

DFID's Use of Contractors

Evidence to the International Development Select Committee from Adam Smith International

1. Introduction

1.0.0 Adam Smith International is a company owned by all its employees that helps the poorest people in the most fragile areas of the world by developing good governance and strong economies. For avoidance of doubt, Adam Smith International has no affiliation with the Adam Smith Institute. We have conducted a range of projects for DFID, other donor organisations and governments. We are pleased to submit this evidence to assist the Committee with its inquiry.

2 Comparative costs and advantages of DFID using contractors

2.0 Cost advantages

2.0.1 There is misplaced, inaccurate and recurrent criticism regarding the 'high' costs of contracted specialists financed by the UK's Department for International Development (DFID). An adviser day-rate is often compared with civil servant and multilateral staff salaries, which is grossly inaccurate. Contracting is actually significantly cheaper.

2.0.2 A new study (see "Comparative Analysis: DFID Contractor Costs") reveals that the cost of using contractors is substantially less than the cost of deploying DFID staff, and much lower than multilateral staff. It shows that using DFID staff would cost 50% more and multilaterals can cost over 200% more. The paper also demonstrates that the cost of contracting companies is similar to that of non-governmental organisations (NGO).

2.0.3 Moreover, cost comparisons do not take into account the extensive risk that is transferred from DFID to contractors, which cannot easily be financially quantified.

2.1 Value for money and clear results

2.1.1 Contractors deliver high value for money and are an important, leading tool for DFID to achieve transformative, sustainable change. The facts starkly contradict those who say aid "doesn't work." For example:

2.1.2 In Afghanistan, Adam Smith International has helped increase tax revenues from US\$200 million to US\$2 billion. This year we helped Sierras Leone's National Revenue Authority collect £55 million of tax arrears in just two months. This is reducing aid dependency.

2.1.3 The Nigeria Infrastructure Advisory Facility (NIAF) has worked with Nigerian state and federal government agencies to secure cost savings of £691 million on capital investment in public-private partnerships by removing non-commercial costs.

2.1.4 The International Development Committee (IDC) has highlighted the significance of enabling Nepal in finally unlocking its hydropower potential. The first four major hydropower projects will deliver £11.3 billion and end Nepal's electricity shortage, while creating 20,000 construction jobs.

2.1.5 The Somalia Stability Fund, which we manage, has helped re-establish governance structures in districts newly-recovered from Al Shaabab in south-central Somalia and has facilitated the creation of three democratic states.

2.1.6 In Syria, our award-winning Tamkeen project is performing ground-breaking work by rebuilding municipal governance, whilst delivering public services. As a result, 13 local councils are now delivering basic services to a high standard of participation, transparency and accountability. Over 1.6 million Syrians are benefiting from improved access to water, electricity, education and health services, including 329,000 internally displaced persons.

See Annex 1 for beneficiary testimonies from a variety of programmes.

2.2 Contracting: DFID's most precise, and accountable instrument

2.2.1. Contracting is the most precise instrument available to DFID. Unlike most aid modalities, using contractors allows DFID to direct and oversee the design and implementation of each project and ensure targeted impact. Contracting also requires the largest commitment of DFID's own staff resources of any aid instrument. DFID staff are involved at every stage, from the concept, business case, choosing the right implementing organisation, supervising implementation and/or changing the focus of the programme in-line with changing socio-political circumstances.

2.2.2 DFID staff lead in areas where they add most value and are recognised as holding world class expertise – in policy work, in programme design, in the evaluation of technical impact and in government to government consultation and negotiation.

2.2.3 The transfer by DFID of financial resources to other organisations, for example the World Bank or United Nations (UN), which design and implement their own programmes, requires much less resources. The provision of grants to NGOs requires more DFID supervision, but much less than with contracts, where DFID is in full control.

2.2.4 Contracting is at the centre of DFID's efforts to tackle long-standing development problems by crafting country-specific interventions to achieve long-term and permanent transformative impact. It is central to DFID's ability to carry out its mandate successfully.

2.2.5 However, contracting is not always successful. It has to be managed effectively. Like other aid modalities, interventions are not always successful and quantifying impact can take time. Socio-political contexts can rapidly change, so each programme must be flexible and adaptable. This is where contractors can add value: they can quickly adapt, change teams and mobilise experts at short-notice.

2.3 DFID's ecosystem of contractors

2.3.1 DFID has built an ecosystem of contractors that enables it to implement a wide range of sophisticated interventions. This ecosystem has evolved over several decades to augment and extend the capabilities of DFID, and it works well because it is both competitive and complementary: not all of the various service providers can fulfil the same roles, but collectively they offer different strengths across numerous disciplines. Such diverse expertise is a strategic asset that helps to keep DFID a leader in global development.

