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Carillion: Two years on

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Summary

Two years after the collapse of Carillion, and a year after the government published its *Outsourcing Playbook* containing reforms to the way it outsources services, this report provides a stocktake of whether changes have been implemented. Overall, there are encouraging signs of progress. But improvements in key areas are patchy, and the reforms remain a long way from being fully embedded.

The government will need to provide further political support and investment if continued problems with outsourced contracts are to be avoided.

The Cabinet Office has done well to establish the new guidance in Whitehall and roll out training, at a time when the civil service has been under substantial pressure. The department has improved its relationship with big suppliers, the reforms have wide support from industry and there is some evidence that the guidance is being used directly to change poor behaviour by departments. Efforts to improve outsourcing have also been bolstered by the success of a longer-term initiative to bring in commercial expertise from outside government.

However, many suppliers still complain of poor practice. Several departments continue to ignore aspects of the new guidance, and many have not updated their internal policies. There is little evidence of improvements to the way government assesses risk and balances cost and quality. And scrutiny of departmental plans is not yet rigorous enough, meaning good practice is still dependent on individual ministers and senior officials.

The incomplete implementation of these reforms is to be expected. Only a small number of contracts have passed through the process in central government since the new guidance was brought in – meaning the full impact will not be apparent for at least another year. It is also not clear whether the guidance is being followed on lower value and less complex contracts, which the Cabinet Office does not monitor.

And there appears to be little awareness of the reforms beyond Whitehall, in local government and public bodies, including the NHS. These bodies manage procurement spend worth over £100bn annually, but the Cabinet Office currently has no remit or budget to extend the reforms beyond central government.[1]

In the wake of Carillion, Theresa May's administration outlined significant changes needed to improve government's approach to outsourcing and construction projects. In our September 2019 report, *Government Outsourcing: What has worked and what needs reform*,[2] we praised this approach, and argued that implementing the reforms contained in the *Playbook* fully would address most of the problems in government outsourcing. We recognised this would be difficult. But the new Johnson administration must commit to delivering those changes. Without continued political support, they will be forgotten amid other priorities.

The team in the Cabinet Office providing training and support must also be centrally funded for the rest of the parliament and enabled to support local government, the NHS and other public bodies to improve their procurement practices. Reflecting on the experience of reforms so far, the government should also take further action to strengthen compliance and address continued problems around risk transfer and low-cost bidding.

Carillion's collapse was also a stark illustration of a rotten corporate culture: the company took imprudent risks, acquired huge debts, and disguised its problems with aggressive accounting practices.[3] That the company was able to behave so recklessly for so long demonstrated that the system of checks and balances was wholly inadequate. These weaknesses had been made apparent before, for instance with the 2015 inquiry into the sale of British Home Stores, and again after Carillion during the collapse of Thomas Cook in September 2019.[4]

But Carillion may yet prove a crisis large enough to spur action. Five inquiries into how to strengthen UK corporate governance have been launched since the company's collapse; several have returned serious proposals for reform. Implementing recommendations from these reviews – and ensuring no company can get away with such behaviour in future – is essential if government is to show it has truly learned the lessons of Carillion.

The collapse of Carillion

Carillion's collapse on 15 January 2018 sent shockwaves through government and industry. In the corridors of Whitehall, it raised concerns about the day-to-day running of services on which the public relies, and prompted reflection on the wider health of government's outsourcing markets. In the boardrooms of government suppliers, it was a stark warning of where a high-risk, low-margin business model could lead – and a clear indication that government's largest suppliers would be allowed to fail.

Government's immediate response to Carillion's collapse was effective

Carillion was the UK's second-largest construction and services company, with 18,000 employees in the UK and global revenues of more than £5bn. At the time of its collapse, it held 420 UK public sector contracts, including for the construction of hospitals, highways and railways; the maintenance of army homes; and cleaning in schools and prisons.[5]

In the schools and prisons where Carillion provided services, the company's collapse may not even have been noticed, but for a change of company logos. Most of Carillion's government contracts were handed over to new suppliers and continued relatively seamlessly. This was a major success of contingency planning initiated by government in advance of Carillion's collapse, with alternative suppliers agreeing to pick up contracts.

Some projects proved more difficult to unpick. Carillion's private finance initiative (PFI) contracts to build new hospitals in Liverpool and Birmingham were severely delayed as government had to find new suppliers and renegotiate complex arrangements. The hospitals are currently set to be up to five years late, harming patients who urgently need upgraded facilities.[6] Other construction contracts also saw delays.

Government refused to bail out Carillion, despite the company issuing what MPs described as a "last-minute ransom note" in early January requesting £160m of support.[7] Carillion's chairman claimed this was necessary to avoid "enormous costs to government, far exceeding the costs of continued funding [as well as] widespread loss of employment, operational continuity, [and] impact on our customers and suppliers".[8]

In reality, the most recent update put the company's liquidation cost at £62m – less than half the amount Carillion asked for – and this figure could fall further yet.[*,9] The joint parliamentary inquiry into Carillion concluded that government had made the correct call in refusing a bail out, arguing that taxpayers should not have to cover private sector losses or allow rewards for failure.[10] Government's refusal to step in also established an important precedent for others seeking government support.

* The government initially made £150m available for liquidation and the National Audit Office (NAO) originally reported costs of £148m, but the official receiver provided an update in December 2018, reporting an estimated figure of £72m, and a further update in September 2019, reporting an estimate of £62m, with the possibility of further reductions.

Not everyone came out of the collapse well. More than 2,000 employees were made redundant, although the official receiver minimised job losses by finding employment for over 11,000 staff where contracts were transferred.[11] The firm also owed around £2bn to 30,000 of its suppliers, subcontractors and short-term creditors, many of whom lacked trade insurance against its default.[12] On 25 January 2018, insurers reported they had paid out only around £31m to firms that were covered, while most of Carillion's assets also went to secured creditors during liquidation.

It is unclear exactly how much subcontractors lost because government has not measured the impact on Carillion's supply chain.[*,13] A survey found that, on average, small businesses in Carillion's supply chain were owed £141,000; medium-sized firms (those with 50–250 employees) £236,000; and large firms £15m.[14] Analysis by the accountancy firm Moore Stephens suggested 780 small UK construction companies entered insolvency in the first quarter of 2018, up one fifth on the same period the previous year, which the firm attributed to Carillion's collapse.[15]

But without better data it is not possible to draw firm conclusions. As previous Institute for Government research has argued, the government should improve the data it holds on its supply chains by requiring contractors to publish contract award notices for subcontracts worth over £25,000.[16]

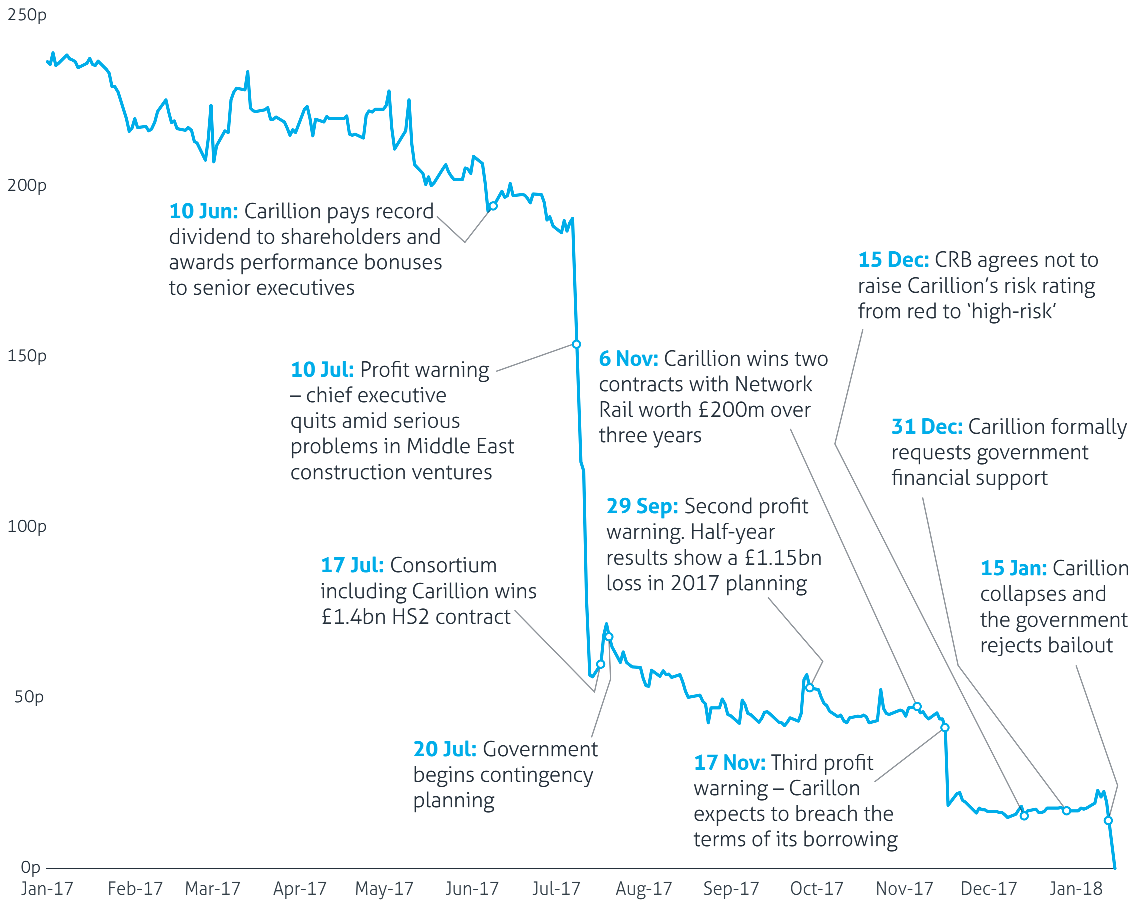
These outcomes are unfortunate, but companies (including those in Carillion's supply chain) are ultimately responsible for the risks they take on, and taxpayers cannot be expected to sustain a reckless, failing business, in which investors have lost confidence. On balance, in its immediate response, government played a difficult hand well – and succeeded in minimising disruption, costs to taxpayers and redundancies.

