

# Expert public procurement consultancy for Buyers and Suppliers at your service



## PASS Consultancy

BiP's Procurement Advice and Support Service (PASS) provides organisations with access to experts in public procurement practices and procedures, thus helping you develop and deliver effective and efficient procurement/tendering. Our team offers a range of services to meet your specific needs. Whichever area you would like evaluated and improved, we have the experts to help.

The PASS consultancy's mission is to help you deliver the best in government procurement/tendering through:

- Practical solutions to improve performance
- Innovative approaches to knowledge transfer within government
- Procurement manual and strategy
- Improved performance indicators
- Strategic direction and performance
- Opportunities offered by e-government
- Capacity to deliver change to meet identified needs
- Continuous improvement of services and challenging poor performance
- Sustainable development within decision-making processes and delivery of services
- EU-compliant processes
- Best-practice procurement training

## PASS Health Check

The PASS service can help your organisation examine its current procurement/tendering organisational structures, strategies, processes, practices and related strengths and weaknesses. It delivers a detailed PASS Mark Health Check Outcome Highlight Report (OHR) that outlines areas of strength as well as those requiring further attention, and provides an outline Project Initiation Document (PID) designed to deliver a more effective and efficient procurement/tendering process that will help you achieve optimum performance.



## PASS – Helping You Meet Key Objectives

The key objective of public procurement professionals is to ensure that the most suitable supplier is selected to provide goods and services on terms which are likely to offer the best value for money. The PASS service helps you meet this requirement and deliver contracts that offer best value-for-money terms with suppliers who will execute them efficiently.

## PASS Training

Our consultants can provide you with bespoke training packages to suit your needs. Consultancy and training is available for the following: environmental purchasing, partnering, evaluation, e-government, supplier debriefing, UK legal processes and precedents, contract management, EU-compliant tendering, tender writing and much more.

## PASS Online Guidance

The PASS service provides online guidances on all aspects of the public procurement/tendering process and legal requirements: [www.bipsolutions.com/html/briefing.php](http://www.bipsolutions.com/html/briefing.php)

## PASS – CAPS Service

Introducing CAPS – the public sector's guardian through the EU public procurement process, helping you to quickly access in-depth, authoritative EU public procurement procedure assistance. We are now pleased to offer your organisation access to this vast knowledge base as and when required, through subscription to BiP's new Contract Administration & Process Support (CAPS) helpline service. The CAPS service level agreement aims to answer 99% of your enquiries within one working day and 85% of these within one working hour.

## PASS In-house Presentations

PASS consultancy can provide you with in-house presentations suited to buyer or supplier as appropriate. Each presentation will be tailored to your requirements, whether they be with regards to improving your tendering practices or your procurement strategy or processes. Contact: [pass@bipsolutions.com](mailto:pass@bipsolutions.com)

The PASS Mark Health Check is a process-based evaluation technique that helps identify how your company can develop more effective processes when tendering for public sector contracts.

For further information on the PASS service, contact our Customer Services Team on 0141 332 8247, email [pass@bipsolutions.com](mailto:pass@bipsolutions.com) or visit [www.bipsolutions.com/pass/](http://www.bipsolutions.com/pass/)



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# THE DEFENCE INDUSTRIAL POLICY

## PART ONE OF TWO

The UK Ministry of Defence (MoD) is the largest customer of the private sector in the UK. An understanding of its Defence Industrial Policy (DIP) is therefore vital to those companies in the private sector that either currently supply to, or intend to supply to, the MoD.

The Defence Industrial Policy was launched in October 2002, after 18 months of discussion between the UK MoD, the Department of Trade and Industry (DTI) and industry. The Policy covers four broad areas – Acquiring Capability for the Armed Forces; Market Access; Research and Technology; and the Future.

There were six 'Overarching Themes':

- Provide required equipment at best value for money at a price the UK can afford.
- Review policy and implementation.
- Treat all defence suppliers that create value in the UK fairly, regardless of ownership.
- Maximise economic benefit to the UK from defence expenditure.
- Maintain close dialogue with industry.
- Sustain an environment that enhances competitiveness of defence industry.

The House of Commons Defence Select Committee examined the Policy in last year's Defence Procurement report and concluded: "We very much welcome the publication of the Defence Industrial Policy, bringing as it does a useful, though overdue, increase in transparency to this important area. The way its provisions and statements should be interpreted will inevitably have to be developed; by further debate and through 'case law'. Indeed, in some areas, including the use of competition and open markets and in risk management (two of the perhaps more contentious of its themes), the Policy's utility will be evident only with the passage of time."

