

# DFID's use of contractors: call for evidence

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**Contact:**

Sinéad Magill: Regional Director International Development EMEA

[Sinead.magill@thepalladiumgroup.com](mailto:Sinead.magill@thepalladiumgroup.com)

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## About Palladium

Palladium is a leading international development services provider. With offices in 30 countries, our 2,000 staff are currently delivering sustainable developmental impact in 90 countries worldwide.

Our DFID portfolio includes over 30 contracts in more than 20 countries. Through our DFID programmes, we employ 115 full time UK based staff in addition to 580 programme staff. Of our programme staff, fewer than 10% are international advisers, the remainder being recipient country nationals.

We are proud of the impact and value we deliver on behalf of the UK tax payer. Our programmes empower the marginalised, support the economic independence and health of the poor, and help national governments play an active stewardship role in natural resource management. All of our programmes under implementation are rated A or above by DFID in their annual review process, demonstrating the consistent quality and integrity of our work.

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## Summary

- Palladium is a specialist international development service provider. With offices in 30 countries, our 2,000 staff are delivering sustainable impact in 90 countries worldwide. We are one of DFID's leading providers and an active participant in their Key Supplier Management (KSM) programme.
  - Delivering sustainable development impact is immensely challenging and often requires a bespoke partnership involving development actors with specialist skills; the 'right mix' is dependent on the specific objective pursued.
  - For each programme, DFID selects the best mechanism for impact delivery based on a robust value for money assessment. In most cases, the service provider is selected through open procurement, entailing a transparent and highly competitive process which assesses the value of service providers; including the private sector, NGOs, small and medium sized firms (SMEs) and local contractors.
  - For-profit private sector providers are often selected to deliver programmes even where NGOs competed for the work. This is because DFID is required to select the best value provider to give the best outcome for the tax payer.
  - Most competitive procurements, particularly for large contracts, result in a partnership between development organisations. Whilst the programme may be led by a large private sector provider, they commonly work in partnership with, or channel funds through, other agencies.
  - Appointing a private sector service provider offers the UK taxpayer the following advantages:
    - Access to specialist technical expertise and experience not available elsewhere.
    - Ability to operate in very challenging security environments where others are unable to mobilise cost effectively.
    - Access to capital to finance programmes removing the requirement for government pre-financing.
  - Most importantly, as DFID contracts are issued on the basis of payment by results, service providers hold the risk of non-delivery and bear full responsibility for any cost overrun. We see this contractual reality as the single biggest demonstration of our commitment to providing the best development outcomes with the best value for money.
  - The UK is a world leader in development. We should celebrate the fact that some of the best development companies in the world are based in the UK.
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# 1. What are the comparative costs and advantages of DFID using large contractors, as opposed to managing programmes itself, via NGOs and other community-based organisations, or through multilateral partners?

1.1 Prior to commissioning any programme, DFID conducts a robust value for money assessment of the procurement mechanisms available to them. This includes an assessment of DFID's capacity to deliver, as well as the potential use of multilaterals, private sector organisations or NGOs, and direct implementation through community based organisations.

- **Multilateral organisations:** the cost and value delivered by multilateral agencies were assessed in detail by ICAI in 2015. Mark Lowcock, DFID's Permanent Secretary, informed the International Development Select Committee (IDC) that multilaterals are less focussed on the poorest countries than DFID's bilateral aid programme. Whilst multilaterals may be well placed to deliver impact on issue-based agendas, they are not well placed to deliver aid to the poorest or to deliver aid to the most difficult fragile and conflict-affected states (FCAS) – both of which are pivotal to DFID's aid strategy. Moreover, their internal bureaucracies and mandates are not well suited to the adaptive and responsive programming that DFID requires, prevent rapid mobilisation and do not prioritise the UK national interest.
- **In-house implementation by DFID personnel:** DFID's ability to deliver programming in-house has been reduced by administrative budget cuts which have limited the number of personnel available. These cuts are also increasingly restricting the number deployed to oversee programmes in-country. An analysis by leading private sector providers of the number of team members provided to DFID in 2015/16 has enabled estimates to be made of how many additional staff DFID would need to hire to facilitate in house implementation. In addition to its existing staff of 3,500, DFID would have to recruit a further 25,000 to 30,000 personnel, many of which would not be required when policy priorities change following changes in Government or development priorities worldwide.
- **NGOs:** Many NGOs, particularly large international NGOs, offer in-house technical expertise and specialist support on a par with private sector providers and as such they provide a credible alternative. However, when DFID puts programmes out to tender, private sector providers are frequently deemed to offer greater value to DFID and awarded the contract. Private sector providers can offer cost efficiency savings; but also, as they are not issues-based (as with many NGOs) they are often better able to respond and adapt to DFID's programmatic requirements.
- **Community based organisations:** Programme implementation by community based organisations can represent high risk for DFID. Whilst there may be initial cost savings, implementing programmes through community based organisations carries high fiduciary risk and most of these organisations would require substantial capacity building to deliver the quality required. This approach would also demand a significant increase in DFID staff numbers.