Carillion's recklessness was mostly to blame for its downfall, but government also bears some responsibility

Carillion's rise and fall was, in the words of the joint parliamentary inquiry, "a story of recklessness, hubris and greed".[17] It took on a string of low-margin, high-risk contracts in the UK and abroad, and hit problems when these projects started to go wrong. A dispute over payments on large contracts in Qatar, and big losses on the Royal Liverpool Hospital and Battersea Power Station projects, destroyed the company's cash flow, which fell from £512m in December 2016 to just £29m a year later.[18]

* The Department for Business, Energy and Industrial Strategy set up a lending facility for affected companies but take up has been low. Comptroller and Auditor General, *Investigation into the Government's Handling of the Collapse of Carillion*, Session 2017-19, HC 1002, National Audit Office, 2019.

Figure 1 **Timeline of Carillion's collapse, share price in pence (Sterling)**



Source: Institute for Government analysis of Carillion share price, sharesmagazine.co.uk, www.sharesmagazine.co.uk/shares/share/CLLN/historic-prices, retrieved 02 March 2020, retrieved 27 February 2020. CRB = Commercial Relations Board.

Carillion exemplified bad business practices. It was renowned for bidding aggressively (and unsustainably) low to win work, undercutting other companies. Even as its debts piled up, it continued to take huge risks, acquiring companies for more than their value and bidding for work in uncertain markets, particularly in the construction sector.

It paid its suppliers extremely late, offering standard payment terms of four months* and demanding a price cut for earlier payment – an arrangement it used to shore up its balance sheet without care for its suppliers.[19] It failed to make adequate contributions to pension schemes and disguised all of its problems with aggressive accounting practices.[20] Rather than challenging such behaviour, Carillion's board continued to award generous bonuses even as performance declined.**

* A maximum of 60 days is considered best practice.

** For instance, in June 2017, weeks before it issued a profit warning and seven months before it collapsed, it awarded large performance bonuses to executives. See House of Commons Business, Energy and Industrial Strategy and Work and Pensions Committees, *Carillion: Second joint report from the Business, Energy and Industrial Strategy and Work and Pensions Committees*, Session 2017–19 HC 769, The Stationery Office, 2018.

But while Carillion became a corporate monster, government also bears some responsibility for its creation. Checks and balances intended to prevent just such behaviour failed (and will be discussed in detail below). But also, through its contracting of both construction and services, government supported the creation of increasingly low-margin, high-risk markets.

People we interviewed while researching this report agreed that while in the 2000s suppliers may have "made off like bandits" – making excessive profits due to government's commercial naivety – since 2010, the pendulum had swung too far back the other way, with many contracts becoming loss-making and contractors struggling to break even. At the same time, government often tried to transfer all contract risks to suppliers, including those they could not control or reasonably manage (this has also been a problem on large infrastructure projects, including HS2).[*,21]

Companies were reckless in taking on such contracts. But government encouraged this recklessness through its own behaviour, and often failed to conduct sufficient due diligence to understand whether Carillion and others were financially or operationally able to deliver the contracts they were signing.

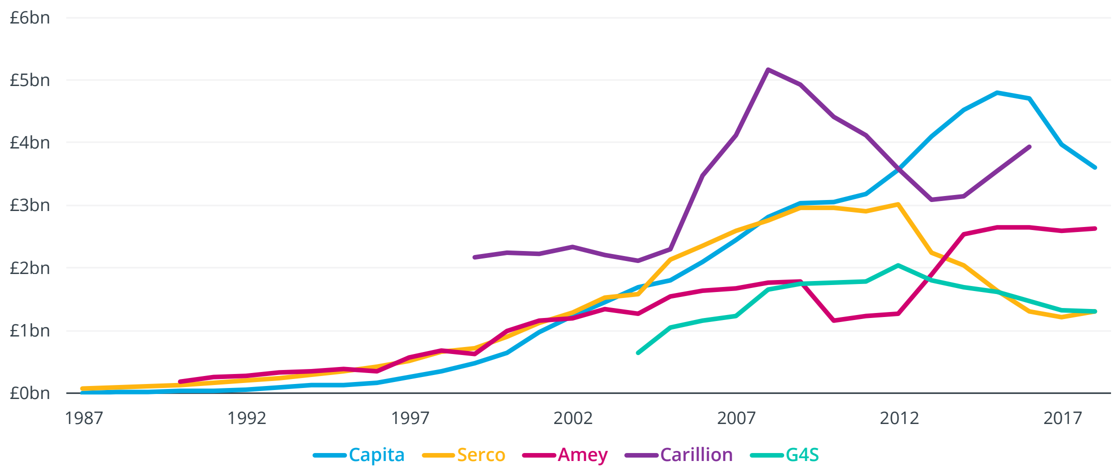
The hospitals Carillion was redeveloping in Liverpool and Birmingham, for which construction work began in 2014 and 2016 respectively, were a classic example of this. A National Audit Office (NAO) investigation published in 2020 found that in both cases the contracting organisations selected bids submitted by Carillion that were priced too low to meet the required specification.[22] When large risks materialised – including the presence of asbestos and cracks in structural beams – Carillion proved unable to manage them.

* It is important to note that construction, in particular, is an inherently risky business for both clients and suppliers. Large contractors will bid on hundreds of contracts a day. Ground conditions, logistical constraints, subcontract requirements and structural requirements all create scope for overspend and delay. Nevertheless, government's approach to managing risk in these areas has deteriorated in recent years (we discuss this more on pages 21–23). Stevenson J, 'Why auditors cannot build a reputation on construction', *Financial World*, June/July 2018.

Carillion’s collapse highlighted wider weaknesses in the sector

Carillion was an extreme example of risk-taking, but it was not an outlier. In fact, most of government’s largest suppliers had similarly grown very large in a short amount of time (see Figure 2), often by pursuing revenue growth at the expense of operational control.

Figure 2 **UK revenue growth of selected major outsourcing companies, 1987–2019**



Source: Institute for Government analysis of annual reports and accounts for selected companies. Figures shown in June 2019 prices.

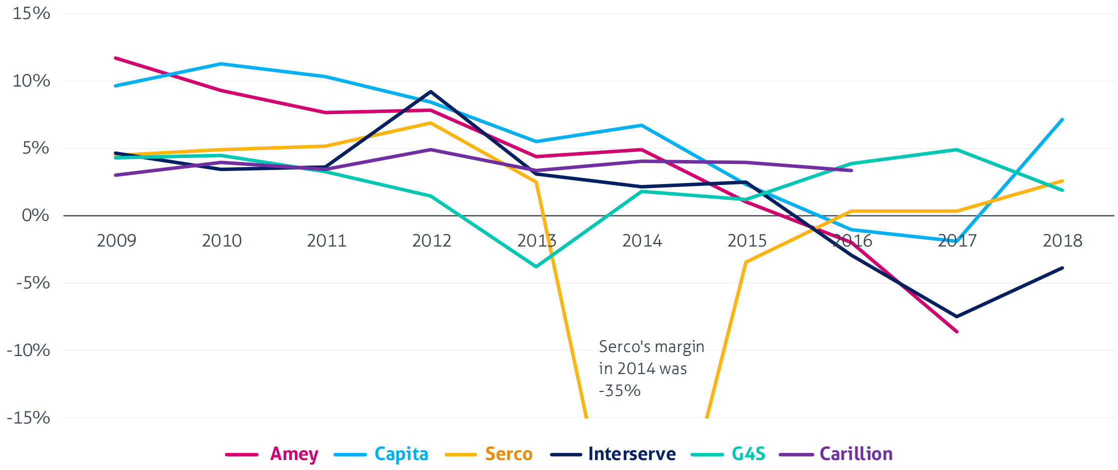
When Carillion collapsed, several other companies also had weak balance sheets and declining margins (see Figure 3). In 2016/17, none of government’s three largest suppliers – Capita, Carillion and Amey – made a profit, despite all winning more government work.[*] Another told us it had not made a profit on UK central government work for five years.

