

Making savings from contract management



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Summary

The pressing need to find savings means many councils are exploring new ways of commissioning and delivering services. Councils need effective contract management to ensure they maximise both the opportunities and the potential savings these bring.

- The 2010 Spending Review cut government funding for councils by 33 per cent to 2014/15. The 2013 Spending Round cuts will result in cumulative cuts of 43 per cent by 2015/16. Councils urgently seek savings from all areas of the business.
- As councils enter more third-party arrangements to find savings, good contract management becomes increasingly important. It is about more than ensuring suppliers meet their contractual obligations. It can help councils to identify and manage their own and their suppliers' risks, and achieve savings and continuous improvement throughout the life of the contract.
- There are many examples of different arrangements put in place by councils to manage their contracts with suppliers effectively. This report has captured and detailed a number of these to help the sector draw on this learning.
- Elected members have a crucial role to play in setting the strategic direction for commissioning, procurement and contract management. They can ensure their council supports all three functions to obtain the wider community benefits they seek from their spending on third-party organisations.

There is a diverse and growing market for council services. In 2011/12, councils spent nearly £30 billion on contracts with third-party organisations. This brings risks, as well as opportunities.

- In 2011/12, local authorities spent £56.6 billion on buying goods and services, of which over half – £29.2 billion – was on payments to third parties. Most (76 per cent) of this amount went to private and third sector organisation.
- Councils spend different amounts on third parties, depending on the services involved and their approach to service delivery. Social care accounts for most third-party payments, and education the least.
- Councils deal with many suppliers – on average, a district council has just under 200 suppliers and a county council nearly 1,300. But overall, councils spend over 90 per cent of their third-party payments on no more than 20 per cent of their suppliers. The biggest savings will come from managing these contracts effectively.

- Third-party arrangements bring risks, as well as opportunities. If these risks are not managed corporately, they can bring about supplier insolvency, service failure, or fraud; all with reputational and financial damage to councils.

A corporate approach improves internal and external collaboration that in turn, helps councils to improve contract management.

- A corporate approach does not have to mean all contract management is centralised. Sheffield Council has developed the Intelligent Client approach, which allocates responsibilities for managing contracts to the centre or to service managers, depending on the risks involved.
- Other councils in our research had different, but still corporate, approaches. Essex County Council is bringing all contract managers into one department, dealing with procurement, category management, and supplier and contract management. District councils tend to use cross-departmental groups to coordinate and plan procurement and contract management.
- Collaboration across councils and with suppliers can bring significant benefits. Increasing transparency about costs, prices and benefits in collaborative arrangements serves to improve benchmarking across councils.

Potential savings and other benefits result from robust performance management, good data, and incentives for contractors to be flexible. Change is inevitable, and in the current fiscal climate, councils will need contractors to share the pain, as well as gains.

- At a basic level, good contract management is about attention to detail. It means understanding what the contract contains, who has responsibility for managing it, and whether performance and costs are on track. The best results are achieved when those who are involved in procurement and running the service work together to manage the contract and have clear agreed processes and procedures in place to help them do so.
- Renegotiating contract terms comes about because of changing business or service user needs, better technology, market developments and legislative changes. But also – simply – because councils need to save as they have less money to spend.
- Good relationships with contractors based on trust will help when councils seek to renegotiate terms and conditions. Councils can find this difficult, but they will find incentives such as profit share, and better data using spend analytics, can help them prepare well for negotiations.
- In a time of austerity, contractors may be more willing to consider sharing the pain of reduced funding, post-award. Timing is important; if the contract doesn't have review or renewal clauses, contractors have less incentive to renegotiate.

The high volume and value of third party contracts suggests councils have scope to achieve savings and other benefits from contract management. This requires investment to obtain returns.

- In our research, councils obtained savings of between 3 and 15 per cent on the value of the contracts over their duration, after the award.

- While this is not necessarily replicable across all councils, it shows that councils of different size and type, and facing different circumstances, have the potential to save money from contract management.
 - As well as direct savings from reducing the scale and scope of the contract, councils can achieve other financial benefits, including cashable and non-cashable efficiencies, avoiding unnecessary costs, enforcing penalty clauses and sharing additional income from growth.
 - Sheffield City Council's comprehensive benefits tracker system shows the financial and other benefits contract management brings. It also allows it to calculate a savings per contract manager team member of eleven times their average salary.
- technical skills such as negotiation strategies and contract law, it can foster commercial acumen and other attributes among staff who are more likely to be commissioners than providers.
- Above all, better contract management skills will make councils more confident that they can release value from their contracts and place them on an equal footing with suppliers

Ensuring people with the right skills are in place to carry out contract management is essential to release more value from contracts.

- Managing contracts well requires specialist skills, including understanding costs and value, negotiating, and procurement and commissioning processes. Some councils have recruited staff with relevant experience, while others have successfully used consultants to manage or renegotiate contracts.
- Training in contract management is increasingly common. Sheffield City Council and Essex County Council have developed comprehensive training courses. In Sheffield's case, these support a toolkit for central and service managers. Sheffield has shared this with several councils.
- Training in contract management is vital in order to prepare councils for third-party arrangements. As well as developing

Recommendations

1. We urge councils to take contract management seriously. Its time has come, because councils spend significant and increasing amounts via contracts with suppliers, often as part of their transformation to meet financial challenges. There will be benefits and savings to be delivered by focusing on contract management.
2. We encourage elected members to consider the example of Birmingham City Council and others in having a lead for commissioning, procurement and contract management. This signals to the whole organisation the importance of contract management in achieving a council's objectives.
3. Based on this research, and our own work to develop the National Procurement Strategy, the LGA recommends that councils draw on the learning from these case studies and follow the principles of good contract management outlined in Appendix 1. These are to:
 - provide corporate support for contract management;
 - aim to get continuous improvement in contractors' performance;
 - invest in developing commercial skills;
 - collaborate to maximise gains;
 - monitor and benchmark costs and performance.
4. We recommend councils should approach the case study councils in this research to learn from their experience. The LGA will work with the sector to promote this learning to enable councils use this to support their own work to better manage contracts. Their stories show that councils can release value from existing contracts.

Introduction

The pressing need to find savings means many councils are exploring new ways of commissioning and delivering services. Councils need effective contract management to ensure they maximise the opportunities these bring.

The government's deficit reduction plan involves significant cuts in public spending. The 2010 Spending Review set out plans to reduce government funding for councils by 33 per cent from 2011/12 to 2014/15 (Ref. 1). Analysis by the Local Government Association (LGA) shows that the 2013 Spending Round will result in council funding provided through the Department for Communities and Local Government's budget being reduced further, the cumulative figure being 43 per cent by 2015/16 (Ref. 2). In response, councils urgently need to find savings from all areas of business.

This includes getting more savings and other benefits from effective management of contracts. As a proportion of overall spending, councils have increased the amount that goes to third-party organisations¹ and extended contracting into new areas. This brings opportunities for councils to do more or better for less. But it also brings risks that councils must manage.

This report aims to help councils do both. It is for council officers and members who have a specific responsibility for commissioning, procuring and managing contracts with third party organisations as well as those who oversee and monitor value for money. It uses case study examples to show how councils have reduced costs and achieved savings from renegotiation. It outlines the benefits contract management brings, as well as those achieved through the initial procurement².

Procurement and contract management

About half of what councils spend is on buying goods and services. This is a great deal of money and they have made significant efforts in recent years to procure well and efficiently, to maximise value for money for local and national taxpayers.

To date, there has been less focus on contract management, but there is – or should be – a close link between the two. Put most simply, contract management enables councils and their suppliers to meet their contractual obligations at an agreed cost and quality. But circumstances change over the life of a contract, so it also involves managing changes and variations in scope, terms and prices.

¹ Councils call these organisations by different names; most commonly, 'contractor', 'provider' and 'supplier'. We use these terms interchangeably.

² It does not address the question of whether contracting out provides better value for money than keeping services in-house. It does not cover procurement for goods. It addresses councils only.