1.2 Generating meaningful and sustainable impact is not about setting one agency or delivery modality against the other; it's often about selecting the best blend and building partnerships between delivery organisations. Most competitive procurements, particularly for large contracts,

result in a partnership between these actors. Whilst the programme may be led by a private sector provider, they often work in partnership with, and channel funds through, other agencies. For example, the lead contractor will work in partnership with local firms and actors who provide specialist services and have detailed in-country expertise, and will allocate funding directly to beneficiary organisations through grants.

1.3 Partnerships of this kind recognise the specialist expertise, capability and cost advantages each organisation offers and it is this that drives value for the UK tax payer.

**Example 1:** The Maternal, Newborn and Child Health programme (MNCH2) is a large health investment in DFID's portfolio and an example of how a diverse and nuanced consortium can provide the right mix for sustainable and value for money impact. As lead contractor, Palladium partners with six international and local private and NGO organisations. This consortium is mobilised in the conflict-affected and highly challenging environment of Northern Nigeria. The consortium works with and strengthens local health systems and community based organisations to prevent maternal and childhood deaths. During the first two years, 1.36 million women have accessed potentially life-saving antenatal services through the programme.

**Example 2:** Through our Enabling Sustainable Health Equity for Family Planning programme in Kenya (ESHE), Palladium are working with an international NGO, the Kenyan Ministry of Health, religious leaders and community members to address barriers to the use of contraception and promote child spacing. Nuria, one of the Islamic teachers says:

*"There is a major improvement in how members of the community perceive child spacing. This is a joint effort from our religious leaders, female madrasa teachers and Ministry of Health; and thanks to ESHE for bringing us together."* Through ESHE's dedicated work, there are 100,000 more users of family planning services in rural counties.

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## 2. Could these costs be reduced and, if so, how?

2.1 Reducing costs and maximizing the value of DFID's private sector partners has been a significant focus of the Department over the past five years.

- DFID's KSM programme includes an assessment of the value for money provided by the key suppliers across DFID's portfolio of programmes.
- As programme size has increased, so too has the intensity of competition. Price has become a key driver of the outcome of the procurement process. This has resulted in downward pressure on fee rates, overheads and profit levels; driving further efficiency within firms.
- Contracts are predominantly based on payment by results. This means that contractors share the risk of non-delivery and bear responsibility for cost over-run.
- During tender processes, suppliers are now required to provide full disclosure of all costs contained within each bid. This includes an "open book" policy on fee rates paid to individuals, overheads and profit levels. Analysis of the profitability of DFID's service

providers (recently completed by DFID) shows that DFID's competitive procurement procedure is driving better value, with private sector suppliers being assessed as receiving very modest profits.

- As DFID's understanding of the market has improved, the Department is increasingly working with private sector providers, NGOs, SMEs and community groups to understand the cost base of their programmes and to encourage partnerships between groups that recognise the comparative cost advantage each grouping provides. It is these partnerships which drive best value for DFID.

**Example 3:** Private contractors, like NGOs are committed to reinvestment in development. At Palladium we are committed to reinvesting in development. Our *Let's Make it Possible* impact fund channels 1.5% of profit into innovative new ideas and technologies with the potential for real impact on the communities in which we work. We also proactively support thought-leadership and better programming by allocating staff time to policy debates in development.

2.2 There are two areas where DFID could support further cost reduction:

- **Pre-funding of grant funds:** Many DFID programmes contain significant grant funds which the lead partner allocates directly to local community based organisations, NGOs or private entities. It is not uncommon for grant funds to exceed £10 million. DFID normally requires private sector service providers to pre-fund these grants. If DFID followed the practice of other donors – by funding grant funds in advance– this would reduce the working capital burden on suppliers, reduce costs and open the market further to SMEs who are unable to meet the pre-funding requirement. On a £10 million grant, this could represent a saving of £150,000.
  - **Tax exemptions on ODA spending:** We take great care to ensure that we comply with taxation, social security and regulatory requirements both in the UK and in beneficiary countries. Taxation represents a significant cost element of our fee rates. Should DFID choose to obtain tax exemptions for ODA spending, as other donors do, savings on fee rates in some countries could be as high as 30%.
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### 3. How does DFID decide when and where to use contractors?

3.1 In DFID's IDC submission on DFID's use of resources, they outline how resource allocation decisions are made. Specifically, through the Business Case Model, DFID appraises delivery options according to their capability and capacity, costs and benefits, risks and likelihood of success and concludes with a preferred option. All business cases are available on DevTracker.

3.2 All programmes tendered by DFID are open to NGOs, SMEs and local consultancy companies, as well as private sector service providers. Where an organisation is selected to implement a programme, it is the result of a highly competitive procurement process that assesses which provider represents best value for money. In many cases, this is a private sector provider.

3.3 For most programmes of significant size, the selected private service provider works in partnership with local consulting organisations, NGOs and community based organisations. It is the combination of these resources that represents best value to DFID and the UK tax payer.

3.4 In addition to the direct technical inputs provided by the private sector, the lead firm plays a critical role in driving value for the UK tax payer. Specifically, lead contractors:

- Engage with and build the capacity of local implementing agencies and firms, thereby ensuring the sustainability of developmental impact.