Serco and G4S hit their respective crises slightly earlier, in 2013/14, following a major dispute over failed prisoner tagging contracts. This poor performance led some to call government contracting a ‘winner’s curse’ market.[**]

* This is according to published spend, which is necessarily an incomplete picture. See: Davies N, Chan O, Cheung A, Freeguard G and Norris E, *Government Procurement: The scale and nature of contracting in the UK*, Institute for Government, 2018, www.instituteforgovernment.org.uk/publications/government-procurement

** This means a market in which there is “a tendency for the winning bid in an auction to exceed the intrinsic value or true worth of an item” Investopedia, ‘Winner’s curse’, Investopedia, no date, retrieved 24 May 2019, www.investopedia.com/terms/w/winnerscurse.asp

Figure 3 **Profit margins for selected large UK outsourcing companies**



Source: Orbis analysis of annual reports and accounts for selected companies. The profit margin given is pre-tax profit after expenses (including interest, depreciation and amortisation) as a percentage of sales. There are considerable fluctuations due to exceptional charges such as penalties and impairments to goodwill. Carillion did not file accounts after 2016.

Many of these companies had, like Carillion, taken on high-risk, low-margin contracts.[*] In March 2019, Interserve – Britain's largest provider of probation services, which also cleaned and maintained schools, hospitals and train stations – entered 'pre-pack administration'. This means it arranged to sell its assets to a buyer before appointing an administrator to facilitate a sale, allowing it to continue to operate under the ownership of its banks.

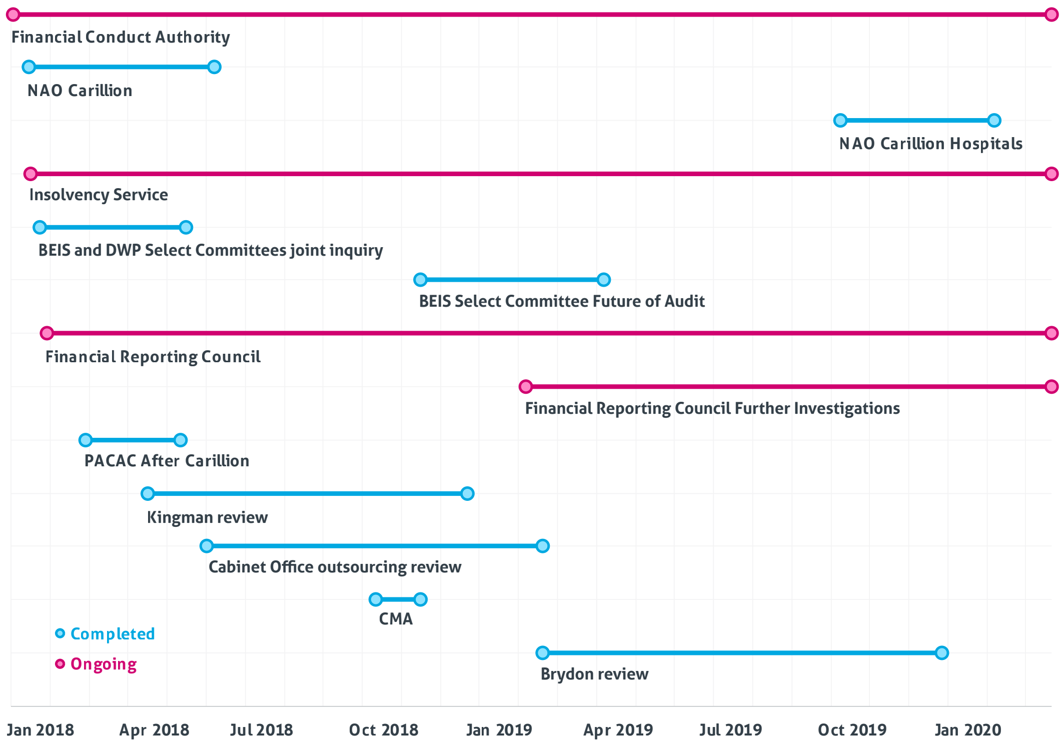
Interserve's problems were largely the result of its decision to take on contracts in the UK energy sector – an area in which it had insufficient expertise, according to Debbie White, who was appointed as its CEO in September 2017.[23] It also held loss-making contracts in probation, where it also had little prior experience, facilities management and construction.[24]

The collapse prompted an examination of government's approach to outsourcing and its system of checks and balances

John Manzoni, chief executive of the civil service, said Carillion's collapse had put government "firmly under the microscope".[25] In its wake, no fewer than 13 inquiries have been launched by a range of bodies, looking variously into the company's collapse, the government's wider approach to outsourcing, and the role of audit and corporate governance regulations (see Figure 4). Four are still ongoing.

* We discuss these contracts in Sasse T, Guerin B, Davies N, Nickson S, O'Brien M and Pope T, *Government Outsourcing: What has worked and what needs reform?*, Institute for Government, 2019 www.instituteforgovernment.org.uk/publications/government-outsourcing-reform

Figure 4 **Inquiries launched since the collapse of Carillion**



Source: Institute for Government analysis. A list of abbreviations is found on page 31.

The Cabinet Office's review, carried out in partnership with suppliers, acknowledged the problems described above. In January 2019, it published the *Outsourcing Playbook*, a guidance document for officials that aims to set out principles of best practice. The *Playbook* includes proposals on how to make the right decision on whether to outsource, strengthen early market engagement, improve risk allocation, and get the right balance of cost and quality in selecting a bid.

In our September 2019 report *Government Outsourcing: What has worked and what needs reform*, we argued that if the *Playbook* was fully implemented, it would address most of the problems in government outsourcing.[26] However, we noted that implementation and culture change would be difficult. Many of its proposals were already government policy – and had been frequently ignored.

Other reviews focused on the wider system. A joint parliamentary inquiry found that checks and balances had failed, which allowed Carillion to disguise its problems for too long. It argued that the Crown Representative system[*] was ineffective and gave little warning of risks; Carillion's auditor, KPMG, was "complacent" and "failed to exercise professional scepticism" towards Carillion's accounting judgements, meaning it was complicit in them; and the Financial Reporting Council (FRC), responsible for regulating

* Since 2011, government has appointed 'Crown Representatives' to improve government's relationship with its largest suppliers, small- and medium-sized employers (SMEs), charities and specific sectors, such as consultancy. There was a Crown Representative responsible for Carillion. The post was vacant between August and November 2017, but a parliamentary inquiry found the role was ineffective prior to this. See Commons Select Committee, 'Crown Reps "more Johnny English than James Bond"', parliament.uk, September 2018, www.parliament.uk/business/committees/committees-a-z/commons-select/work-and-pensions-committee/news-parliament-2017/carillion-government-response-17-19/

audit, and the Pensions Regulator were "united in their feebleness and timidity".[27] The inquiry also found that the Prompt Payment Code, overseen by the Department for Business, Energy and Industrial Strategy (BEIS), had been wholly ineffective.[28]

Three further reviews have returned detailed recommendations for strengthening corporate governance. The Competition and Markets Authority (CMA) recommended an operational split of audit from consulting services, beginning with the 'big four' audit firms in the UK.[29] This 'firewall' – similar to the separation of retail and investment banking following the 2007/08 financial crash – would entail the separation of management (both CEO and board), accounts and remuneration and an end to profit-sharing. The CMA also proposed measures for increasing competition in audit.

The Kingman review – commissioned by the then business secretary, Greg Clark, and led by Sir John Kingman, former second permanent secretary of the Treasury – recommended replacing the FRC with an independent statutory regulator. (The FRC had begun as a private membership body and, unlike almost any other major regulator, had no statutory powers, relied on voluntary action and self-regulation, and was funded via a voluntary industry levy.) The Audit Reporting and Governance Authority (ARGA) was established by the government in 2019 and is accountable to parliament.[30]

Kingman also recommended in a separate letter that government should create an independent body responsible for appointing auditors, rather than auditors being chosen by a company's board and shareholders.[31]

The Brydon review focussed on the audit profession, recommending a redefinition of the purpose of audit based on new principles, and new practices to strengthen the audit process, including looking beyond financial statements.[32]

The FRC's own investigation into KPMG, opened in January 2018, has still not reported. The FRC says it expects to complete the first stage by this summer and attributed the delay to the sheer complexity and scale of the case.[33] The official receiver's investigation into potential wrongdoing of company directors and the Financial Conduct Authority's investigation into potential insider trading have also not concluded.

Has government implemented reforms?

The *Outsourcing Playbook* has been widely accepted and it has led to some improvements in government procurement practice, such as the publication of commercial pipelines. Commercial skills are also improving. But implementation across government has been inconsistent, and there is little evidence yet of improvement in areas such as risk allocation and bid selection. Proposed reforms to corporate governance have also not yet been fully implemented.