This guidance, based on a report from the Defence Select Committee, looks at the first review of the Policy, industry's view of DIP and consolidation in the UK defence industry.



## FIRST REVIEW

The First Review of the implementation of the Defence Industrial Policy published in November 2003 set out the progress that had been made in the first year since the Policy was launched.

Minister of State for the Armed Forces Adam Ingram summarised the First Review as follows: "Since we launched the Policy we have worked closely with industry to develop and pursue a joint implementation plan. We have completed a review of progress over the first year. During this time our close and productive relationship with industry has developed further and we have agreed how we will take forward our common aims over the next few years.

"The Policy has been a significant driver in bringing together government and industry, resulting in better communication and access to information. We both recognise that the Policy is for the long term and that it will take some time to measure the full effects on defence programmes and the industry that supports them. We remain committed to the Policy and will continue to monitor its effectiveness and to develop best practice in this area among the MoD acquisition community. We will also continue to work to improve access to overseas defence markets and to maximise the benefits from our investment in research and technology."

## INDUSTRY'S VIEW

From the written evidence we received, it was clear that the Defence Industrial Policy has been very much welcomed by the defence industry, and that industry was keen to see the Policy developed further and implemented in full. Indeed, the Defence Manufacturers Association considered "the successful implementation of a DIP... crucial to the future defence policy, security and strategic independence of the UK".

A consistent message from the evidence we received from industry

was that the main impact of the Defence Industrial Policy to date was the improved dialogue between industry and government. John Howe, Vice-Chairman of Thales UK, told us that “there is actually more dialogue between industry and government ... than there was a few years ago”. His view was echoed by the Defence Industries Council, who acknowledged that the Policy had “intensified the dialogue between HMG and industry about the economic implications of defence”.

The Defence Manufacturers Association concluded that “after some 20 months of the Policy being launched no identifiable, tangible benefits have been delivered to date”, but acknowledged that the Policy was not expected to lead to significant changes in the short term. The Defence Industries Council considered the achievements to date to have been modest, noting that “it is hard to point to examples of positive application of the Policy, and decisions could still be taken that would run counter to any coherent framework on industrial capability”.

In several areas further progress was needed in implementing the Defence Industrial Policy, or the Policy needed to be developed further, or there were other concerns relating to the Policy.

These included:

- The need to develop an industrial strategy.
- The need to implement the Policy through the procurement process.
- Consolidation in the UK defence industry.
- Issues relating to open markets and access to technology.
- Relations between MoD and industry.

## INDUSTRIAL STRATEGY

A common concern identified by industry was the need for clarification on what UK industrial capabilities and defence industry would be required in the future.

This was emphasised by John Howe, who told us that: “there is still some way to go in one particular area which is clarity about what kinds of industrial capabilities and indeed what kinds of technologies are judged to be of crucial strategic importance in the long term. What kind of industry does the UK think it is important to have in the future? What kind of capabilities is it important to retain for strategic reasons? That is the area where I think we need to go on working to achieve more clarity.”

Sir Richard Evans, Chairman of BAE Systems, also highlighted the need for industry to have “some clear indications as to what the long-term requirements are, particularly in terms of where we are going to invest R&T for the future, and we need that a lot more quickly than appears to be the case at the moment”. He considered that “we should ... identify those areas that are strategically important for us in the long term and together concentrate our joint resources into making sure that we stay in the premier league in those areas”.

The VT Group considered that at the strategic level greater openness regarding long-term government expenditure planning would be helpful. This would not be detailed information on individual programme budgets but more general data on, for instance, future expenditure in a general capability area. They considered that this would reduce uncertainty for industry and encourage more effective investment decision-making.

Defence Procurement Minister Lord Bach also agreed that the main area where the Defence Industrial Policy needed to be developed further was in producing an industrial strategy to sit alongside the industrial policy. He told us that “we need to further develop and state what technologies and industrial capabilities are of the greatest importance to us in maintaining existing capabilities, and which ones we expect to require in the long term”.

