurement was "an explicit rejection of the market", the changes would not be "regulations" from the point of view of the Regulatory Policy Committee. The new framework would therefore not be subject to the "One-In-One-Out" policy.

### **Approach to Consultation**

6. The Single Source Regulations Office (SSRO) is required by legislation to keep the regulations under constant review and to make recommendations to Secretary of State on such changes as it considers appropriate. In addition, the SSRO was required to carry out a full review of the regulations and submit recommendations to Secretary of State six months before the end of the review period (i.e. by June 2017). This is to inform the Secretary of State's review of the regulations which must be completed within three years of the framework coming into force (i.e. by December 2017).
7. As part of its consideration of the regulations, the SSRO undertook extensive engagement with stakeholders, including a public consultation, from May 2016 to March 2017. In June 2017, the SSRO submitted its recommendations on proposed changes to Secretary of State. These included supporting

the MOD intent to clarify the regulations regarding exclusions. Details of the SSRO consultations and its recommendations to Secretary of State can be found on the SSRO website (at [www.gov.uk/ssro](http://www.gov.uk/ssro) ).

8. In June-November 2017, MOD carried out further engagement with key stakeholders in industry and the SSRO to explore the SSRO recommendations and to consider other proposed changes before final advice was presented to Secretary of State in November 2017. This identified several proposed changes which could improve the operation of the framework. Secretary of State completed his review of the legislation in December 2017 but asked for further work to be done on implementation. This resulted in further engagement with stakeholders in January to March 2017. There has also been consultation between MOD and OGDs (notably with HMT, CO, and BEIS, including BRE) on the proposed changes.

9. The Government's position on the review will be set out in a Command Paper ("Review of the Single Source Contract Regulations – 2017"). This thorough engagement has allowed MOD to develop the proposed solution iteratively with industry and the SSRO; taking account of their concerns as far as is possible without diluting the intent behind the changes.

10. One of the main MOD priorities in carrying out its review was to ensure that as many qualifying single source defence contracts and sub-contracts as possible should be covered by the framework. The SSRO recommended that the definitions of exclusions used in the regulations be amended with regards to international co-operative defence programmes and contracts wholly for intelligence activities. This will allow for more precise definitions to be used to exclude the smallest number of contracts from the framework required to meet the MOD's policy intent. The MOD proposal also includes adding a new exclusion to the regulations to cover new contracts which replace an existing contract.

### Analysis of options

11. Three options were considered as part of developing the Business Case:
- a) Option 1 - "status quo"
  - b) Option 2 - "Improvements based on a non-legislation outcome"
  - c) Option 3 - "Amend SSCR Legislation"

#### Analysis of Option 1 – “status quo”

Option 1 – Status Quo	
<b>Description</b>	The existing Framework continues to operate as it has since December 2014.
<b>Advantages</b>	None identified.
<b>Disadvantages</b>	The framework as it currently operates is effective in meeting the main objectives set on it but the 'status quo' option would not allow MOD and suppliers to realise the very real additional benefits identified with this proposal in terms of extending the scope of the regime and clarifying how it is implemented.
<b>Monetary / Non-Monetary Costs &amp; Benefits</b>	No additional costs to MOD, suppliers, or the SSRO.

#### Analysis of Option 2 - "Improvements based on a non-legislation outcome"

Option 2 - "Improvements based on non-legislation outcome"	
<b>Description</b>	No improvements can be made without changing the legislation.
<b>Advantages</b>	N/A
<b>Disadvantages</b>	N/A
<b>Monetary / non-monetary costs and benefits</b>	None.