2.3.2 Contracting is a competitive process, open to many different organisations and an effective means of driving innovation, attracting the best talent to address the tasks required, and achieving value for money. The number of organisations competing to help DFID deliver impact is large and diverse. In recent years, DFID has succeeded in widening the pool of organisations, including non-governmental organisations, universities, think tanks, for-profit firms and UK government agencies.

2.3.3 Contractors are a critical part of DFID's capacity, without actually being formally part of DFID. They are effectively a key implementing arm of DFID. Many of the individual contracted advisers have been working in development, often on DFID programmes, for decades. They are a valuable resource for DFID because of their extensive knowledge and experience. Adam Smith International spends about £250,000 per annum providing pro-bono knowledge transfer services to DFID across all programmes. Our knowledge and experience is shared with DFID permanent staff.

2.3.4 For example, Adam Smith International has been active in Afghanistan since 2002. We have conducted a wide range of projects and built a strong operational platform, forming good relationships with a wide range of leading figures. In contrast to DFID permanent staff who are rarely in Afghanistan for more than a couple of years, many of our staff have been in Afghanistan since 2002-4. They have in-depth knowledge of the country and how to successfully achieve change. This is an important resource for DFID and the FCO.

2.4 Is it feasible or wise for DFID itself to manage and implement programmes instead of contractors?

2.4.1 DFID has always been a commissioning organisation rather than an implementing one. DFID itself to manage and implement programmes would not only cost more, but it is not feasible or realistic for it to retain in-house on a permanent basis the extremely wide range of technical skills that is needed by programmes that can be delivered by external technical experts. Most interventions involve specialist skills of a particular nature that are only required for a certain length of time. Those skills are required on a project-by-project basis, not permanently. Were DFID to develop a permanent cadre of staff to handle its current implementation needs, it would quickly find that the cadre was not matched to changing requirements.

2.4.2 Moreover, if DFID were to be responsible for implementation, its programmes could no longer be carried out in many priority countries, as duty of care rules applying to civil servants would prohibit this. Many conflict-affected areas are largely inaccessible to DFID staff given the restrictive security protocol imposed on serving officials.

2.4.3 Contractors, by contrast, can implement DFID programmes in the most difficult and dangerous places in the world. This significantly extends DFID's reach in many of its key target countries. The risks are high and over the last few years, several contractor staff have been killed and injured.

2.4.4 Then there is the issue of competition. Transferring implementation responsibility to a single monopoly supplier would mean less innovation, collaboration, partnerships, lead to a reduction in skill diversity and likely complacency.

2.4.5 Lastly, an analysis of the number of team members provided to DFID in 2015 by seven companies has enabled estimates to be made of the numbers of additional permanent staff who would need to be hired by DFID if it were to take over the implementation role. In addition to its existing staff complement of some 3,500, another 25,000 to 30,000 personnel would need to be recruited.

2.5 Managing programmes via NGOs and other community-based organisations as an alternative

2.5.1 Contracting is a status-neutral modality – the best organisation for the job is hired, regardless of whether they are an NGO, a private company, or a university for example. NGOs and community-based organisations do win and implement contracts for DFID. Some NGOs have a large portfolio of DFID contracts. However, the decision as to which organisation should be chosen in a competitive tender should clearly be made on the basis of merit, rather than on subjective preference for one organisational form over another. The organisation which puts forward the best proposal that offers the greatest value for money should be chosen.

2.5.2 Where an NGO or community-based organisation has the deepest experience and can put forward the best team in a proposal offering the best value for money, clearly should be chosen to carry out the work.

2.5.3 It is also worth noting that the proposals DFID receives to undertake complex programmes are, more often than not, submitted by consortia. These consortia often include a mix of larger firms, niche players and international and local NGOs. The market response to DFID's tender is driven by a competitive process that sees DFID's ecosystem of providers being flexed to ensure the best possible mix of service providers – whether private, public, NGO, international or local.

2.5.4 In the wider world it is usually private companies who provide specialist professional services, rather than NGOs, although this is not a universal rule. The beneficiaries of contracted technical assistance have a clear preference for receiving the best quality professional services. This is natural and correct. It is the same in our personal lives. When we hire a professional we want to receive a good service of a high quality. We would never put up with second-best or third-rate.