Lord Bach said that a meeting had taken place with the National Defence Industries Council at the end of May 2004 and that “the NDIC supported fully our approach to an important development of an existing part of the Policy, namely ... our emerging work on industrial strategy. We are aiming to identify more explicitly the technical capabilities that we need to meet defence needs now and well into the future. We will assess the importance of sustaining these capabilities in the UK for national

security, for technology, or for wider economic reasons. This is a complex undertaking that will take some time to do properly.”

We welcome the fact that the MoD has recognised the importance of establishing an industrial strategy to sit alongside the Defence Industrial Policy, and that work is now in hand to take this forward. Such a strategy needs to provide industry with a clear picture of which industrial capabilities and technologies are considered to be of crucial strategic importance in the future. We recommend that the MoD takes forward this work as a matter of urgency.

In terms of specific sectors within the defence industry which need to be retained, Sir Peter Spencer KCB, Chief of Defence Procurement, told us that: “The nuclear sector is very important in terms of supporting the submarine building programme for a nuclear steam raising plant. The surface shipbuilding sector is very important in terms of ensuring that we have actually got the capacity, the skills and the capabilities to deliver the very large programme which is planned for surface shipbuilding, but we have got a bit of a gap in the meantime, which is a worry, and the work is wholly aimed at how we keep those key skills in place and reassure the companies concerned that we are looking at this intelligently.”

Sir Peter recognised that the MoD had “a responsibility to industry, as well as to the taxpayer, to make the most efficient use of those industrial assets”.

In terms of the criteria to be used to decide which sectors of the defence industry it was vital to retain, Sir Peter told us that: “We can all think of areas where we currently have industry and where the instinctive reaction is to say, ‘we need to keep it in being’, in perpetuity perhaps, but we have to test those against some criteria. The first is, are they absolutely critical to national security. The answer for nuclear is self-evidently, yes ... Secondly, is it imperative for defence capability, in other words are we going to need to have these skills in the longer term to support the front line ... are we going to need to upgrade them through life and respond to urgent operational requirements during operations. Then there are the wider technical benefits for the nation, do we need these skills for wealth creation, and then there will be area employment issues.”

We consider it critically important that the MoD develops clear criteria for deciding which sectors of the defence industry it is vital to retain in the future. Issues such as security of supply, in particular to meet urgent operational requirements, should not be underestimated in making such decisions. Much equipment being procured today will be in service for the next 20–30 years or more and will need to be upgraded and maintained. The imperative of retaining the skills within the UK to undertake such work must be recognised. This applies across the range of equipment: from the highest level to the most basic of military requirements.

## IMPLEMENTING THE DEFENCE INDUSTRIAL POLICY THROUGH THE PROCUREMENT PROCESS

A common concern relayed to us was that the wider factors to be taken into account in acquisition decisions (which are set out in the Defence Industrial Policy) tended to be considered only at a very late stage in the procurement process. Sir Richard Evans, for example, told us that the Policy is “a good start but it is absolutely not going to make progress until people implement it through the procurement process and, right now, there is insufficient evidence to say whether or not that is being done effectively across the board”.

Lord Bach acknowledged that this was a legitimate concern, and told us: “I think there has been a tendency for it to be considered at a late stage. I think on occasions it is the sort of thing that has been left, as it were, to ministers to consider when the advice comes up to them from officials. I think that is changing ... I do not think it should just be left to ministers at the end to consider these wider issues. I think they should be part and parcel of procurement processes from the start.”

We are concerned that the wider factors to be taken into account in procurement decisions are still often being considered at a late stage in the process. We expect the Defence Procurement Agency (DPA) to ensure that additional guidance or training is provided to its staff to address this issue.

In our 2003 report on defence procurement, we referred to the Advanced Jet Trainer Programme and the “unsolicited offer from BAE

Systems to supply its Hawk 128 for that programme”. At the time, we understood that the MoD was expected to decide whether to select the Hawk 128 or open up the programme to international competition. We considered the Hawk case to be an early test for the Defence Industrial Policy, not just in terms of taking account of the long-term prospects for competition, but also in terms of managing risk, because the aircraft chosen for the Advanced Jet Trainer programme was then likely to be subsumed in the Military Flying Training System PFI programme.

The MoD announced on 30 July 2003 that it was to purchase 20 Hawk 128 aircraft with options to buy up to another 24. The MoD’s news release announcing the decision noted that the MoD had originally explored the possibility of a PFI arrangement with BAE Systems, but the terms proposed by the company did not offer value for money for the taxpayer.