The *Outsourcing Playbook* has gathered wide support in Whitehall and industry – and the initial rollout to departments has been successful

The *Playbook* has passed the first hurdle of any attempt to reform government process: it has been widely accepted as sensible and helpful. This was not a given.

While many of its policies were not new and had been included in other government procurement policies, training or spending guidance, the *Playbook* brought a wide range of guidance together into one structured process, to which departments could then be held accountable. Commercial directors and other senior officials we spoke to all strongly supported this change, as did suppliers. None of our interviewees disagreed with, or objected to, any of the *Playbook*'s policies, although some felt they could go further in certain areas.

The Cabinet Office has also, since 2018, provided introductory training to departments, as well as more specialist training in areas such as producing 'should cost models' (a total estimation of the cost of delivering a service) and conducting financial evaluation. All departments have participated in the training and take-up has been relatively high – 8,000 officials have taken part – despite it coinciding with a period of high pressure for many civil servants due to Brexit. The Cabinet Office is also looking at producing online learning materials to make training more widely accessible.

This training has led senior officials in central government to use the *Playbook*. One director responsible for a large, complex procurement said: "It's not gathering dust; we talk about it regularly… everyone agrees with it and we keep referring back to it". However, officials acknowledged that in terms of practical adoption of its reforms, they were still "in the foothills" – that is, there is still a long way to go. Several suppliers suggested that dissemination at more junior levels had so far been less successful, and that the "cascade process" had not happened.

The *Playbook*'s guidance applies to all outsourced services, however some aspects, such as the requirement to conduct 'should cost models', only applies to 'complex' projects or those over the value of £10m.[*] Indeed, the training and support appears to have focused on larger or more complex contracts – and it is unclear to what extent the principles are being applied to other contracts. Training so far has also focused mostly on those in commercial roles, but the Cabinet Office plans to discuss the reforms more widely, including with policy, legal and operational officials.

* The Cabinet Office defines a complex contract as any of the following: "first generation outsourcing; significant transformation of service delivery; obtaining services from markets with limited competition or where Government is the only customer; and/ or any service obtained by contract that is considered novel or contentious."

The Cabinet Office recognised that it currently has limited ability to roll out the reforms beyond central government. The outsourcing team in the Cabinet Office is funded via a levy on central government departments, and those departments expect value for money. While the Cabinet Office has held meetings with local authorities, it is unable to provide local government and public bodies with training and support on a larger scale.

The reforms got strong ministerial support from the minister for the Cabinet Office, Oliver Dowden (who was also involved in their development), but he was promoted in the February 2020 reshuffle. At the time of publication, it is unclear which Cabinet Office minister will take on these responsibilities, but it is critical that they put their weight behind these reforms.

David Lidington, who oversaw the reforms, told us that he gained the support of other ministers across government when the *Playbook* was published, and as yet, there are no signs of ministers of other departments opposing processes in the *Playbook*. However, one senior official suggested that not all officials and ministers and taking seriously. And it will likely face tests in future when decisions are needed quickly.

Outsourcing reforms are helped by improvements in commercial skills

The collapse of Carillion in 2018 was a catalyst for change. But government is also starting to reap the benefits of reforms to strengthen commercial expertise initiated before 2018, whose impact has become clear in the last two years. This increased expertise is supporting efforts to raise standards set out in the *Playbook*. It is vital these efforts to build commercial expertise continue to receive support.

Government's commercial expertise has historically been identified as a weakness. In 2013, Institute for Government research found patchy capability in procurement, contract management and commissioning; in 2014, a review by the NAO found that contract management was often weak.[34] The civil service itself acknowledged in 2016 that commercial skills in government remained "scarce"; internal reviews at the time identified that "substantial value and money had been lost [due to] insufficient business acumen and capability".[35]

In May 2016, the late Lord Heywood, then cabinet secretary, and John Manzoni, chief executive of the civil service, said that "improving commercial skills and capability is one of the Civil Service Board's top three priorities".[36] They hired Gareth Rhys Williams as government chief commercial officer to lead the creation of a new commercial function, with the aim of raising standards across government. Manzoni and Rhys Williams both came to the civil service after careers in the private sector.

In 2017, we reported on the initial progress of those reforms, which included efforts to improve recruitment, retention and training, and to develop common standards and assessments.[37] We found they were focused on the right issues and had the potential to succeed, if they were given consistent leadership and the Cabinet Office maintained the buy-in of departments. The only areas of weakness our report noted were a lack of stable funding and limited engagement with non-specialists.[38]

Figure 5 **Timeline of commercial reforms**

2010

July 2010
Government begins renegotiating over 40 existing contracts with strategic suppliers.

February 2011
Contracts Finder, a centralised online log of upcoming government contracts worth over £10,000, launches.

April 2011
Crown representative roles created, to lead government relationships with strategic suppliers and get better value for money.

December 2013
After overbilling by G4S and Serco on MoJ electronic monitoring contracts, government launches commercial capability review.

March 2014
Chief commercial officer role established to lead the commercial profession.

April 2014
Crown Commercial Service established to centrally manage procurement of common goods and services across government.

September 2014
NAO finds contract management "weak" in areas including governance, payment, performance and risk in a majority of government contracts.

April 2015
DWP introduces 'category management' approach to commercial relationships. BEIS and others begin to do the same.

March 2016
Government Commercial Function – a network of commercial professionals – launches to co-ordinate across government.

July 2016
Civil Service Workforce Plan 2016–20 highlights the need to develop and retain "scarce" commercial skills.

February 2017
Government Commercial Organisation (GCO) launched to employ senior specialists (grade 7 and higher) on a competitive pay structure.

February 2019
Government publishes *Outsourcing Playbook*, new guidelines to improve quality of government outsourcing.

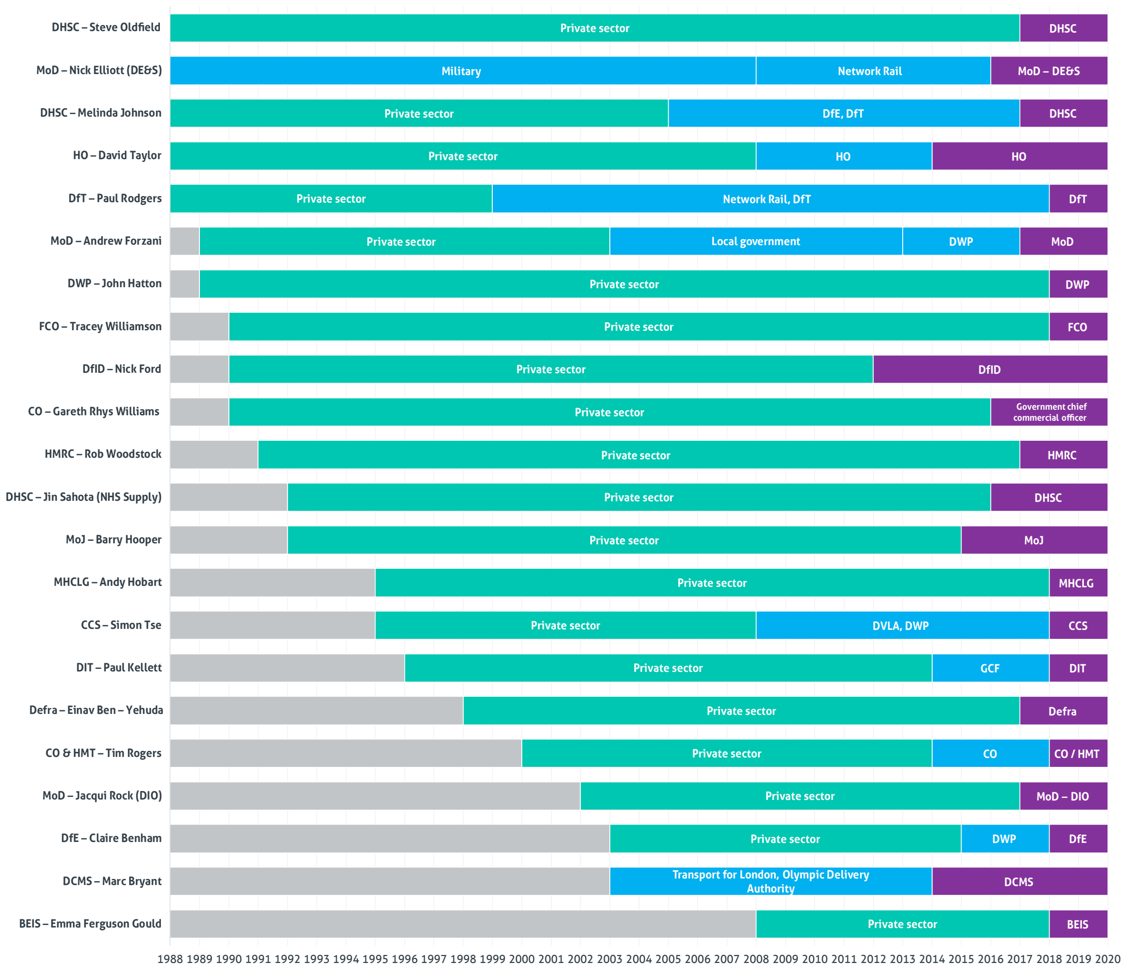
2020

Source: Institute for Government analysis. A list of abbreviations is found on page 31.