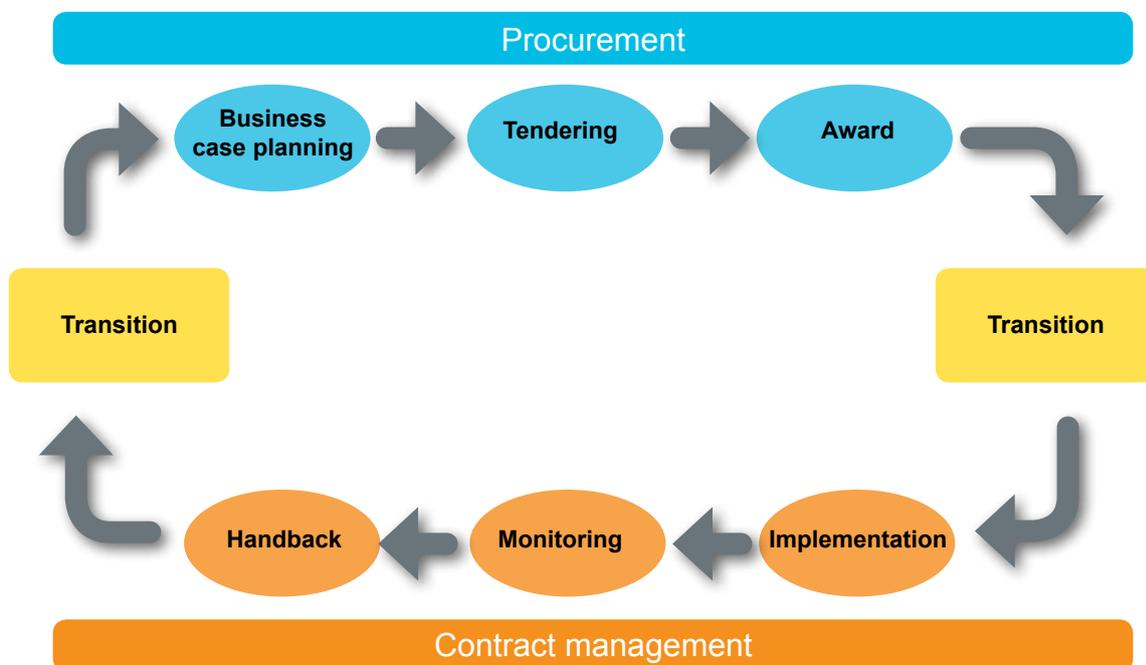
More broadly, it is part of a strategic and holistic approach called supplier relationship management (SRM). Good SRM enables both parties to explore contractual issues that affect the relationship between councils and their suppliers or providers. For example, councils can engage with suppliers to renegotiate and review processes to reconfigure services to take out costs, or to respond more effectively and efficiently to emergencies.

Good contract management is active and dynamic; ensuring councils can manage change and aim for continuous improvement. It helps councils to identify and manage their own and their suppliers' commercial risks, within a collaborative and professional relationship (Ref. 3). In short, good contract management helps councils to maximise savings and service quality.

The most effective councils plan and organise procurement and contract management together, even if they involve different staff. It makes sense to involve all relevant staff from the planning stage, through the contract award, then during the contract period, to the point when the contracts are due to end and retendered or procured. The LGA has published guidance addressing this point, among others.

Foundations are laid during the procurement process including specification and setting of service level agreements and KPIs. Determine approach, roles and responsibilities and involve the contract manager at an early stage. Focus on delivery of benefits. (Ref. 4)

Figure 1: The procurement and contract management cycle



Source: Audit Commission

The key is to think of both procurement and contract management as a cycle, with two transition points, which councils should plan for (Figure 1).

Each of these stages is challenging and requires careful thought and planning. Essex County Council has mapped the main risks and remedial action in the transition from the procurement through to the operational phase in their longer term contracts (Figure 2).

Figure 2: Procurement risks and issues



To maximise the benefits from procurement and contract management together, councils need to provide clear corporate leadership and support for contract managers, whether in the centre or in service departments.

Elected members have a key role to play.

Elected members

Elected members can play an important role in setting the overall strategic direction for commissioning and procurement. Birmingham City Council has created a cabinet member role for Commissioning, Procurement and Contract Management. This reflects the importance the Council attaches to getting maximum value from the £3.5 billion annual spend, of which £1 billion is via contracts with third party suppliers.

Member involvement is key to ensuring that the right goods and services are procured, thus delivering more of their Council's priorities at prices that reduce the needs for cuts elsewhere. Scrutiny has an equal role with the Executive in driving additional value, including Social Value, from contracts, grants and partnerships

Councillor Stewart Stacey, Cabinet Member for Commissioning, Contracting and Improvement Birmingham City Council (Ref. 4)

Principles of good contract management

Based on the research for this project, we have identified five key principles that underpin effective contract management. Appendix 1 contains full details. In brief, they are:

Principle 1: Provide corporate support for contract management. Become an intelligent client, integrating contract management within the commissioning model and ensure clarity of roles and accountabilities.

Principle 2: Aim to get continuous improvement in contractors' performance. Build in incentives that minimise costs and maximise quality, to the mutual benefit of councils and their suppliers.

Principle 3: Invest in developing commercial skills. Recognise that contract management requires specialist commercial skills that may be in short supply within the council and invest in training and external help where necessary.

Principle 4: Collaborate to maximise gains. Extend the benefits from collaborative procurement to the management of contracts, and realise the benefits from greater cross-council collaboration, as well as effective partnership and supplier relationship management.

Principle 5: Monitor and benchmark costs and performance. Use ICT and other systems and processes to produce information about the number and value of contracts, the benefits and costs they generate, and where possible, how this compares with other councils.

This report shows how councils have made progress in these important areas, the barriers they have faced and the benefits they have achieved. It covers:

- the growing market in third-party suppliers (Chapter 1)
- a corporate approach to contract management (Chapter 2)
- continuous improvement in contracts (Chapter 3)
- the benefits contract management brings (Chapter 4)
- the skills needed for contract management (Chapter 5).

The appendices contain the principles of good contract management, information about case study councils' approaches, and the study methodology. There are contact details for each case study council, so that readers can follow up any matter with them directly.

Chapter 1

The growing market in third-party suppliers

There is a diverse and growing market for council services. In 2011/12, councils spent nearly £30 billion on contracts with third-party organisations. This brings risks, as well as opportunities.

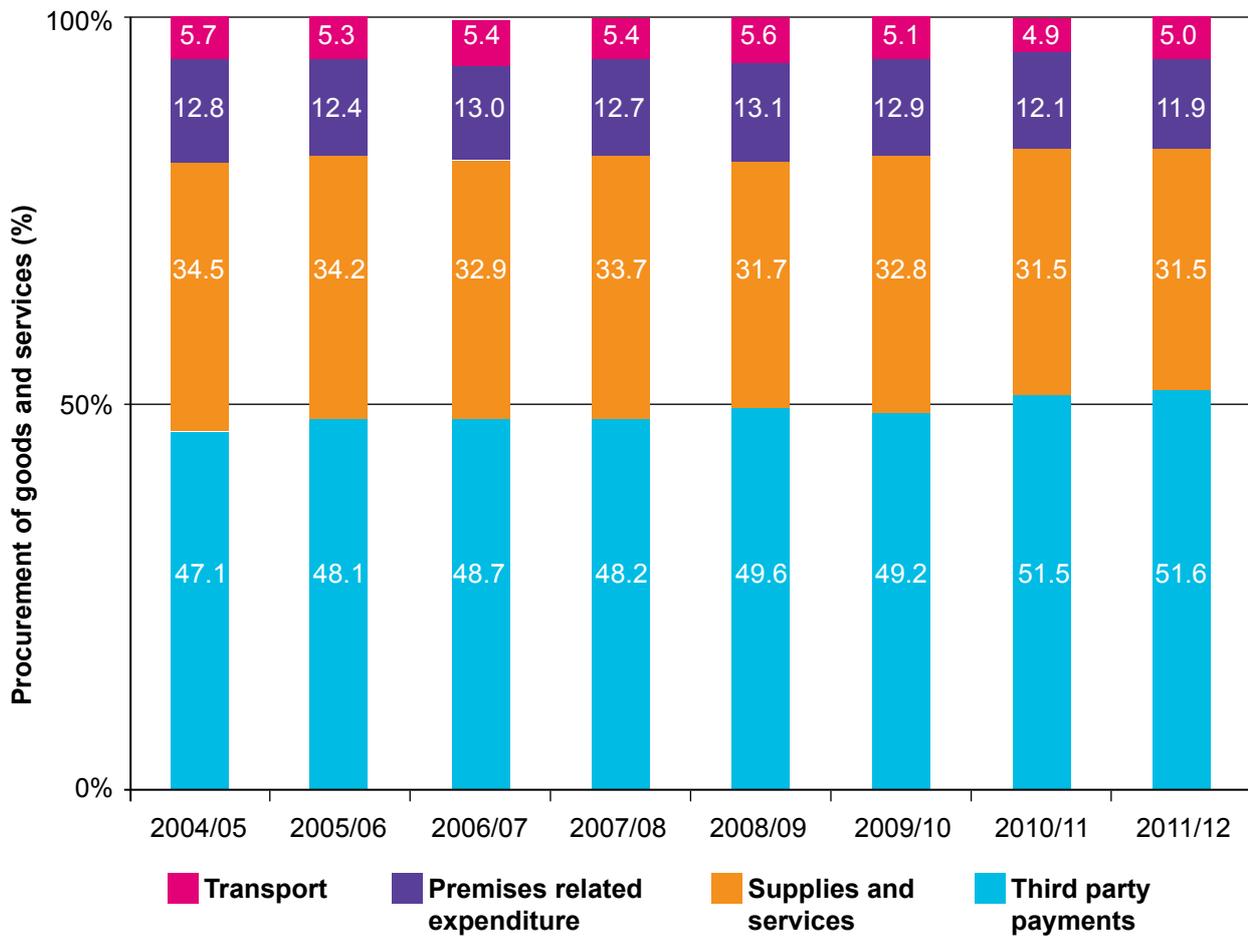
A large and growing part of council spending is on third-party organisations to provide services. In 2011/12:

- local authorities spent £56.6 billion on buying goods and services³, which was nearly half (49 per cent) of all their revenue spending
- over half of this amount (£29.2 billion) was spent on external organisations and internal trading organisations, together called 'third-party' payments
- Most (76 per cent) third-party payments were to private contractors, including voluntary sector organisations providing a contracted service.

Council spending, including on third parties, has fallen since 2009/10, following the 2010 Spending Review. But third-party spend has risen as a percentage of all spending on goods and services. In 2011/12, spending on third parties in real terms accounted for 52 per cent of all procurement, compared with 49 per cent in 2009/10 and 47 per cent in 2004/5 (Figure 2).

³ Spending on goods and services includes premises, transport, supplies and services, internal trading organisations, external contractors and discretionary transfer payments.

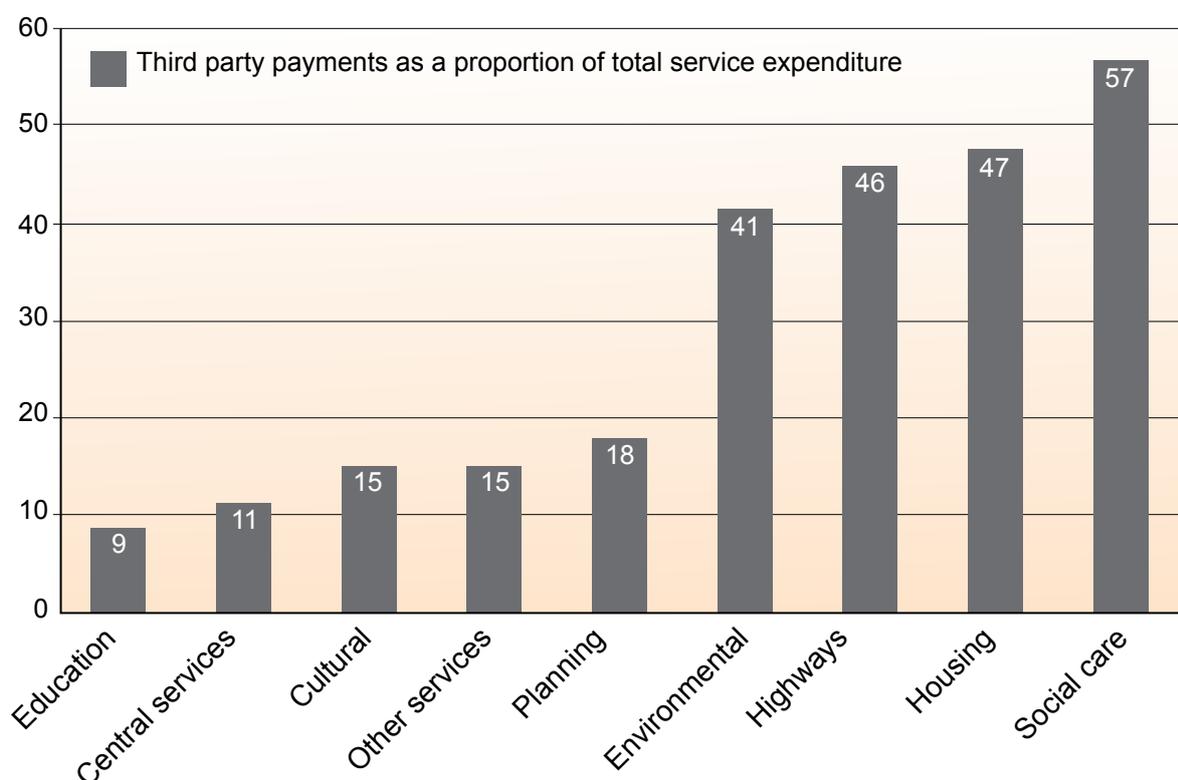
Figure 2: Proportion of local authority spending on goods and services 2004/05 to 2010/11



Source: Local Authority Subjective Analysis Return

Within councils, different services spend varying amounts of their total budgets on third-party suppliers. In 2011/12, social care accounted for the largest proportion (57 per cent) and education the smallest (9 per cent). This variation reflects the different markets in suppliers (Figure 3).

Figure 3: Third party payments by service area



Source: Local Authority Subjective Analysis Return 2011/12

The market for third-party suppliers is large and diverse. The Audit Commission analysed the spending data over £500 per item published by councils between April 2011 and March 2012⁴. In this period, the mean average number of suppliers across the councils in the analysis was 517, but this varied widely across and within each type of council (Table 1)⁵.

Table 1: The numbers of suppliers in each type of council

Council type	Districts	Counties	London Boroughs	Metropolitan Districts	Unitary Authorities	Single Tier and County Councils	All
Mean average number of suppliers	195	1,249	881	897	777	914	517
Minimum	30	617	531	418	211	211	30
Maximum	369	2,119	1,306	2,202	1,461	2,202	2,202

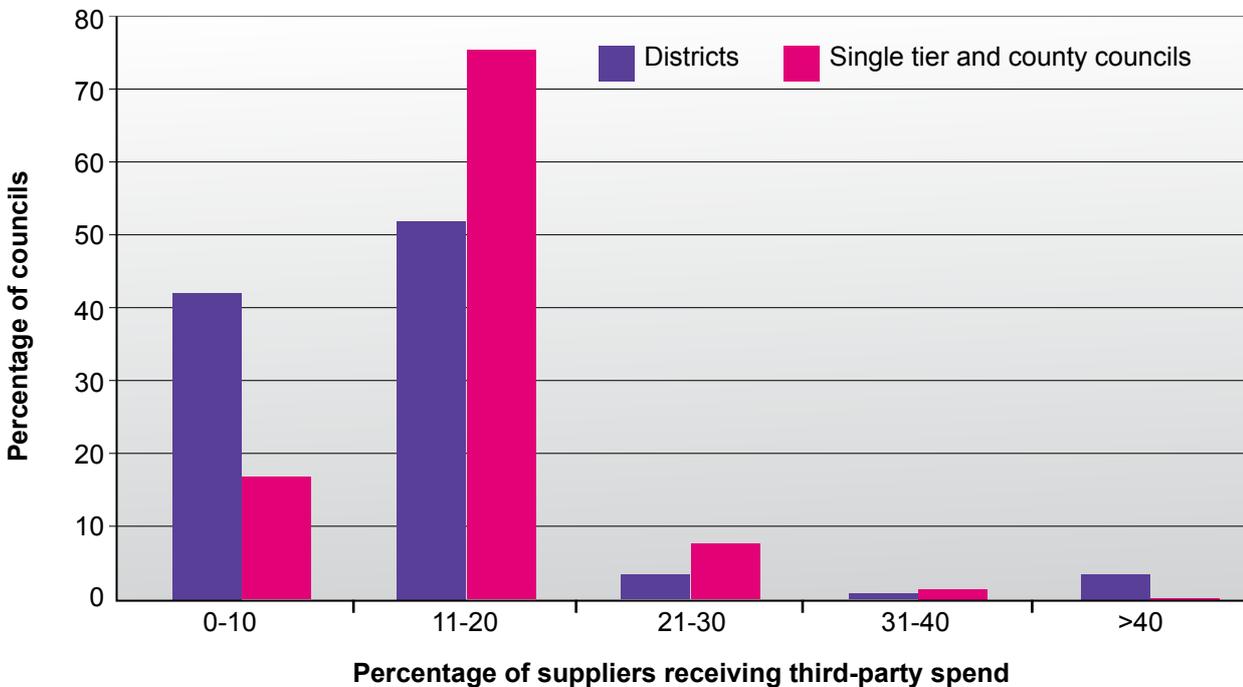
Source: Audit Commission

⁴ In 2011, the Secretary of State for the Department of Communities and Local Government directed councils in England to publish all payment items over £500. This provides a potentially valuable source of data on third-party spend, although the variation in recording practice across councils makes collation and analysis difficult. Appendix 2 gives more detail about these issues.