2.5.5 The alternative of using grants to NGOs across the board instead of contracts is not a good one. Contracts involve much higher levels of accountability and DFID control with contractors held accountable for the delivery of tangible results. Monitoring and evaluation are built into contractual arrangements, thus activities and results are transparent.

2.5.6 However, it is important to note that solutions that combine modalities work well. Many contractors work closely and partner with grant-funded NGOs to deliver the best solution. In South Sudan, our customs reform work on the border with Uganda enables UN trucks carrying food aid to access the country over 90% quicker. This shows how systematic change can benefit humanitarian aid. Differing modalities do not have to be exclusive.

2.6 “Large contractors” versus small contractors/SMEs

2.6.1 It is incorrect to assume that the market for DFID's contracted services is dominated by a handful of large companies. The DFID market for contracted services is more competitive than that of other bilateral donors:

- In Australia only three firms held 69% of contracts by value in late 2015 and the top 10 firms manage around 93% of the Australian Department of Foreign Affairs and Trade's (DFAT) work;
- In Canada, following a series of mergers and acquisitions, the bulk of tenders are won by only two firms;
- In the United States of America, over 50% of tenders by value in 2015 were won by five firms;
- In Germany, the market is dominated by just three firms.

2.6.2 By contrast, DFID's top five firms have a 35% market share, the top 10 have 48% and the top 20 60%. Concentration is lower in practice, however, because these figures do not take into account

that large quantity of funds that are passed on by leading contractors to others, largely NGOs, in their role as fund managers. For example, the Girl's Education Fund alone involves £300m of funds being distributed to others. Moreover, new organisations are constantly entering the market and the make-up of the list of the top 20 changes significantly over time. These are all signs of a very healthy competitive market.

2.6.3 Adam Smith International is not a 'large contractor,' it is a small-medium sized enterprise (SME). There are other SMEs in the list of DFID's top 11 contractors. We have been successful in working for DFID primarily because we provide a high quality service, have delivered good results and are able to resource, deploy and manage teams effectively. Organisations that are less successful should get better at these things if they want undertake more work for DFID. It is vitally important to preserve the principle of contracts being awarded on the bases of competition and merit, if the delivery of results is to remain a primary focus of DFID's programme.

2.7 Could costs of contracted services be reduced and, if so, how?

2.7.1 Any supposition that the costs of contracted services are high is incorrect. They are much lower than the costs of using DFID or multilateral staff. Costs of contracted services in the DFID market are also much lower than equivalent services retained by other UK government departments. Moreover, if it costs less to deploy a professional specialist to a dangerous and difficult developing country than it does to hire a plumber in central London, one can tell that costs are not high.

2.7.2 The costs of contracted services are determined by the market through a strong competitive process that is influenced by the design of tender evaluation criteria. In recent years, DFID has been increasing the percentage of marks allocated to cost in tender evaluations. This has a downward pressure on fee rates as bidders seek to win by putting in cheaper, less experienced team members. The effect on value for money of such an approach is negative. As one adviser recently commented:

"DFID Rates: There is a group of consultants out there that have high technical competence and extensive experience, working in complex and insecure environments to deliver real value for money. Low rates are driving these consultants out of development and deterring competent new entrants. This is not value for money."

2.7.3 There are ways of reducing contractor costs however, by cutting the costs incurred by contractors and by making it less burdensome for smaller organisations to compete. These include:

Simplification of the contracting process: Commercial proposals have become very complex. At a recent DFID workshop, smaller organisations pointed out that about half the time of preparing a proposal was now devoted to the commercial proposal whereas it used to be 10%. Larger organisations have had to build up specialist commercial departments to handle DFID commercial matters. Smaller ones can't afford these. Much of the complication appears to have resulted from official nervousness about negative media commentary. Simplification would make it easier for smaller organisations, and cut the costs of contracting.

More reliable payment terms: Small firms need to be paid quickly. Their cashflow cannot stand delayed payments. DFID used to pay reliably on a monthly basis for inputs delivered. It has now in most cases switched to paying for 'milestones,' such as reports, seminars and other activities. The timing of these payments is much less certain, making it significantly more difficult for smaller organisations to cash-flow larger projects.

Fewer burdensome requirements: DFID's new standard terms and conditions are more than twice as long as the previous set and contain many more obligations, for example relating to data posting and insurance. There is a trade-off between imposing requirements on contractors and the desire to keep costs low.

3. How does DFID decide when and where to use contractors? The balance between the use of contractors and the development of in-house skills to meet changing needs.

3.0.1 An important issue is the overall quantity of the DFID budget spent through contracting. At 11% this is much smaller than the proportion spent by other major bilateral donors, such as USAID who spends 16% on contractors and DFAT who spends 22%.