It is now clear that those commercial reforms are reaping benefits. Two reforms have made a particularly big difference in raising standards: recruiting senior leaders with extensive private sector experience, and rolling out challenging examinations across the wider profession.

Ten commercial directors have been appointed from the private sector since 2016. Historically, these posts tended to be filled by people with experience only of managing contracts in government, which led to a lack of business experience in negotiations with private sector counterparts. As Figure 6 shows, almost all of the current commercial directors have extensive private sector experience.

Figure 6 **Career path of commercial directors**



Source: Institute for Government analysis. Green = private sector; blue = public sector; purple = current role. A list of abbreviations is found on page 31.

The Cabinet Office created the Government Commercial Organisation (GCO) in 2017 to recruit and manage senior commercial officials, who are employed centrally but work in individual departments. Recognising that government must compete with much higher private sector salaries, the GCO has more flexibility on pay than normal civil service salary bands, which has been important in its success in filling bigger roles.

Several commercial directors noted that the group of commercial directors is now functioning more effectively across government, with a regular meeting being used to discuss problems and agree common approaches.

In 2016, the commercial function piloted an Assessment and Development Centre (ADC), which became fully operational in 2017.[39] Every commercial official above the G7 grade, a mid-level position typically two grades below the senior civil service, must pass through the assessment to gain accreditation as a commercial expert. The centre is also used for external recruitment.

So far, over 2,700 officials have been assessed, three quarters of whom were internal candidates. The assessment is designed to be a difficult: while the pass rate is not publicly available, one senior official told us this training had led to them "getting rid of a large number of commercial officials who weren't up to the job". Further training should be applied to more junior staff: officials below the G7 grade are often responsible for contracts, and interviewees had observed less improvement at these levels.

The Johnson government will also need to invest to continue benefiting from these changes. Contract management requires improvement, and too often it is still left to junior officials who lack the confidence or expertise to challenge suppliers. And interviewees noted that while people may join the civil service from the private sector because they are motivated by public service, retention will always remain difficult due to inferior compensation packages.

The civil service should also further integrate senior commercial officials, such as commercial directors, into departmental leadership teams and ensure they are given early sight of policies, particularly in departments with high procurement spend.

Continued commitment to improving commercial skills in government is particularly important given that Manzoni, who has championed these reforms, will leave the civil service in the coming months, having completed a five-year term. Commercial reforms must remain a priority for his successor.

But implementation of reforms has so far been patchy

The adoption of best practice set out in the *Outsourcing Playbook* has been patchy, and suppliers we spoke to diverged on which departments and specific procurements had been compliant (or not). For their part, some departments recognised they have "further to go" to reach consistently high standards.

Suppliers with positive views highlighted the change of culture in departments' work, and noted improvements on several contracts, especially in pre-market engagement. One told us that the Prisoner Escorting and Custody Services contract, awarded in October 2019, was one of the best-run procurements they had seen during their career.

However, others insisted "nothing has changed". One CEO of a large charity, which does 10% of its work for a government department, said that "conversations have not changed at all. It feels exactly as it did before: government wants more for less, there's no evidence of 'should cost models' or a more sensible approach to risk."

Interviewees raised several specific contracts that they believed were not compliant with the guidance, including a large facilities management contract that showed limited evidence of proper 'should cost modelling'; a framework contract that ignored principles around risk provisions and cost versus value; and several other frameworks, including for IT services, construction and consultancy, that contradicted *Playbook* principles.

Suppliers' experience will, of course, be coloured by the bids and contracts they work on. An industry expert, with a view across the sector, said they would estimate the level of 'penetration' – how often departments were following the *Playbook* – at 50%. One big supplier who works on contracts with many departments said they had "seen some traction, some departments using it, but others not at all".

Suppliers and officials recognised that some departments have "further to go" because they are starting from a lower base. One supplier said the Department for Work and Pensions (DWP) and the Ministry of Defence (MOD) were "still the departments that give us grey hairs". They noted the two departments dealt with complex estates programmes but said that issues around data quality, frequent policy changes and extending or delaying procurements were more common with them than other departments.

Suppliers' awareness of the *Playbook*, and their ability to raise problems, also varies. Strategic suppliers tend to be highly engaged: many were involved in developing the *Playbook* and have a direct line to the Cabinet Office through their crown representative who can raise issues of non-compliance on their behalf.

At least one supplier we spoke to was training its staff on the *Playbook*'s principles. But awareness among small and medium-sized suppliers is low, as it is for some large suppliers who are less closely involved with government policy. One executive responsible for a business with several hundred million pounds' worth of government contracts had not heard of the *Playbook*.

While the Cabinet Office cannot force compliance, it can work with suppliers to identify problems, use the controls process to improve projects, and deploy its 'soft power' to encourage or cajole recalcitrant departments. Suppliers told us they felt over time this "pincer movement" would deliver results.

Below we set out where best practices have and have not been adopted in the past year, focusing on five key priorities identified in the *Playbook*: pre-market engagement, the decision to outsource, piloting, risk allocation and bid selection.

Pre-market engagement

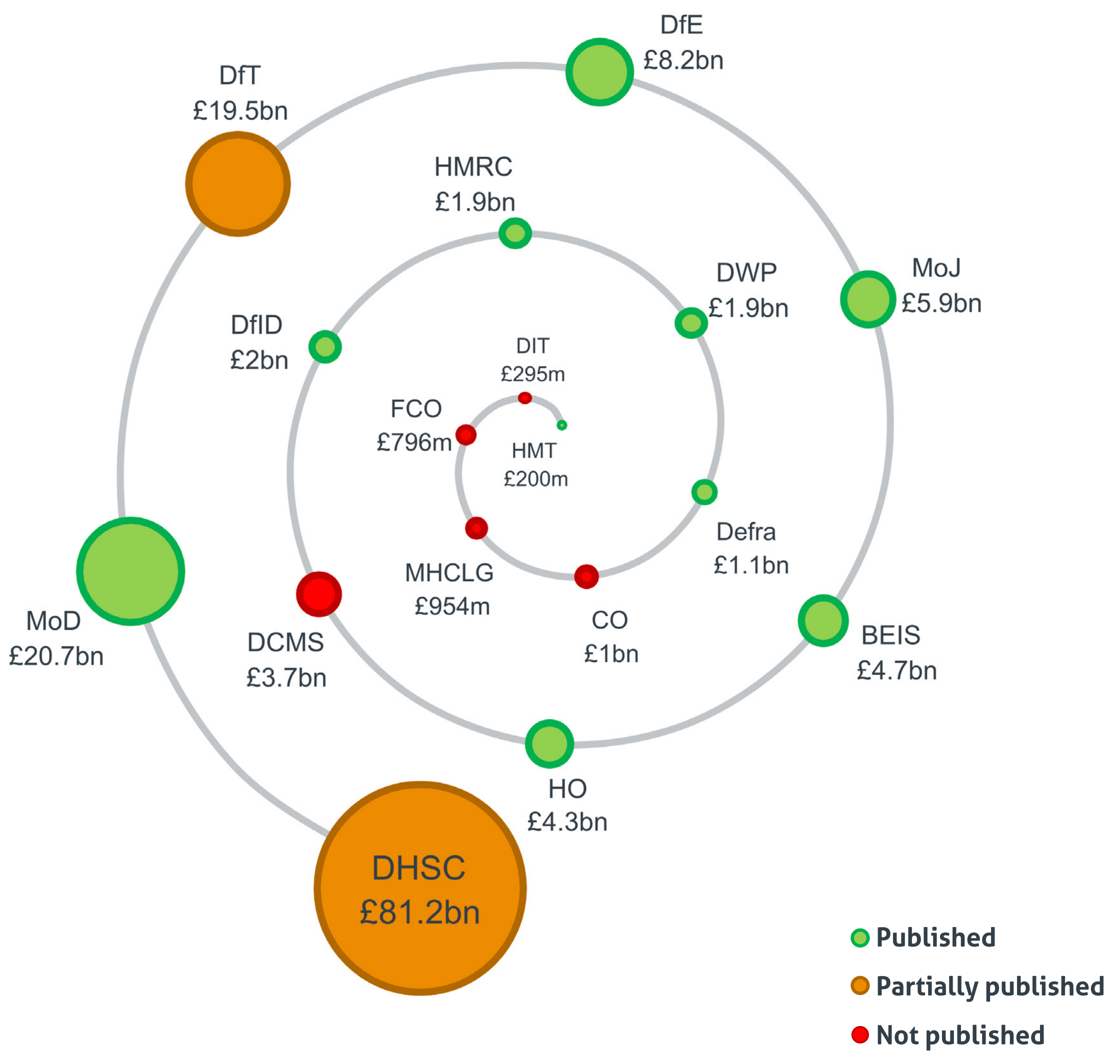
Poor market engagement has been a historic weakness of government procurement and often caused problems with negotiating and managing contracts.[*,40] Pre-market engagement – research and conversations with suppliers prior to procurement, before any tenders or business cases are drawn up – is often limited due to a lack of time, expertise and confidence.[41]

* Bill Crothers, who was chief commercial officer during the coalition government, argued in 2015 that departments typically spent too little time on pre-market engagement and, as a result, too much time negotiating the contract, because they had let tenders poorly.