**Example 4:** In Pakistan, through the Empowerment, Voice and Accountability for Better Health and Nutrition programme (EVA), Palladium provided capacity building and guidance to the Centre for Communication Programmes, a local consortium partner. The Centre's Executive Director, Atif Ikram Butt, attests to the transformative effect our support has had:

*"Palladium's experience of managing large programmes has been invaluable to Centre and has helped us meet internationally accepted operational standards. We believe this partnership speaks volumes for Palladium in terms of their commitment to strengthening a local organisation's capacity, to make them capable of independently delivering development solutions."*

- Provide rapid access to specialist expertise which DFID cannot retain in-house cost effectively.

**Example 5:** At Palladium we have established networks of experts and local partners through whom we can rapidly deliver quality solutions. Our global health team provides the three largest international donors (DFID, USAID and DFAT) with world-class specialist skills in a number of areas; including policy and health systems governance, universal access to healthcare and child health and development.

- Pre-finance DFID's programmes and assume DFID's delivery risk, thereby facilitating inputs from SMEs and local contractors who are unable to access the necessary funds or take on these risks. On many of our programmes, up to 100% of our fees are dependent on the delivery of pre-determined development outputs and outcomes.
- Provide DFID with a cost effective mechanism for deploying personnel to FCAS. The IDC enquiry into DFID's work in FCAS shows that the costs of deploying contractors are

up to 50% lower than deploying DFID personnel. Moreover, our security regimes enable us to access regions which DFID personnel are often unable to visit, such as parts of Khyber Pakhtunkhwa in Pakistan.

- Provide continuity on DFID programmes. Whilst it is common for DFID personnel to move posts every two to three years, our personnel are commonly engaged on programmes lasting for five years and longer from inception to completion.

**Example 6:** For eight years our State Accountability and Voice Initiative (SAVI) in Nigeria has maintained the same leadership team and is independently assessed to have achieved strong results including a 1.8 billion Naira increase in the health budget in the Yobe State House of Assembly. Continuity over long periods is an essential part of effective development.

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#### 4. To what extent is DFID finding the right balance between the use of contractors and the development of in-house skills to meet changing needs?

4.1 As stated in para 1.1 above, DFID is a commissioning agency. It does not have the in-house capacity to deliver on its objectives without the support of external organisations. Partnership is anyway required to deliver effective development programmes.

4.2 For partnership to be successful, DFID staff must retain both the capacity and the ability to oversee the delivery of these programmes and to work in partnership with their supply base across a range of technical and operational issues.

**Example 7:** The Human Development Innovation Fund (HDIF) identifies innovations which are new to Tanzania and can be adopted and scaled up to have tangible impact in health, education and sanitation. By its very nature, the programme takes risks to achieve human impact. DFID programme officers have worked very closely with Palladium to shape the programme and adapt to the changing needs of the environment. The programme has moved from a B rating to A+ in two years – evidencing effective adaptive management and partnership.

4.3 DFID has invested considerable time and effort to improve its partnership with delivery partners; including through better commissioning, oversight and evaluation of programmes, and particularly through the introduction of the SMART rules and capacity building of in-house personnel to facilitate intelligent risk taking and oversee adaptive programming. As outlined below, this bodes well for the management of the DFID budget, its programme portfolio, and programme delivery. We observe a strengthening in our engagements with DFID as a result.

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5. How effective are DFID's procurement, contract management, risk management and programme management processes in achieving value for money and effective long-term development? How could these processes be improved?

5.1 DFID has invested considerable time and effort in improving its systems for procurement, contract management, risk management and programme management in the last two years. They are committed to a programme of continuous improvement which we support.

- **Procurement systems** have become more guided and transparent and DFID demonstrate a greater understanding of their delivery partners and the market. There has been a significant increase in the quality of submissions required by the procurement process; both in terms of technical approach and explicit demonstration of value for money. The contract negotiation process has also changed radically, becoming much more rigorous.
- **Risk management:** DFID has in recent years encouraged service providers to strengthen their focus on risk management and duty of care. This is a welcome development. However, whilst DFID concentrates on security and political risk, the same focus is not applied to programmatic risk. This can reduce service providers' ability to manage risk as DFID does not always provide all available information that could affect programming. Additionally, despite the existence of the Cabinet Office-owned Management of Risk route map for risk reduction, DFID's country offices do not use a common risk management methodology. This makes it difficult for service providers to implement uniform risk management across programmes.
- **Programme and contract management:** DFID's management of the technical and operational delivery of its programme portfolio has improved considerably; specifically with the introduction of the new logframe, greater use of theories of change, revised processes and formats for annual reviews, the introduction of the contractor performance review framework and the use of SMART rules. Programmes are managed more adaptively than before, with improved efficiency in delivery. Successful programmes are acknowledged, and less-successful programmes are subject to amendment or termination.

5.2 We have been working in partnership with DFID for over 15 years and believe that the past five years represent a real change in DFID's capacity to deliver effective aid and commitment to continuous improvement. DFID are widely recognised to be one of the most effective and progressive aid agencies and we are delighted to work in partnership with them.