⁵ This figure excludes redacted and non-third party organisations.

The analysis also suggests that the biggest savings are most likely to come from the largest contracts. Figure 4 shows that councils spend most money (93 per cent) with a relatively small number of suppliers.

Figure 4: Most councils spend over 90 per cent of their third party payments on no more than 20 per cent of their suppliers



Source: Audit Commission

The analysis showed that the 25 firms that received the most third-party spending from councils had contracts worth £6.6 billion (14 per cent of all third-party spending). These large organisations often work with several councils, including one that worked with 317 councils (Table 2).

Table 2: The number of councils contracting with the top 25 suppliers by volume of council spending

Number of councils with which contractors work	Number of top 25 contractors
1-25	2
26-50	5
51-100	9
101-150	4
151-300	4
301- 350	1

Source: Audit Commission

Some of these large suppliers are specialists, for example, in waste management or construction, while others provide multiple services. Most work for all types of council.

This suggests that there is opportunity for councils to take a more strategic and collaborative approach to supplier relationship management (SRM). It is worth exploring within and across councils whether major suppliers could more effectively – and cost-effectively – meet their strategic objectives. This will in many cases include local economic development, through using its procurement spend to invest in local small and medium-sized enterprises (SMEs) in the supply chain. (See section on SRM in Chapter 4).

One 2013 survey found that nearly half (47 per cent) of councils' procurement spend goes to small and medium-sized businesses (Ref. 5). Many social care providers are in this category. Another project in London reported that 29 councils in the capital worked with more than 53,000 suppliers (Ref. 6).

Councils are changing their business models, as they restructure to make large-scale savings. Shared services and outsourcing are more common. Such measures are often associated with transformation programmes, involving large-scale restructuring and reconfiguring of services, staff redundancies and transfer under TUPE regulations.

In a 2012 survey conducted with 34 Chief Financial Officers, over half (54 per cent) reported that financial pressures will lead to greater outsourcing (Ref. 7). In times of upheaval and disruption, it is all the more important that councils retain the capacity to manage the risks involved in third-party arrangements.

Risks

Councils remain legally and democratically responsible for services they outsource and so must manage the associated risks of their outsourced contracts. These include supplier insolvency⁶, service failure, reputational damage, and extra costs (Ref. 8).

Our research suggests that these risks are greater when councils:

- have a fragmented approach to procurement and therefore contract management, with service and other departments following different approaches
- have poor documentation and systems for capturing knowledge, leading to loss of organisational 'memory' when staff leave
- fail to read, understand and monitor contracts.

Contract fraud, known as mandate or change of bank details fraud, is a growing risk in local government. It occurs when fraudsters persuade councils to divert contract payments to their bank account. This is a high-value, high-risk fraud, where just one failure to follow prevention procedures can lead to a big loss. In 2012, the Audit Commission reported that ten local government organisations detected mandate fraud with a total value of more than £4.6 million (Ref. 9).

The councils in this research have been on a journey to manage these risks. Some – like Sheffield City Council and Essex County Council – have developed comprehensive systems and processes. Others are at different stages on the journey. But all have reduced risks and improved benefits as a result of paying corporate attention to contract management. The next chapter shows how a corporate approach to managing contracts helps.

⁶ There have been a number of high profile service failures in local government in recent years. For example, building and social housing repairs firm Rok went into administration in November 2010 just one month after winning a £10 million contract for homes in St Albans City and District Council, and a few months after winning contracts worth £2 million across the North West.

Chapter 2

A corporate approach to contract management

A corporate approach to internal and external collaboration helps councils to improve contract management.

A corporate approach does not necessarily mean centralising all responsibility for contract management. It is possible for councils to treat procurement and commissioning as corporate and strategic functions, leaving contract management to departments. But this requires leadership and clear policies to support a corporate approach. Links between the centre and services can create an effective and proportionate means of monitoring and managing risks, and drive a consistent approach and accountability.

Some service managers resist greater control from the centre, believing that their technical and professional knowledge makes them best equipped to procure and manage contracts. There is truth in this; across services of different types, from safeguarding vulnerable children and adults to large-scale design and build projects, professional, service and technical expertise is vital. But so is specialist contract management skill.

Our fieldwork revealed that councils used different ways of sharing responsibility for contract management. But they all have a corporate overview of the contracts that are important strategically and how to manage them. They establish clear ownership of, and roles and responsibilities for, contract management.

The councils in our research also believed it was important to pay attention to the basics. These include knowing:

- how many contracts the council has
- how much spend is on contract
- when contracts are due for renewal or retendering
- where contract documents are
- who is responsible for monitoring contract compliance
- what terms and conditions contracts contain.

This research confirms the importance of the guidance published by the LGA and Local Partnerships, which contains a number of critical success factors for contract management.

Contract management – critical success factors

- Requirements specified in comprehensive specification with identifiable and measurable outcomes (including service level agreements and key performance indicators).
- Involve the contract manager at the outset of the project.
- Accurate understanding of the service requirement, performance standards and any social value implications.
- Good supplier selection against an effective award criteria.
- Relationship built during procurement process and actively managed.
- Clear roles and responsibilities.
- Good knowledge of the contract.
- A contract management manual that explains key contractual provisions and documents key processes
- A good document management system.
- Identification, allocation and continuous management of risk.
- Focus on realising the benefits identified in the business case (outcomes), which also helps reduce costs.
- Encouragement of continuous improvement.
- Management of performance shortfalls.
- Adequate tools to tackle poor performance.
- Continuity of knowledge throughout the procurement and contract management phases.

Source: LGA/Local Partnerships (Ref. 4)

It is often a failure to answer straight forward questions that leads councils to establish a corporate approach. The 'Intelligent Client' approach is an excellent example of this.

Becoming an intelligent client: the Sheffield approach

Sheffield City Council has over 400 contracts with third party organisations with a total value of £730 million a year; about two-thirds of its annual revenue budget of £1.2 billion.

The council has spent five years developing the Intelligent Client approach, drawing on best practice approaches in the private sector. It ensures the council gets best value from suppliers, prioritises service quality and manages risks.

The model is based on separating the roles and responsibilities of the corporate centre and service managers. The Head of Commercial Services manages a corporate team of 55 staff responsible for all procurement, and managing all high value and/or high risk contracts.

Figure 5 summarises how the council allocates responsibilities, based on the risks assessed.