3.0.2 By contrast, DFID spends a higher percentage (63%), and a higher total volume of funds on multilateral organisations than any other country. Given the greater control, more transformative results that are achieved through DFID's contracting programme, it would be good policy to expand it

3.0.3 Regarding the issue of whether DFID has enough in-house skills, those we have consulted in DFID think the balance is about right, although areas where further strengthening might be needed are financial management and risk management. DFID does have the in-house technical expertise to design and oversee effective programmes. DFID resources are stretched, particularly given the amount that is now diverted to dealing with increased external scrutiny. The smart rules are helping; less time is spent on unnecessary paperwork and there is greater clarity as to what can and cannot be done, but more action is still needed to speed up processes and reduce bureaucratic barriers to delivery.

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

4.0.1 DFID's various procurement approaches have been a key, and deliberate, driver to ensure that its contractors are encouraged to invest in particular areas of capability and expertise. These procurement approaches and the evaluation mechanisms that underpin them actively encourage firms to retain, and further develop particular areas of expertise in undertaking innovative work to refine technical approaches to particular development challenges.

4.0.2 Less effective bilateral and multilateral donors often follow less rigorous, perverse approaches – appointing contractors with limited relevant technical expertise to implement programmes. This is not the case with DFID. Its approach has been both highly effective and economical, particularly given that the drive to develop expertise and innovative approaches has been conducted at the cost of the firms, and not DFID.

4.0.3 However, as noted above, we believe that excessive complexity has been added to DFID contracting approaches in recent years, to the detriment of VfM. In addition to simplification, the most important area that DFID should concentrate on is developing stronger partnerships and closer involvement in its contracted programmes. This is already good in most cases, but not universal.

Annex 1: Testimonies from beneficiaries of projects implemented by Adam Smith International

“The world-class expertise provided by DFID through its Centre for Inclusive Growth programme has been absolutely invaluable in helping us to achieve these ground-breaking deals, which are likely to transform Nepal’s prospects.”

**Radhesh Pant, Chief Executive Officer, Nepal Investment Board
(referring to 4 hydropower projects)**

The Growth and Empowerment in States Employment 3 project introduced the Systematic Land Titling and Registration Concept to Jigawa in 2013. It invested a lot of energy and effort to ensure that the goals of the work were understood and carried the Ministry along throughout.

We now look at the efficiency of long standing practices and improve them whilst also developing stronger co-ordination and relationships with partner MDAs such as Agriculture. GEMS3 ensured that other MDAs gained a deeper appreciation of the difficult and complex nature of land matters and helped the Governor create models that released land to investors in ways that accommodated the needs of the rural communities more fairly while facilitating release of land to the investor. The processes developed in collaboration with GEMS3 will be used for future land releases to generate investment and the SLTR work will also be scaled up to all LGAs in accordance with the processes created by GEMS3."

Abdullahi Hassan, Surveyor General, Ministry of lands, housing, urban development and regional planning, Nigeria

We are seeing substantial improvements in education as a result of the DFID funded Punjab Education Sector Programme 2, implemented by Adam Smith International and McKinsey and Co. We are making schooling more accessible and meaningful by improving our schools, teachers and textbooks, and strengthening management, monitoring and assessment. The team on the ground has introduced several innovations for holistic education sector reform. As a result, we are annually increasing enrolment across the province, especially among marginalized communities, and our students are staying longer in school, and as a result of this are learning more.

**Punjab Education Sector Programme II, Statement from HE Rana Mashhood Ahmed Khan,
Minister for Education, Government of Punjab**

DFID, through the SUGAR programme, and with technical support of the Basel Institute has given invaluable assistance to the Financial Intelligence Authority, Uganda (FIA). FIAs institutional capacity has been enhanced through regular training sessions held at the FIA premises in Kampala and occasionally through electronic platforms. Great assistance was also rendered in providing input in draft legislation in the AML/CFT area to assist Uganda in making the reforms required by FATF. Further assistance was concentrated on assisting with development of the FIAs own internal operational policies given that the FIA is a very young institution. Presently, we are receiving support in the conduct of the AML/CFT National Risk Assessment.

The difference is already evident. The quality of our analysis of suspicious transaction reports has improved. FIA is better equipped to coordinate the ongoing AML/CFT National Risk Assessment. FATF has given its stamp of approval on the laws that have recently been amended to meet international standards.