<b>Option 2 - "Improvements based on non-legislation outcome"</b>	
<b>Costs to MOD &amp; Industry arising from regulations</b>	N/A
<b>Benefits</b>	N/A
<b>Non-monetary considerations</b>	N/A

### Analysis of Option 3 - "Amend SSCR Legislation"

<b>Option 3 - "Amend SSCR Legislation"</b>	
<b>Description</b>	The MOD Business Case seeks to amend the definitions used for the exclusions relating to (a) intelligence activities and (b) international co-operative defence programmes. In addition, the MOD proposes to add another exclusion relating to new contracts which replace an existing contract. Details of the MOD's policy intent behind these proposed changes are given in the Explanatory Memorandum which accompanies the draft Statutory Instrument (SI).
<b>Advantages</b>	The main advantage to amending the definitions used for exclusions in the regulations is that it would clarify the scope of the framework to cover additional contracts which currently fall outside of the regulations and so increase the vfm benefits for MOD.
<b>Disadvantages</b>	The process of preparing for and successfully implementing changes to secondary legislation is time-consuming and costly for MOD, but when set against the degree and speed of change that could be negotiated through contracts, this is not a significant concern.
<b>Costs associated with regulatory body</b>	The changes would involve a measure of additional burden in terms of amending and, where necessary, extending guidance for suppliers but this would largely be a one-off cost of adjustment and would not be a significant additional burden.
<b>Costs to MOD &amp; Industry arising from regulations</b>	MOD accepts that suppliers may incur costs in adapting to the DRA and SSCRs and has agreed that, subject to a full audit of their expense claims, suppliers can recover these costs. However, the <u>additional costs</u> to industry arising from the proposed changes are assessed as negligible. Most of MOD's main suppliers are already engaged with the system because they already have qualifying defence contracts or sub-contracts with the Department subject to the SSCRs. For them, this proposal may involve a small number of contracts / sub-contracts being brought under the framework but the additional costs are likely to be marginal because the new processes will already be in place on a 'business-as-usual' basis.
<b>Benefits</b>	Industry and MOD will benefit from having clarity over the definitions used for exclusions, thus reducing the administrative burden.
<b>Non-monetary considerations</b>	Clarifying existing legislation on exclusions would reduce scope for confusion, negotiation, and disagreement between MOD and suppliers.

### Option Selection

12. Option 3, amending existing secondary legislation on exclusions is strongly recommended to maximise the effectiveness of the framework.

### Risks

13. The main risk to the successful implementation is that the new proposals turn out not to work as effectively as was hoped, or become overly burdensome relative to the value they offer. This is assessed as being – Probability Low; Impact Low.

14. There is also a risk that the supporting guidance is not in place when the amended legislation comes into force or that industry struggles to adjust to the changes. This is assessed as being – Probability L, Impact L.

#### *Mitigation of Risks*

15. The following approach has been adopted to mitigate the identified risks.

a) Quality of regulations - the SSRO will continue to keep the operation of the new framework under scrutiny and a further review will be completed by December 2020;

b) MOD is engaging closely with the SSRO and industry on the implementation of the changes.

### **Wider Impact**

#### *Markets, business and competition.*

16. The proposed amendment does not regulate competition or markets in any way.

### **Equality Impact Assessment**

17. Recognising the importance of demonstrating that the changes described above do not have any disproportionately positive or negative effects on any protect groups of individuals, we conducted an Equality Impact Assessment in line with Cabinet Office guidance prior to the introduction of the DRA in 2014. This assessment covered all nine protected groups (age, race, gender, disability, religion or belief, sexual orientation, gender reassignment, pregnancy and maternity, marriage and civil partnership) and concluded that there will be no equality or discriminatory impacts on any such groups.

18. We assess that the proposed amendment will not change this conclusion.

### **Communications**

19. There is a requirement to communicate the changes effectively to the relevant stakeholders both within MOD and with suppliers. We are already engaging with industry and the SSRO on the changes and this will continue through implementation.

#### *Periodic Review of Regulations*

20. The SSRO must keep the SSCRs under constant review and may recommend changes it considers necessary to the Secretary of State. In addition, the Secretary of State is required by legislation to complete a review of the regulations within three years of them coming into force and then every 5 years. The first review was completed in December 2017 and, given the complexity of the regulations and the need to keep them current, Secretary of State has decided to complete the next review in three rather than five years (i.e. by December 2020).