Figure 5: Sheffield City Council's contract management risk matrix

Cost per year	Greater than £2m			
	Between £25k- £2m			
	Less than £25k			
		Low risk	Medium risk	High risk

- Managed by Commercial Services
- Commercial Services or Council Service
- Council Service

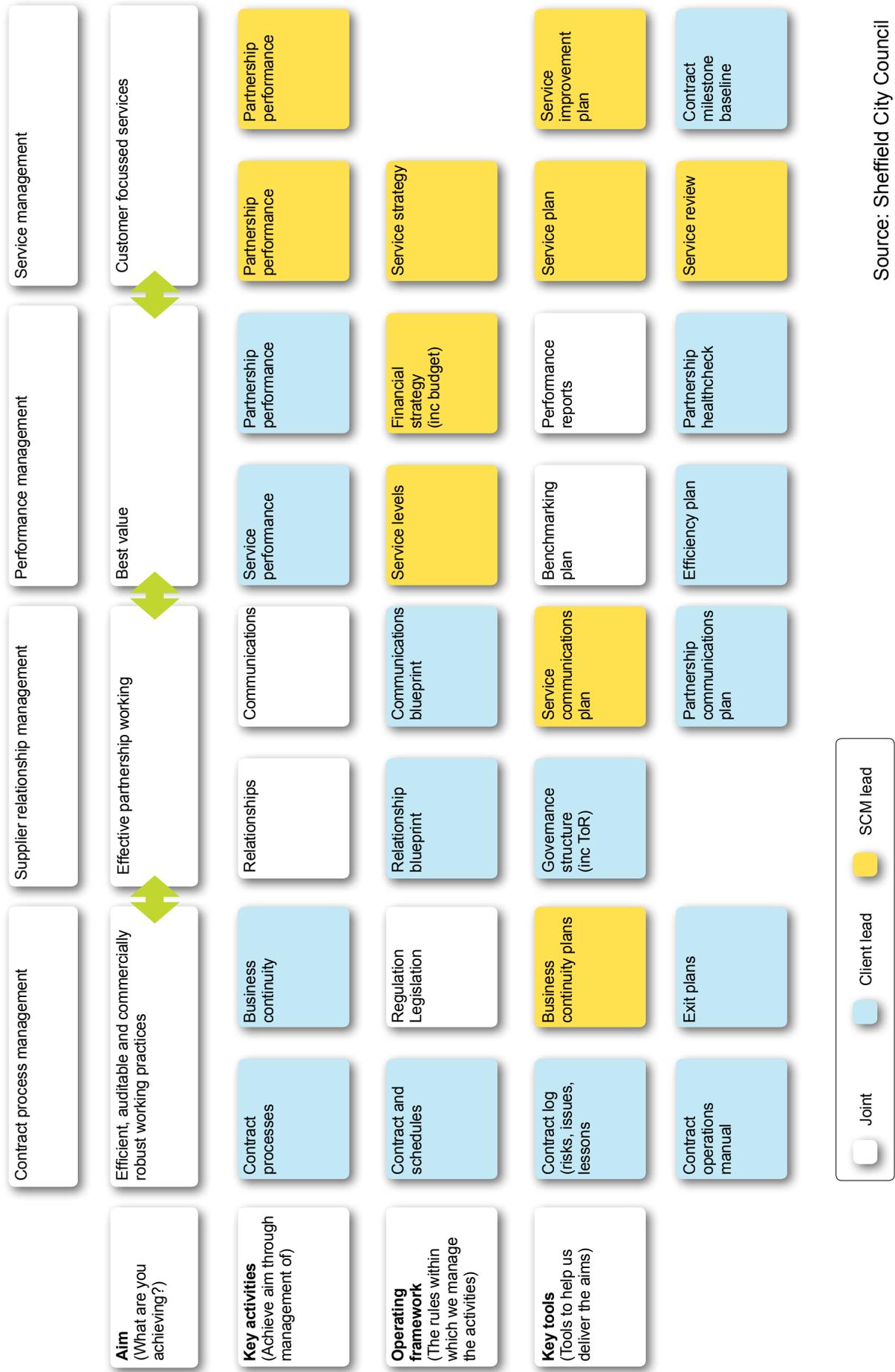
Source: Sheffield City Council

Behind this summary matrix is a spreadsheet with more detailed risk assessments for each contract, including weighted scores for different risks.

The corporate Commercial Services Team (CST) now directly manages a third of all Sheffield's contracts, and provides support and training to service managers who manage the rest. The CST supports service managers through a comprehensive toolkit for managing different types of contract, based on common standards and principles.

The CST provides guidance and support to service clients on using the toolkit. Figure 6 shows the summary matrix of themes, objectives and activities within it, and how responsibility for them rests with the centre, service managers, or with both jointly.

Figure 6: Sheffield City Council's Intelligent Client Approach



Source: Sheffield City Council

While the toolkit and the principles upon which it is based are relevant to all councils, the level of resources and organisation Sheffield has invested may only be possible in larger councils.

Developing a corporate approach: the Essex experience

Essex County Council spends £900 million a year on about 7,500 third party suppliers. This represents 45 per cent of its annual revenue budget. It is restructuring to strengthen its procurement and contract management functions, as part of its transformation programme.

The council currently has 35 corporate procurement staff, of whom seven are supply chain managers, offering support to service departments in procurement and contract management in a loose 'hub and spoke' arrangement. In the new structure, all procurement and contract management will be centralised in a new Commercial function within Strategy, Transformation and Commissioning Support.

Procurement and contract management roles will remain separate in the new structure. This allows appropriate focus to be given to contract management activity and for the development of the required skills in the different roles which may vary dependent on the discipline.

Like Sheffield, supply chain managers become involved in service procurement and contract management based on their assessment of financial and service risks. The assessment allocates every contract the council has into one of five tiers or sub-tiers:

- Tier 1 is for the highest value or highest risk contracts. It has three sub-levels: the highest level is for contracts worth over £10 million per year, but will also include some smaller value contracts that carry reputational or major service risks.
- Tier 2 is for spend levels between £1 million and £10 million per year that are not considered high risk.
- Tier 3 is for the multitude of lower value, low risk contracts.

Commissioning Outcome Groups (COGs) provide a corporate approach for managing against the delivery of outcomes. They aim to break down service silos, encouraging commissioners and service experts from different disciplines and other organisations (if appropriate) to work together, and commercial staff to get involved in the early stages of commissioning.

COGs comprise staff from different functions and at different levels, whose role is to:

- bring together commissioners to join up efforts to deliver outcomes
- act as the mechanism to get the right resources across the authority (and outside) to support decision-making
- take a long term, strategic view as directed by elected Members
- be independent from internal and external operations and take a truly agnostic view
- increasingly work in partnership and make joint investment decisions with partners
- increasingly build up evidence for why the Council should invest in particular outcomes or activities.

Figure 7: COG Summary

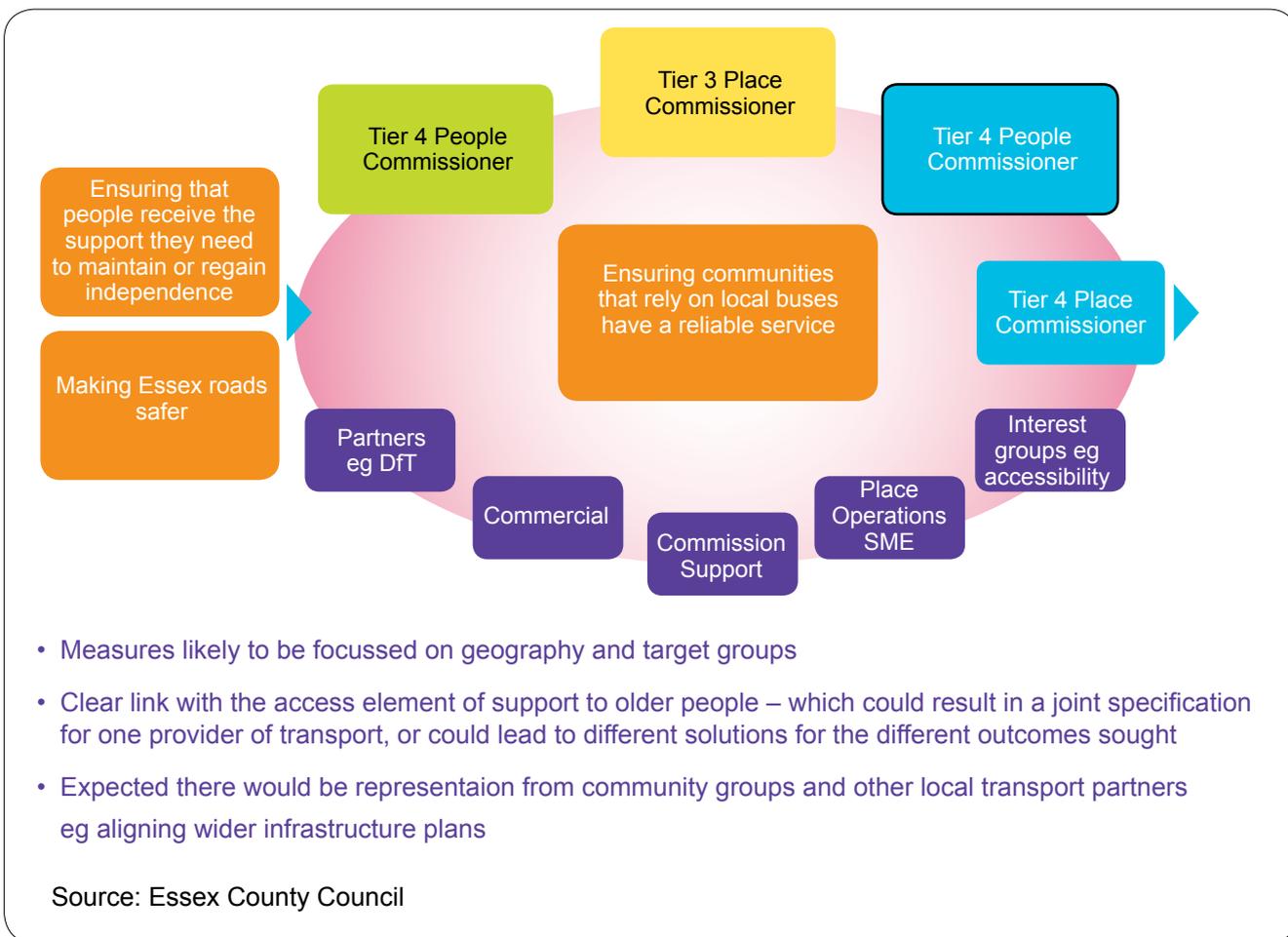
COGs will....	COGs won't
Bring together commissioners to join up our efforts to deliver outcomes	Lose the link to a specific outcome/outcomes for which they are accountable
Act as the mechanism to get the right resources across the authority (and outside) to support decision-making	Make decisions – this is the Member/ Commissioner role, the COG supports them
Take a long term, strategic view as directed by Members	Focus on tactical, short term and reactive activity
Be independent from internal and external operations and take a truly agnostic view	Act independently of each other – we will still be acting as one ECC and not e.g. losing our economies of scale without conscious choice
Increasingly work in partnership and make joint investment decisions with partners	Focus on ECC services only and assume these are always the best delivery option
Increasingly build up our evidence for why we invest in particular outcomes/activities	Replace or override political decision-making