The *Playbook* set out clear guidelines to help address this: all central government departments would be expected to publish their 'pipelines' of upcoming procurements, and officials would assess the health and capability of the market early on in all outsourcing projects.

There has been clear progress on the publication of pipelines, but their quality needs to be improved if they are to be useful to suppliers. Of 17 departments, 10 have fully published a commercial pipeline (see Figure 7) in the past 12 months.* Others are expected to follow, but factors including internal sign-off procedures, ministerial approval and national security concerns can delay publication.

Figure 7 **Government departments' publication of commercial pipelines by size of procurement spend**



Source: Institute for Government analysis of GOV.UK and planned expenditure 2019/20 in Public Expenditure Statistic Analysis 2019. A list of abbreviations is found on page 31.

* We judged two departments as having 'partially published' their pipeline. The Department of Health and Social Care has published a pipeline, but none of its public bodies, which make up most of its spending, have done so. The Department for Transport has not published a pipeline, although several of its public bodies have.

One commercial director explained the importance of departments publishing commercial pipelines, telling us that suppliers often previously complained: "we don't know what you're doing, you give us no certainty". With a clear pipeline for different clients across government, suppliers can plan much more easily and effectively, and avoid costs related to uncertainty. For large private sector companies who contract out a lot of services themselves, offering clarity to suppliers is standard practice.

Publishing pipelines is also beneficial for government. When departments offer earlier indications about their plans, they can better prepare for tendering contracts and free up more of their officials' time for pre-market engagement. One official explained it was "better to create space at front end [of a procurement] rather than hoping for space at back end", when ministers get involved and often demand things happen quickly. While ministers change frequently and new ministers may decide to scrap or amend existing procurement plans,[42] the existence of a clear pipeline still enables more effective decision making and prioritisation.

The amount of information provided in the pipelines published in the last year varies. While some were detailed and broken down into categories, others were more cursory. Suppliers told us they welcomed their publication but said they needed to include more detailed scope for services, affordability limits and reasonably firm timetables for them to be useful. While variation is to be expected in the first batch, departments should provide as much detail as possible, and the Cabinet Office and leading commercial directors should help them do so by providing support and coaching.

Departments also need to ensure their pipelines are clearly accessible and up to date. Several are not easy to find on GOV.UK or are buried in other commercial documents, such as SME Action Plans. This is not helpful, and makes it difficult for suppliers to have confidence that the information is up to date. A centralised webpage, managed by the Cabinet Office and containing links to each department's up-to-date pipeline, would help here.

One commercial director argued that publishing two-year pipelines should be standard across government, as all departments should think at least this far ahead to avoid rushed decisions. While there might be a small number of examples where this would be difficult, two-year pipelines would be a sensible standard expectation and would deliver further benefits for suppliers and government. We would recommend that the Cabinet Office make this a formal requirement when they update the *Playbook* in spring 2020.

Interviewees suggested wider improvements in pre-market engagement have been patchy. The *Playbook* process has enabled more collaborative dialogue and more open and detailed conversations, especially in bigger spending departments and with larger clients. But on smaller programmes, while pre-market engagement is happening more, suppliers told us that the quality has not improved. In addition, suppliers complained that engagement is still often a "tick box exercise" which doesn't lead to proper dialogue, and it typically does not happen early enough.

This suggests that improving skills and devoting enough resources to conversations with suppliers will remain key.

Government also appears to have made progress on market monitoring. It has a stronger relationship with strategic suppliers than it did two years ago, and has developed a clear code of conduct. The Cabinet Office acknowledged that officials have at times been too timid in asking for information. Departments have also started using more market information – such as 'H scores' and 'Z scores' used by brokers – to assess the financial health of providers, and these assessments are being shared and discussed more between departments.

Deciding whether to outsource

Improving the initial decision about whether to outsource a service or manage it in-house – referred to as a 'make vs buy' decision – was identified as a key priority in the *Playbook*. Getting such decisions wrong can be extremely costly.

The *Playbook* sets out several steps to improve decision making, and provides a new framework that includes a more rigorous make vs buy assessment, informed by cost-benefit analysis, and a beefed-up approvals process for particularly large and complex projects. Interviews suggest this has led to a more structured approach to decisions on whether to outsource, but that it may need further strengthening by giving the Cabinet Office extra resources, passing more projects through the full approvals process and ensuring ministers back up official-level scrutiny.

Departments have adopted the framework with enthusiasm: as of January 2020, the Cabinet Office had been called in to support make vs buy decisions on more than 25 complex outsourcing projects. This is more than was expected. One official responsible for insourcing a service (taking it back in-house) used the framework to show that this was the best option for the project, a decision which may have previously been met with greater opposition. Suppliers and industry bodies we spoke to said that the strengthened process was leading to better-informed discussions at the point of the make vs buy decision (although one noted that the guidance was quite "black and white" and may need more acknowledgement that in some cases a mix of public and private provision could be beneficial).

However, we are not convinced that the process is robust enough. Several interviewees suggested that the *Playbook* could be 'gamed' to produce the intended result. "We could make it say outsource and we could make it say insource," one told us. "The civil service is amazing at manipulating process. If you gave me and my team enough time, we could probably articulate anything as being in line with the *Playbook*." Another said the process was at risk of being "used to justify a decision rather than inform it".

The Cabinet Office will need extra resources for scrutiny. Its outsourcing team currently has limited staff capacity, which makes it difficult to effectively scrutinise the large number of make vs buy decisions for complex contracts worth over £10m. As one senior official put it: "does it feel like the Cabinet Office has the resources to properly scrutinise and hold to account big programmes? No, not really."

Cabinet Office officials, whose time for each contract is already limited, struggle to challenge departmental officials working full-time on a project, and who tend to be one step ahead on internal matters.

In terms of wider project approval, the project validation reviews conducted by the Cabinet Office and the Infrastructure and Projects Authority (IPA) are considered by departments to be "pretty exhaustive", although only a small number of projects currently go through this process, and it may need to be expanded.

The approvals process at official level is also heavily influenced by discussions at ministerial level, making strong political commitment vital. Ministerial sign-off of major procurements through cabinet sub-committees is much less robust than the assurance provided by the Cabinet Office and the IPA. When ministers in the Cabinet Office or the Treasury are not interested, it is difficult for officials to provide robust "check and challenge". Independent challenge panels – involving non-executive directors and commercial lawyers – can provide useful bolstering and should be used more often.

Officials also identified a potential tension between the *Playbook* and the accounting officer guidance that permanent secretaries are bound to by the Treasury's earlier guidance publications, *Managing Public Money* (2007) and the *Green Book* (2003). While interviewees agreed that the principles are aligned, some felt the *Playbook* could require more onerous standards, checks and processes. If these were not fully integrated into the plans of permanent secretaries and ministers early enough in their decision making, it could cause problems in following the *Playbook* guidance.

It will take time for the *Outsourcing Playbook* to be taken as seriously as these older and so more embedded guidance documents (which are also used to justify political decisions).[43] But it should be. All permanent secretaries have been briefed on the *Playbook*; it is vital they integrate it into their decisions.

Piloting

The *Playbook* established a presumption that there would be a pilot whenever a service is outsourced for the first time. This was a welcome step, intended to prevent departments from outsourcing complex projects at national scale without a clear idea of how they will work, as happened with probation.[44]

However, views vary on what constitutes a pilot and the level of burden deemed acceptable. For example, several charities and private companies argued that the Ministry of Justice's (MoJ) plan to bring the management of offenders back in-house while continuing to outsource some interventions, such as drug and alcohol services, had not been properly piloted.

However, the MoJ said that the operating model in Wales had served as a pilot for the introduction of the revised operating model in England, and that "prolonged engagement with the market had led to a detailed and considered approach" being taken to ensure the lessons had been learnt from previous outsourcing.

Several departments highlighted that it is often difficult, both politically and technically, to run a robust pilot before approving a project. As one senior official put it: "in parliamentary government when ministers want things to happen, you're never going to get things to happen in a really slow staged way". One commercial director said that running pilots also raises difficult questions:

> "How do you price a pilot, in cases where the investment would normally be amortised over the life of the contract? How do suppliers recover costs if they are not awarded a contract post-pilot? Who do you choose for the pilot (under fair and open competition rules)? Is the pilot a precursor to the issuance of a formal tender or part of it, and how do the other market players gain insight and learnings from the pilot? What are the success criteria against which pilots will be assessed? What if three worked and two failed, and how does this translate to a formal framework? Where a supplier fails at pilot stage, are they to be excluded from tendering? Do you embed a pilot in the contract with a break clause, or run it separately?"