Sydney Asubo, Executive Director of the Ugandan Financial Intelligence Authority

On behalf of Bakol regional administration, I would like to convey my highest appreciation to the Somalia Stability Fund (SSF) upon the tireless support towards the livelihood improvement of the Bakol vulnerable and besieged community, and particularly those communities of Xudur and Wajid. Our administration highly registers the SSF devotion of funding support in the context of stabilization programs implemented through Danwadaag + and NIS Foundation both in Xudur and Wajid districts. We fully acknowledge without your sincere intervention of supporting such significant stabilization projects, our communities would have remained more vulnerable as they were in a desperate need of such stabilization programs which gave them a new hope of prosperous life.

We wish to extend the commitment of the SSF's continuous support that has made a very tangible positive impact in promoting both peace, stability and development in the area, thus encouraging other development partners to join these concerted efforts.

Our administration hopes that SSF will continue and extend its support to the remaining liberated districts of the region.

Mohamed Abdi Mohamed (Toll), Governor Regional Administration

Annex 2: Descriptions of daily activity from individual advisers

For better appreciation of the actual life and practical difficulties experienced by individual advisers on project teams, we supply here descriptions of their daily activity by two of our team members in the field:

"I was so excited when I got a job offer with Adam Smith International, because I love working in Kenya's remote arid regions. This was a perfect opportunity because the project covers the most disadvantaged.

I monitor projects to make sure the money is spent correctly. A typical field monitoring visit would take about a week. If you are thinking that this is a fun drive, enjoying the scenery then you are misinformed. There is no road. It is a daring journey - 320 kilometres through the Chalbi Desert. We start at 6am. Unless you have a local driver, you will get lost, there are no tracks in the desert. This journey takes about seven hours, nonstop.

And the temperature is usually above 40 degrees. Dehydration is a real threat and carrying water and emergency medicine is part of my routine checklist. It is a long, sweaty, dusty and tiring journey. The school is about 30 kilometers from the Kenya-Ethiopia boarder. There is insecurity and communities live in fear of attacks from Oromo Liberation Force rebels. Sometimes I have to travel after dark because I find myself in a small village with no hotel rooms.

You must be wondering why on earth we have to visit such remote, insecure places. Actually, not many organisations dare make this a routine; monitoring projects in over 500 schools. But this is Adam Smith International where monitoring, ensuring accountability and quality of the work is highly regarded.

Sometimes I spend more than a month doing remote monitoring and, travelling from one county to another. Imagine coming back to the office after such a long trip and the Team Leader informs you at around 11am that the Governor from Samburu County has just called and he will be opening one of the dormitories we have constructed in his county. I am forced to rush home to pick my luggage, as does the Team Leader. We have to leave as soon as possible to cover the six hour drive to Maralal ...and it is the rainy season as well. You see, close working relationship with the Governors ensures sustainable project interventions.

But why do I do it? It is satisfying seeing a young Samburu girl excited about the newly constructed dormitory being opened by the Governor and as she concludes her thank you speech, she declares her ambition of being the first woman Governor.”

**Peter Galgalo, Field Officer.
Kenya Essential Education Programme**

“I am used to living in dangerous places. But nothing prepares you for Kismayo. I only have salt water to wash in. It stings your eyes. I sleep in one quarter of a 40 foot container near the airport. An armed guard is permanently located outside my compound and my room is physically locked at night – there is zero manoeuvre for escape, or freedom. I am in my late 70s, have worked in hostile areas such as Benghazi, yet I have never experienced an environment so eerie; a deadly silence with occasional gunfire.

Political instability and bloody conflict has plagued southern-central Somalia for more than two decades. With the emergence of violent extremism from rival militia groups, hope for any kind of legitimate governance institution was slim.

I feel like a prisoner – trapped in a compound unless accompanied by an armoured vehicle. I’m not talking about land cruisers, this is a serious vehicle with a rotating weapon on the top. This is an area so sensitive and dangerous that I can only be here for up to three days at a time. Shabaab is still here; you just don’t know who they are.

I am working with the Somalia Stability Fund. I am here to help the Interim Jubba Administration (IJA) rebuild infrastructure, create regulation and accountability. Shabaab used to make good money from this port: charcoal was their lifeline. I am helping to ensure the money is now used to protect civilians and provide public services.

With the Administration we have implemented a new public financial management system to enable transparent and accountable revenue collections. Within just four months, the IJA’s Ministry of Finance was able to commence financial operations in line with international standards. In 2015 they raised revenue of around US\$3million through taxes, duties and fees. This money is being spent inside Kismayo, to rebuild security and on public service”.

**Alan Pearson,
Public Financial Management Specialist**