Source: Essex County Council

COGs are about outcomes more than structure. Senior commissioners will be responsible for ensuring outcomes are achieved either in geographic areas or for service users in their disciplines. With help from community groups and stakeholders, they will commission virtual task and finish groups for projects, for example, to address a change in legislation, such as a change of social care funding for older people.

A good example is support for older people. A COG could commission and align transport, infrastructure and social care plans to meet assessed needs.

Figure 8: Essex County Council’s Commissioning Outcome Groups



Essex County Council won a Procurement Leaders Award for its procurement, achieving savings of £150 million to protect front-line services by, among other things, lean business processes.

One phrase in the bid document sums up the importance Essex attaches to effective contract management:

As ECC transforms into a commissioning-led organisation Procurement recognised that the role of contract managers would be critical to future success, as ECC becomes increasingly reliant on the performance of third party suppliers.

It’s different for districts?

District councils are likely to have substantially less resource to manage contracts, although their value may be as large, if not larger, a proportion of their annual budgets compared with other councils. But the principles of an effective corporate approach are the same.

Swale Borough Council spends £8.3 million on contracts with third parties, which is 47 per cent of its annual budget. They have created a network of service heads and assistant directors from across the council who meet every two months to monitor achievement and discuss problems. These meetings alert the centre to performance management issues and contract renewal or retendering dates.

Allerdale Borough Council has recently set up a contract management group. This aims to support contract management in service departments rather than assume direct responsibility. It comprises senior financial, operational and legal staff and replaces the old system where the corporate centre only allocated a relatively junior finance team member to oversee the three main contracts, whose combined value is 43 per cent of its annual budget of £15 million.

Selby District Council has taken a radically different path. It was faced with a funding shortfall of £3 million in its £14 million budget over the five years covered by its medium term financial plan. It realised it would not achieve the level of savings it needed from normal cost-cutting ('top slicing') approaches. In April 2011, it set up an arms-length service delivery vehicle (SDV) called Access Selby (AS).

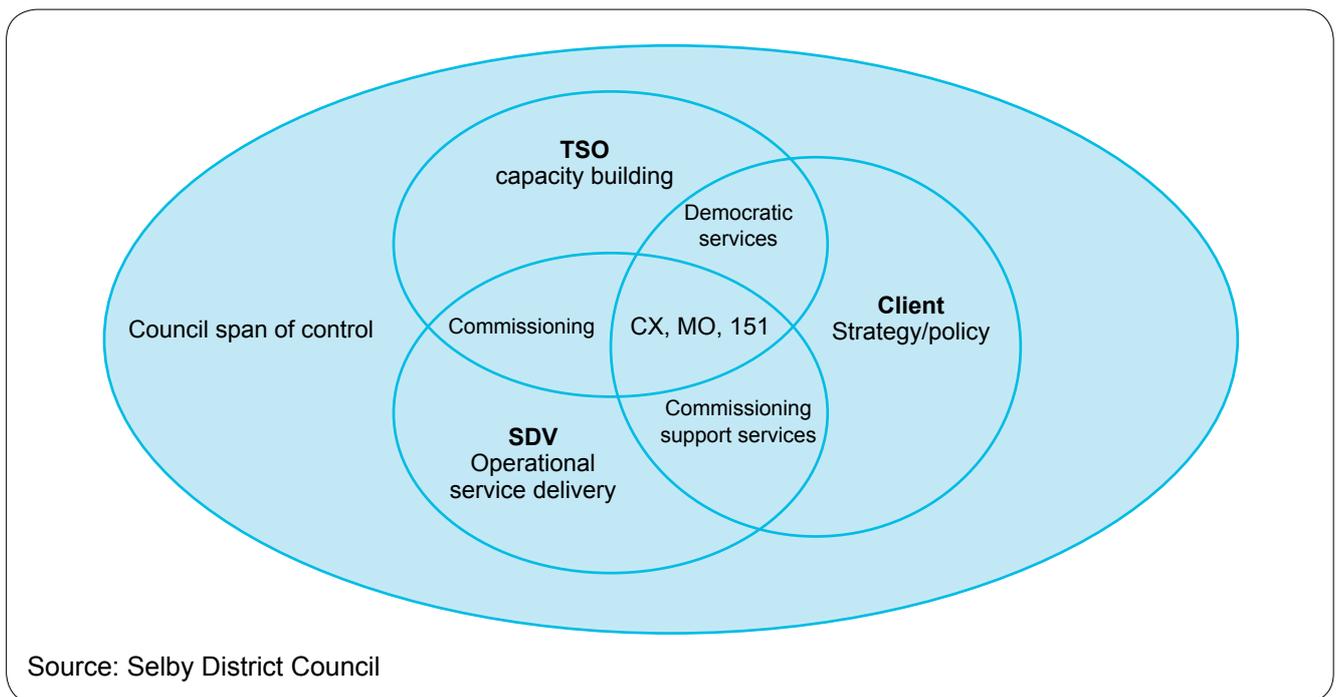
AS delivers all services on contracts for the council, which retains ultimate responsibility for service quality within the arms-length relationship. Over a three-year period covered by a service level agreement, AS works within a fixed cost envelope, which reduces annually in line with the fall in the council's grant income.

The relationship between AS and the council is akin to a partnership contract. The council has in effect delegated its procurement and contract management to AS. The council has accordingly reduced its own contract management function. The delegation to AS makes it clearer to contractors that they will have to meet cost overruns: cost control is, as a result, more effective than before.

Elected members retain the lead role, supported by the council's senior management team, in shaping this

agreement. The council works alongside an umbrella Third Sector Organisation (TSO) based on the local Association of Voluntary Services. The TSO sponsors five Community Engagement Forums, on which the elected members who represent these areas sit. The TSO informs the commissioning of services, set out in a three year service level agreement (SLA) (Figure 8).

Figure 9: Selby District Council Service Delivery Vehicle Model



Access Selby staff are also encouraged to think entrepreneurially, to identify opportunities to generate income as well as ways to reduce costs. They recognise that every pound spent needs to add value to the organisation, reflected in business cases and the language they use.