Officials often don't have experience answering these questions. The Cabinet Office is planning to issue further guidance on piloting in its update to the *Playbook* in Spring 2020. This is sensible: clarification on basic standards and expectations around piloting is necessary. Departments should then be expected to comply with this guidance or explain any deviation. The Cabinet Office should also develop further training and support around piloting, and departments should evaluate their work and make public their findings in a timely way.

Risk transfer

Private companies can price and manage some risks well, but government has often attempted to transfer all risks, including high-cost, low-probability risks, that are beyond the control of suppliers. These cannot be competitively priced by the private sector, which means transferring them reduces competition and raises costs for government. As one supplier put it, "if you can't manage it you price it very high". It also invites companies to take on risks they cannot manage.

Government's approach to risk appears to have become more of a problem in recent decades.[*] Private companies we spoke to highlighted poor risk transfer as a top concern. Poor risk transfer has frequently been caused by nervousness among (often inexperienced) officials about taking on risks; an insufficient grasp of the complexities of risk allocation and liability; and, as the NAO has argued, poor understanding of the risks private companies can reasonably bear.[45] One interviewee summed this up, saying government's default approach has often been to "transfer all risk and see who bids lowest".

The *Playbook* set out a requirement that departments allocate risks to "the party best able to manage them". However, this was established as a principle in the *Green Book* and has been frequently ignored, while a 2018 survey found companies felt government's handling of risk had deteriorated since 2015.[46]

* For example, at an Institute for Government event, Rupert Soames, the chief executive of Serco, said: "huge amounts of completely unmanageable risk have been transferred into the private sector" and that this was the "key change [in government's approach] over the last 10 or 15 years".

We did not find evidence that government's approach to transferring risk has improved since the *Playbook* has been published – and we heard complaints from most of the suppliers we spoke to about the continued use of contractual clauses that breach the *Playbook*'s principles.

The inclusion of 'unlimited liability' – meaning suppliers can be held responsible for full costs and compensation, including finding alternative provision, should the contract fail[47] – came up frequently. The *Playbook* states clearly that "departments are expected to not ask suppliers to take on unlimited liability". But suppliers noted that it was still included in many contracts. Suppliers also highlighted the risk attached to 'change of law' clauses covering future government policy decisions that could have a significant impact on contracts, for instance by influencing the number of asylum seekers, prisoners or offenders using a service.

Suppliers have had risk provisions changed by referring departments to the Cabinet Office, but this is only possible when they are identified early in a procurement.

Interviewees identified several reasons why risk provisions continue to breach the *Playbook*'s rules. Some are cultural: departments have an attitude of "this is the way it's always been done" that will take time to change, while officials (and their external legal advisers) may simply "dust off" the contract used last time. Others are practical: frameworks or contracts agreed or tendered before the *Playbook*'s publication may be legally difficult or time-consuming to change now.

Some departments have updated their internal policies and guidance to align with the *Playbook*, but this has not happened consistently. One supplier reported that a department recently told them it was their policy never to accept capped liability, apparently unaware that this contravened the *Playbook*. All departments should clearly update their internal policies to be aligned with the whole *Playbook*, particularly given inexperienced officials may lack the confidence to break with what has previously been done, even if it is out of step with best practice.

However, further measures are also needed to improve risk allocation. Interviewees suggested that low compliance with the *Playbook* also stems from government lacking the capability to assess and allocate risks effectively. While it is standard practice in many private companies to have a 'chief risk officer', whose job it is to create an organisation-wide approach to risk management, this function does not exist in most departments. The MoJ appointed a director-level official in 2015 to fill precisely this gap, and suppliers suggested this had delivered improvements. Other departments should consider doing the same.

Selecting the right procurement procedure also remains a problem. Over the past five years, many departments have avoided using the 'competitive dialogue' or 'negotiated' procedures because they consider them too costly and slow, preferring instead to use the 'open' or 'restricted procurement' procedures. This means there is limited, if any, opportunity to discuss risk provisions once the process begins.

The *Playbook* states that competitive dialogue or negotiated procedures should be used when complexity and risk are identified as key issues, but departments appear to be ignoring this guidance.

The collapse of Carillion also highlighted the risks that subcontractors can take when waiting for payments. Government sought to address this through reforms to reduce the time taken for suppliers to pay their subcontractors. These changes appear to have been successful. The government's prompt payment policy requires those bidding for large contracts to demonstrate that 95% of all supply chain invoices are paid within 60 days.[48] Across the government's strategic suppliers, the average percentage of invoices paid later than 60 days on government contracts fell from 25% in 2017 to 14% in 2019.[*,49]

Bid selection

Successive governments have aimed to improve the way they assess and select bids to secure the best value. However, suppliers and officials consistently admit that "it always comes down to price". John Manzoni, chief executive of the civil service, said in 2018 that the civil service allows companies to "bid low just to win contracts… in part because we have not had the sophistication internally to do much other than go for price".[50]

The *Playbook* acknowledged a bias towards the lowest-price bid and stated that departments would be required to produce a 'should cost model' as part of the decision on whether to outsource a service. They would also refer any abnormally low bid (one that is more than 10% lower than the average of all bids or the 'should cost model') to the centralised assurance team in the Cabinet Office.

These measures are welcome, and interviewees noted some improvements in conversations around pricing. However, government's reforms do not appear have not delivered wholesale change in how bids are selected. Suppliers highlighted several examples of departments continuing to choose excessively low bids.

The state of the market has also influenced suppliers' bidding behaviour. Carillion was an example of a company taking high-risk, low-price bidding to its logical extreme: since its collapse, many suppliers have adopted more cautious strategies, avoiding very risky contracts and focusing on a narrower range of core activities (although some had begun to change earlier). Companies also noted government's refusal to renegotiate heavily loss-making contracts, which previously they had not expected.[51]

While the sector is still in recovery, the balance sheets of some major suppliers have started to improve, although this appears to have more to do with changes in leadership than the *Playbook*. In 2019, Serco increased its revenue first the first time since 2013 and made an operating profit of £120m.[52]

* The year refers to the end date of the payment period, usually six months, reported by each supplier. Where these payment periods cover the end of one year and the beginning of the next, the data is allocated to the latter year.

Capita's revenue for 2018 was lower than the previous year, but it reported profits above expectations.[53] But these improvements were partly driven by non-UK and private sector work; others UK outsourcing companies are still struggling.[*,54]

As the market picks up, new entrants with riskier strategies will likely further test government's resolve. One interviewee highlighted the recent entry of a large US company with a reputation for aggressive bidding into the facilities management market as one such test.

The Cabinet Office is developing further guidance and support on should-cost modelling, which is sensible. It should also analyse the percentage of contracts that departments award to the lowest-price bid, and use this to inform its guidance and training. While the lowest-price bid may also represent the best value, such a metric would provide a useful indicator.

However, government will need to make deeper reforms to how Whitehall makes spending decisions if it is to deliver real change in departments' approach to price and value in outsourcing. As one commercial director said: "the economics of departments still point towards selecting low price bids... we have limited budgets and a certain amount we need to procure".

Producing robust 'should cost models' is a good start, but these must in turn be used to adjust the Treasury's expectation of what a department needs to spend to deliver services, or a department's expectation of the scope of services that can be delivered. This will be particularly important during the spending review in summer 2020. As one former minister told us: "in the public spending process it's in the interests of the Treasury and departments to massage the figures to make the sums add up, and companies that underbid can be very helpful with that."

Budgets or project scopes will need to be adjusted if what is planned does not appear to be affordable based on government's own modelling.

* Kier made a loss of over £200m in 2019, cut 1,200 jobs and was forced to sell large parts of its business in property development and facilities management. While Interserve has survived in the hands of its creditors, it has struggled to make a full recovery. Amey's owner Ferrovial, a Spanish infrastructure group, has been trying to sell the company off since early 2019, as it seeks to exit the UK outsourcing market.

What should government do next?

Reforms to government processes take time to bed in and, just a year on from the publication of the *Playbook*, it is too soon to make a full assessment of the success of the reforms contained in it. It will be another year until some large procurements, which typically take two years or more from pre-market engagement to the contract being signed, have passed through the full process. However, with a new government and new ministers taking up office, it is important to assess where government stands on outsourcing, to help it make the best-informed decisions it can about upcoming projects.

There are encouraging signs of progress. But reforms are a long way from being embedded, and bringing about a meaningful change in departments' culture will require sustained effort. The new government must commit to implementing changes. It is welcome that Dominic Cummings, the prime minister's chief adviser, has identified government procurement as a priority. We highlight three areas that will be critical to this.

No.10 and the Cabinet Office must continue to give reforms political backing

Any reforms that do not receive strong and consistent backing from ministers at the centre of government will fail. Ministers hell-bent on a delivering a project in a particular way will override assurance processes; officials attempting to provide checks and balances will be undermined; departments that have "always done things a certain way" will continue as before. Our previous research has shown that civil service reform and culture change requires consistent political backing if it is to succeed.[55]

The good news is that, so far, the outsourcing reforms initiated since the collapse of Carillion have been given strong ministerial backing. David Lidington, when chancellor of the duchy of Lancaster, secured support from the cabinet for the *Playbook*. Oliver Dowden, continued to provide clear support and direction until he was moved at the February 2020 reshuffle.