Lord Bach told us that, in terms of specific examples of where the Defence Industrial Policy has had an effect on a procurement decision, “the one I would say it has certainly had an effect on was the Hawk decision”. Sir Richard Evans also referred to the decision to procure Hawk trainer aircraft, and told us “if this policy is going to be effective, we really should not be having situations where Secretaries of State are issuing ministerial directives to their departments in order to turn over recommendations that have been made”. Sir Richard told us that the recommendation from the DPA to the minister was to acquire the Aermacchi aircraft rather than the Hawk, and that in coming to that recommendation there was “absolutely no account taken of that additional value to the UK”. He said that since the decision was taken, the Indian Government had placed an order for 66 Hawks which, had the decision gone against BAE Systems, would not have been placed. He said he could “genuinely see us actually being able to sell 400 to 500 aircraft”.

Sir Peter Spencer would not comment on the detailed advice to ministers, but said that the suggestion that the advice from the DPA to ministers was to opt for the Italian Aermacchi bid was factually incorrect. He considered the episode to have been a good example of the Defence Industrial Policy working “because if you read the Defence Industrial Policy it says: ‘We will address these issues upfront before we invite competitive tenders’”.

We believe that the decision by the Secretary of States to procure the Hawk trainer aircraft was a sensible one, which has resulted in substantial exports for the UK. Possible exports should always be a factor which is taken into consideration in making procurement decisions, and which should be considered at an early point in the procurement process.

## CONSOLIDATION IN THE UK DEFENCE INDUSTRY

The Defence Industrial Policy states that: “The UK defence industry embraces all defence suppliers that create value, employment, technology or intellectual assets in the UK. This includes both UK and foreign-owned companies.”

Restructuring of the defence industry brings increasing commercial opportunities for UK companies, and economic and technological benefits through inward investment into the UK. The UK industry cannot grow by meeting domestic requirements alone, nor can all the technologies required by the Armed Forces be sourced from the UK. We will not constrain UK companies from expanding into new markets, except where national security clearly requires otherwise.

Sir Richard Evans told us that “although there has been a huge amount of consolidation that has taken place already, it is not going to stop where it is”. He considered that the US was likely to be the main predator and that if the process continued “the UK is simply going to become the American metal basher”. However, Sir Peter did not think this was likely to happen.



## RECENT CONSOLIDATION IN THE UK DEFENCE INDUSTRY

At the time of our inquiry there were a number of proposed take-overs and reported take-overs of UK defence companies. These included an offer from General Dynamics of the United States for Alvis; an offer from Finmeccanica of Italy for GKN Westland; and reports that BAE Systems was considering selling its marine division.

Nick Prest, Chairman and Chief Executive of Alvis, pointed out that defence was now an international industry, and noted that Alvis had bought businesses in Sweden and in South Africa. He referred to the offer from General Dynamics for Alvis and told us that the reason why these developments were taking place was because companies believed that a bigger international spread in their business would give them access to a wider range of markets, and would enable them to draw on a wider range of sources of research and technology. In the event, BAE Systems made a counter-bid for Alvis, and it was reported that General Dynamics had declined to revise or extend its offer.

We asked Lord Bach about the offer from Finmeccanica for GKN Westland – the UK’s only defence helicopter manufacturer. He told us that “these are private companies which are entitled, on the face of it, to engage in what transactions they wish to, subject to regulations and subject, of course, to our being satisfied over a number of very important issues, including security of supply”. He added that “it really is time that we left behind the concept that what actually matters in the end is where the ownership of companies actually resides from one day to another, from one month to another. What matters is where the work is done; where the work is produced; where the technology is; and where the value is in the broadest sense”. He added that (in relation to GKN Westland) “we will want to talk over matters which relate to much more than just security, but also relate to jobs, work that is promised for the future and what their intentions are ... we have to accept that it is a global defence market”.

We asked Sir Richard Evans about the reports that BAE Systems’ naval shipyards might be acquired by a French company. He told us that there had been no discussion of any consequence about selling the naval shipyards to the French, and the French had not made any offers to buy the shipyards. However, he added that, if a proposal was put to BAE Systems and “we can see a way of more efficiently securing a long-term interest of this business, we will follow it”.

**The next guidance will focus on ownership of companies, open markets and access to technology, and relations between the MoD and industry.**