Collaboration: achieving mutual gains from contract management

Many longer term contracts bear the name of a partnership, in which councils share both risks and rewards with their collaborator (Ref 10 and 11).

Whether badged as a partnership or not, ultimately councils must ensure compliance with contract terms and conditions. They may be content to do so informally for small-scale projects. But high-value and high-risk agreements usually require dedicated governance and risk management, based on independent evidence.

Case study 1 highlights how Solihull Metropolitan Borough Council has developed successful partnerships in property services.

Case study 1

Solihull Metropolitan Borough Council's partnering contract

In 2005, the council entered a partnership with two companies to provide reactive and planned building maintenance and mechanical and electrical services. The key features are:

- a partnering charter that embodies shared values and principles, and a mutual desire to enhance levels of customer satisfaction
- a range of key performance indicators, developed jointly by the Council and the two partner organisations, which focus on a wide range of qualitative and quantitative performance measures and underpin a drive for continuous improvement
- shared IT, including personal digital assistant (PDA) equipment and integrated works orders and payments
- co-location of staff supported by joint training and staff development
- problem resolution, which regards problems as opportunities to learn and improve
- a shared wish to protect public funds.

The new partnership arrangements have delivered some efficiency savings:

- staff reductions of three full-time equivalents, resulting in an annual saving of £113,000
- a fall in the average cost of contract administration, resulting in an annual saving of £185,000
- overheads savings of £139,000 between 2007 and 2012.

Source: Audit Commission

Councils are increasingly making use of joint partnering arrangements with private sector suppliers. These can result in potentially significant operational and financial benefits to participating bodies, and generate additional cash flow to the private sector partner. Solihull has made its maintenance and repairs partnering arrangements available to other councils, Academy schools and other organisations in this way, allowing them to share in the efficiency savings.

Case study 2

Solihull Metropolitan Borough Council: managing contracts on behalf of other councils

Solihull Council Property Services Team has seven years' experience of making savings through a successful partnership arrangement with their partnering contractors. It has extended this model to other public sector organisations and now manages property services on their behalf.

Participating organisations can choose from up to four delivery models for this shared service, based on how much control over service delivery they wish to retain. The highest savings are realised when Solihull Council Property Services Team and partners provides a full range of their services on behalf of the participating organisations.

In April 2013, Solihull Council's Property Services Team signed a three year Service Level Agreement with Nuneaton and Bedworth Borough Council to provide electrical maintenance for their domestic properties.

The partnership enables Nuneaton and Bedworth Borough Council to join an established model that has delivered savings of £1.5 million for Solihull Council over the previous five years. Solihull Council has agreed guaranteed savings come from joint working between Solihull Council and its partnering contractor to reduce the average job costs. In addition, Nuneaton and Bedworth Borough Council have made additional savings through a reduction in back office costs.

The partnership is set to deliver guaranteed fixed savings for Nuneaton and Bedworth Borough Council of 10 per cent in year one, and an additional 5 per cent in years two and three. Total expected cashable savings are £262,626 over the life of the contract. The predicted savings are subject to the baseline on the number of orders raised, at 2459 per year. The council anticipates that it will be possible to drive average job costs down even further over the life of the contract; and any savings will be shared equally between the two councils and the partnering contractor.

Nuneaton and Bedworth Borough Council guaranteed fixed savings:

Baseline Budget/Annum	Year 1 savings	Year 2 savings	Year 3 savings
£606,875	£60,688	£87,997	£113,941

Nuneaton and Bedworth Borough Council average job cost:

	Baseline	Year 1	Year 2	Year 3
Domestic properties Cost per order	£131	£118	£113	£107
Void properties Cost per order	£521	£469	£445	£423

Purchasing consortia also offer opportunities for contract management savings, on top of those achieved from aggregated buying. Case study 3 sets out how a league table comparing the costs and scope of suppliers within a framework has enabled councils to get better value through benchmarking. This in turn has enabled them to influence suppliers to achieve wider priorities.

Case study 3

Continuous improvement and influencing contractors to aim for council priorities

Improvement and Efficiency South East (iESE) has established, through Hampshire County Council, a regional construction framework, which was a founder member of the former National Improvement and Efficiency Partnership for the Built Environment. The aim is to provide efficiencies and greater certainty to client bodies about cost and time predictability through modern collaborative working. iESE's South East and London construction framework has eight contractors, and any public authority in the South East and London can use the arrangement to procure and deliver building works worth more than £1 million.

The iESE management team manages the framework using nationally agreed performance measures, as well as a number of indicators reflecting local and regional requirements. Information about costs, prices and performance across the contractors is collected on behalf of councils using the framework. This produces approximate benchmarking, accepting that not all jobs have the same specification, depending on each council's circumstances. But greater transparency encourages contractors to improve their performance and councils to work together to share information and increase their individual negotiating power.

Collective working also allows councils to influence suppliers, for example, to engage more local small and medium enterprises, use fair payment charters and recruit apprentices. The quantifiable benefits councils have gained across the former NIEP include:

- 85 per cent of subcontractors are SMEs
- 64 per cent of subcontractors are local to the area
- 87 per cent of all construction, demolition and excavation waste no longer goes to landfill.

Source: Audit Commission

Chapter 3

Managing performance and change to get continuous improvement

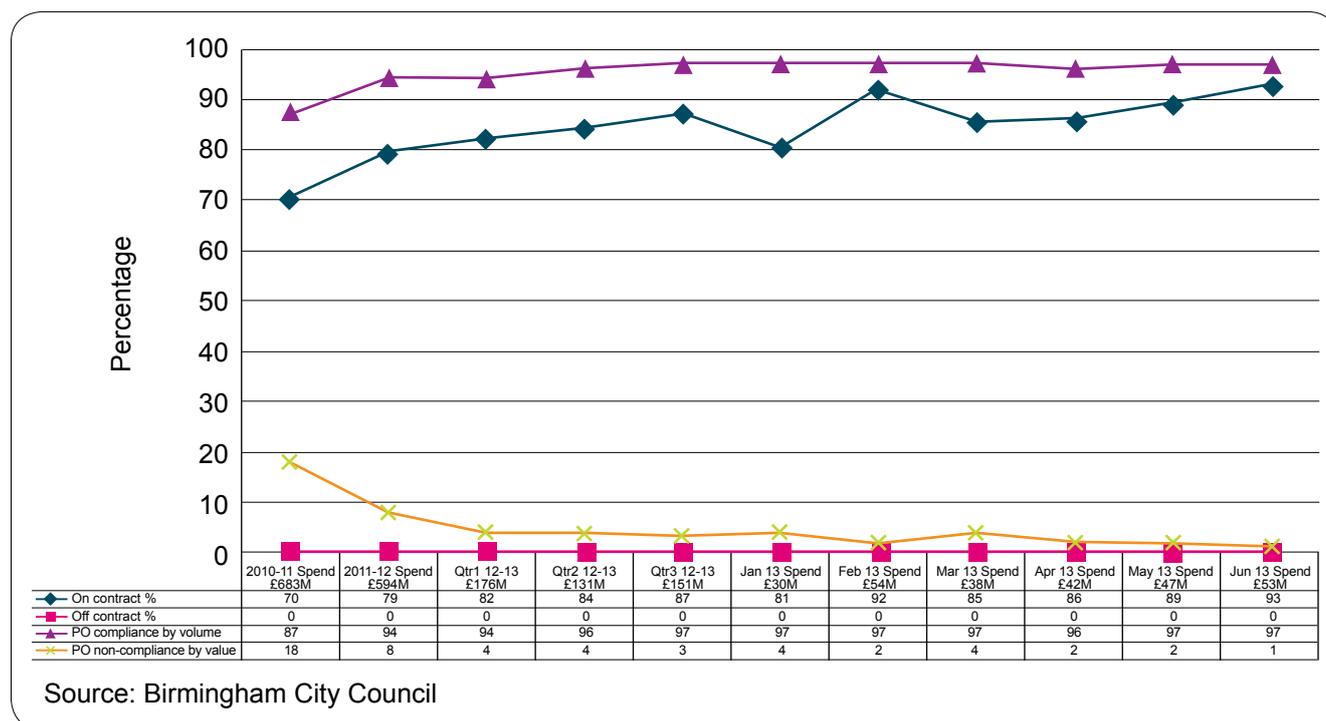
Potential savings and other benefits result from robust performance management, good data, and incentives for contractors to be flexible. In the current fiscal climate, councils will need contractors to share the pain, as well as gains.