Following the reshuffle, it is not yet clear which junior minister will be responsible for procurement. Whoever it is, improving outsourcing should be a key part of their role and they should take it seriously.

This backing is key because the Cabinet Office has limited actual ability to enforce compliance. It can try to improve projects through the controls process, and departmental commercial directors ultimately report to Rhys Williams, which provides some direct accountability. But in truth the Cabinet Office must rely on 'soft power', encouraging and cajoling departments, to achieve change. Several interviewees highlighted that the *Playbook* is "only as good as the spirit in which it's engaged with", meaning that it will have little value if it is gamed or not taken seriously.

Outsourcing reforms will only gain traction if the centre of government makes clear it is a priority, and insists departments comply with robust assurance processes or explain why they have failed to do so. As one minister put it, "cohesion between Number 10, the Cabinet Office and the Treasury will be key" if government is to succeed in delivering lasting improvements in the way government spends money with external suppliers. No.10 should avoid the temptation to develop its own reform programme and put its weight behind implementation of the *Playbook*.

- **The minister for the Cabinet Office and No.10 should adopt a 'comply or explain' approach to departments following guidelines in the *Outsourcing Playbook.***

Transparent assessments would be an effective way to measure progress and apply pressure to departments that do not comply.

- **The Cabinet Office should commission or undertake an annual progress review of the *Outsourcing Playbook*, beginning in 2021, to assess the extent to which different measures have been adopted across all outsourced services.**

The Treasury should fund the implementation of the *Playbook*'s reforms until the end of the spending review period

The outsourcing team in the Cabinet Office is currently funded only until March 2021. Every supplier we asked agreed it would be foolish for the team to be disbanded just as outsourcing reforms were beginning to gain traction. One said it would be a "disaster". It is expected that the upcoming spending review will cover from 2021/22 to 2023/24. The team should be given a funding settlement until then.

The funding model should also change. The current model of 'top slicing' from central government departments prevents the Cabinet Office from working to extend best practices to local government and public bodies. It also creates a potential conflict of interests given the Cabinet Office team is funded by departments it has to quality assure; and departments complained they had lost resources they would prefer to spend in other ways.

It would be more sensible to provide the team with central block funding from the Treasury. This would give the team a more stable footing and the ability to plan their implementation and assurance work properly, rather than living hand-to-mouth. It would enable the team to allocate its resources based on where they would produce most benefit, rather than to justify the demands of sponsor departments. And it would free the Cabinet Office to devote greater resources to implementing the reforms in public bodies and local government.

The amount of funding required would be relatively paltry. In 2019, the Cabinet Office estimated it would need between £7m and £9m a year for two years, and £5m a year thereafter to provide ongoing support to departments. There is a case for investing more than this: several departments said the Cabinet Office would benefit from extra capacity for assurance; and it would need further budget to take on extra work to roll out the reforms beyond central government.

However, the Treasury would easily make this back many times in the money it saves from avoiding costly contract failures across the public sector, which can cost tens of millions of pounds or more for an individual contract.

- **At the 2020 spending review, the Treasury should fund the outsourcing team in the Cabinet Office to implement reforms until the end of the covered period.**

Outsourcing reforms should be extended to public bodies and local government

Local government and public bodies, including the NHS, are responsible for over £100bn of government procurement each year.[56] Just as with central government, these bodies have been responsible for major contract failures, such as NHS England's contract for Primary Care Services, Kernow Clinical Commissioning Group's contract for out-of-hours GP services and Birmingham City Council's contract for road maintenance.[*,57]

However, public bodies and local government are currently not part of government's outsourcing reforms. The *Playbook* makes clear that principles could apply more broadly, and groups such as the Local Government Association have promoted it to councils. But awareness of government reforms in these areas remains low.

This is particularly important because interviewees said that public bodies and local government are further behind in terms of developing commercial skills and raising standards. One interviewee described the NHS as a "basket case" for commercial skills. Although there are initiatives to improve procurement practice in local government and other public bodies, these are not as well resourced.

But as one supplier highlighted, the question is "how far does the writ [of the Cabinet Office] run?". Public bodies that report to central government departments should clearly follow the *Playbook* – and their parent department should support them in building capacity. But central government currently has no authority (or budget) to take a greater role in capacity building in local government or the NHS; its powers over the NHS are also restricted by the legal separation in the Health and Social Care Act 2012.

Interviewees noted that procurement regulations and how they cover different layers of UK government will be a question that comes for the UK as it redraws its relationship with the EU, and work has already begun within government to assess potential options for further reform here too.

However, central government has developed expertise in best practices around contracting that make it best placed to support efforts to build capacity and raise standards elsewhere.

* All of these contract failures are described in detail in our 2019 *Outsourcing* report.

There are clear benefits of such collaboration to central government and other public bodies (in improved contract outcomes) and suppliers (in greater consistency in procurement practice across the country). It should be possible to design an initiative where best practices are shared, while independence is respected and protected. In other areas, such as social value (wider social, economic and environmental benefits that can be delivered through public procurement), central government could reciprocally learn from what is happening in local government.

Local authorities and NHS bodies should also incorporate the *Playbook* into their own approaches to accountability, including audit committees, peer-review and review by independent bodies, such as Local Partnerships, a joint venture between the Cabinet Office and the Local Government Association.

In addition, the *Playbook* is currently not mandatory for large projects in the construction sector. The Confederation of British Industry (CBI) has argued that this undermines efforts to improve risk management and improve financial sustainability in construction.[58] It has recommended that the *Playbook* could be applied to public sector building and civil engineering projects over the value of £10m. This should be included in the next iteration of the *Playbook*.

- **The Cabinet Office should apply the *Playbook* to large construction projects and support the adoption of its reforms by the wider public sector.**

Further action is needed to strengthen checks and balances

In response to the broader inquiries into corporate governance and checks and balances on companies – both government suppliers and other businesses – some progress has been made but further action is needed if another Carillion is to be avoided.

The government has created a new regulator, the Audit Reporting and Governance Authority (ARGA), to oversee audit and financial accounting, and appointed a widely respected figure in Sir Jon Thompson as CEO. However, it has not yet passed legislation to equip the ARGA with the full statutory powers recommended by the Kingman review, and this does not appear to have been prioritised since the election. It should address this promptly.

The government is also yet to respond to Kingman's further proposal for an independent body to appoint auditors. While this appears likely to be rejected, an industry expert we spoke to strongly supported it, arguing that such a move would provide a clear and fundamental change in the system.

Government has accepted the CMA's recommendation of creating a firewall between audit and consulting, however it is not yet clear how this will be implemented. Interviewees warned that the devil would be in detail.

- **The government should implement the recommendations of the Kingman review by legislating to give the ARGA statutory powers.**

Conclusion

Carillion's collapse in January 2018 was a crisis for UK government, but it also created an opportunity to deliver lasting reform.

Since 2018, government has acknowledged long-standing problems with the way it outsources services and has embarked on a serious programme of reform. The *Outsourcing Playbook*, published in February 2019, was a major sign of intent to change behaviour; and several inquiries returned detailed suggestions for strengthening corporate governance.

The outsourcing reforms have made a good start in difficult circumstances. They have been widely accepted as sensible and helpful by officials and suppliers. Despite the pressures of Brexit, training has succeeded in familiarising officials with the new process, particularly at senior levels. There have been improvements in some areas. Suppliers familiar with the reforms now feel they have much stronger recourse should departments misbehave. After only a year, this is impressive.

But there is still some way to go. Some departments continue to ignore the guidance and have not updated their own internal policies. There is not yet evidence of improvements in the key areas of risk allocation and the assessment of the value of a bid. Awareness beyond central government is limited. And wider improvements to corporate governance have also not been properly implemented.

The new government must commit to fully implementing these reforms. It should provide the political support necessary to drive change in departments and equip the Cabinet Office with the resources to oversee implementation. It should work with local government and the NHS to extend best practice. And it should strengthen the checks and balances that allowed such a strategically important company to behave as it did for so long. Doing so is vital if government is to avoid another Carillion.

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List of abbreviations

BEIS	Department for Business, Energy and Industrial Strategy
CMA	Competitions and Markets Authority
CO	Cabinet Office
DCMS	Department for Digital, Culture, Media and Sport
Defra	Department for Environment, Food and Rural Affairs
DfE	Department for Education
DfID	Department for International Development
DfT	Department for Transport
DHSC	Department of Health and Social Care
DIT	Department for International Trade
DWP	Department for Work and Pensions
FCO	Foreign and Commonwealth Office
HMRC	Her Majesty's Revenue and Customs
HMT	Her Majesty's Treasury
HO	Home Office
MHCLG	Ministry of Housing, Communities and Local Government
MoD	Ministry of Defence
MoJ	Ministry of Justice
NAO	National Audit Office
PACAC	Public Administration and Constitutional Affairs Committee

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