Not all third-party spend is on contract (although it should be), but much is. It will involve many different types of contract, according to the type and scale of work and the risks involved. Contracts encompass short-term arrangements, spot purchasing, call-off contracts in time-limited framework agreements, and long-term public finance initiative (PFI) and strategic service delivery partnerships, which can involve joint venture companies and 'bundle' many services.

Managing performance against contract

Our research confirmed the importance of involving skilled contract management staff in procuring and commissioning services. This helps them understand contract detail, so they can spot errors and manage change effectively. Birmingham City Council has a tracking system for showing how much spend is on contract.

Figure 10: Birmingham City Council Spend Compliance tracker 2010-13



Birmingham also finds that staff continuity helps to manage performance and track spending.

Case study 4

Birmingham City Council: staff continuity between contract tender and management

In May 2010, the Council signed a 25 year highways PFI contract worth £2.7 billion. The contract covers 2,500 kilometres of roads, 2000 kilometres of footpaths and 90,000 street lights. The contract reflects the complexity and scale of the operational work covered and runs to more than 1,000 pages.

The contract manager joined the procurement team in 2007, three years before the council signed the contract. The council followed Treasury task force guidance about continuity of staff; most of the team involved in the original procurement remain on the team or available to give advice.

Staff continuity meant the team was able to:

- test new procedures 'live' during a short mobilisation period of only a month between the contract award and its start
- provide advice to the contractor, which had appointed new staff to provide services under the contract who were not as familiar with the contract detail
- helping other internal parties understand the contractor's obligations to support building positive relationships.

Source: Audit Commission

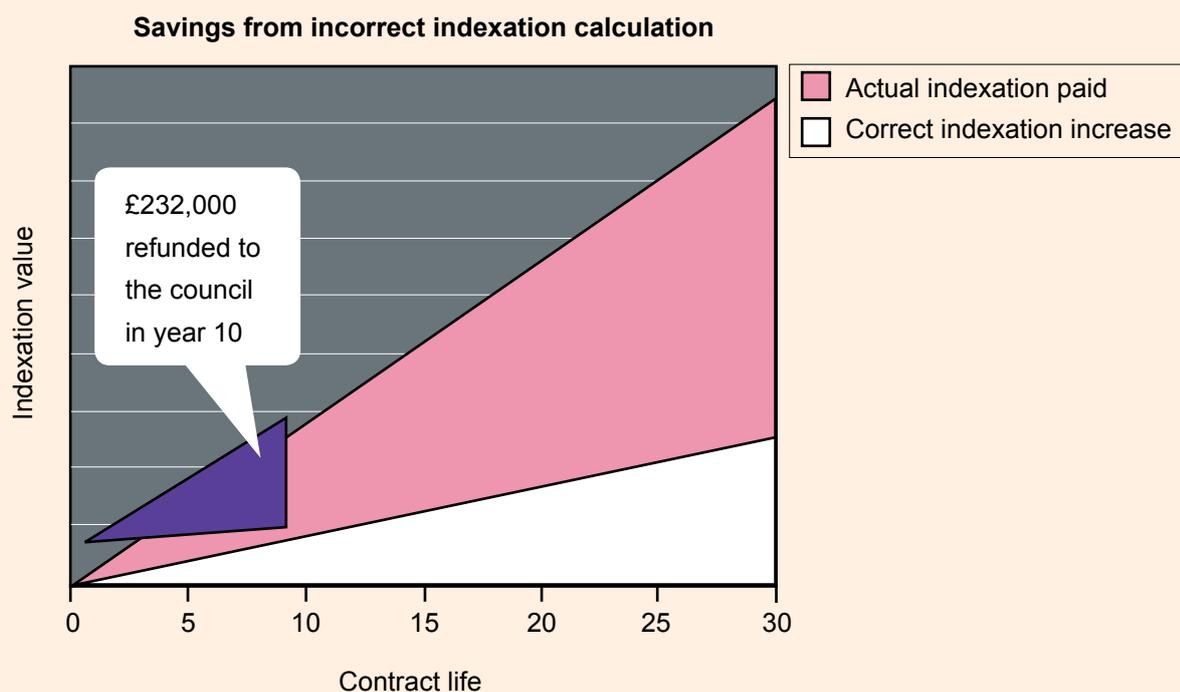
Having dedicated contract managers in place who understand the detail of the contract can help challenge invalid claims.

Case study 5 Sheffield City Council: avoiding unnecessary costs

In 2001, Sheffield Council signed a 30-year PFI to provide new office accommodation in the city centre. The annual cost of the contract is about £4.5 million.

In 2009, the council recruited a dedicated contract manager with commercial experience to manage the contract full-time.

In the 2010/11 financial year, the manager identified an excessive inflation rate applied to the indexation charge. He challenged the formula and successfully renegotiated the index rate, securing a single saving of £232,000 in the ten years of the contract to date, and saving future unnecessary costs.



Source: Audit Commission

An excessive focus on outputs may bring rigidity into contractor performance rather than the flexibility both sides seek. So many councils and their partners seek to agree key performance indicators (KPIs) that measure outcomes. Not all councils find this easy⁷ (Ref. 12)

Solihull Metropolitan Borough Council uses indicators of performance in areas known to affect user satisfaction, which it developed at a strategic level in collaboration with partners. The council and its partners regularly review these KPIs against a 2007 baseline. They regard them as challenging, allowing them to focus efforts to improve on specific areas of importance to service users.

Case study 6

Solihull Metropolitan Borough Council: using effective KPIs

Performance indicator	Target	2007 Baseline (Contractor A)	2011/12 (Contractor A)
Repairs completed on time	95%	97%	98%
Recall to works completed	<5%	5%	4%
Proportion of jobs delayed in comparison to jobs completed	<5%	12%	10%
Reactive repairs completed first time	70%	68%	79%
Response to customer complaints	100% within 10 working days	N/A	100%

KPIs show the partnership has improved performance. Services are more efficient, and customer satisfaction is at a high level. Examples of key achievements include:

- between 2007/08 and 2011/12 the average number of days from reporting a repair to completion, including any delays, reduced from 30 to 8.8 for routine reactive repairs and from 10.8 to 3.47 for urgent repairs
- between 2007/08 and 2011/12, the average job cost for a reactive repair reduced from £269 to £141, resulting in overall savings of £676K over the same period
- in 2011/12, all the 821 customer surveys completed showed that customers were satisfied with the works completed
- the corporate property services team has consistently achieved the government's 'Customer Service Excellence' (formally Charter Mark) award over the last 15 years.

Source: Audit Commission

⁷ The 2012 joint NLGN/CBI report on commissioning found that 39 per cent of councils cited difficulty in defining outcomes and 29 per cent lack of data on outcomes, as limitations in using outcome-based commissioning (Ref. 12).

Renegotiating contract terms

Changes to the contract arise in response to changing business or service user needs, better technology, market developments, and legislative changes. But increasingly, councils seek to change contracts because they simply have less money to spend.

This can mean asking suppliers to share pain as well as gain. This is clearly a difficult matter

Case study 7

Trafford Metropolitan Borough Council: asking suppliers to share the pain

In 2011/12, Trafford Council proposed, for the second year, a 0 per cent inflationary uplift on council contracts with residential care providers. The commissioning and procurement teams hosted several provider forums in autumn 2010 to explain the council's financial context and challenges. For their part, service providers were open about the effect this would have on their businesses.

The council also offered to meet providers individually to discuss the effect of a second year without inflationary increases in contract value. Based on open book accounting, providers that could show this would prove unsustainable might benefit from a contingency fund to support a 2.9 per cent inflationary uplift.

In 2011/12, the council received no requests on the fund. The savings achieved by this measure were roughly £1 million.

Source: Audit Commission

to discuss with potential suppliers and case study 7 highlights how an open and collaborative method can help.

Case study 8 sets out an approach tried out by Swale Borough Council to renegotiate one of its major contracts. In this example, the council worked proactively with the supplier to find a balance that ensured savings were made, but service quality was not compromised.

Case study 8

Swale Borough Council: negotiating savings and maintaining performance

In 2006, Swale Borough Council entered a seven-year contract for household waste and street cleaning. The terms required continuous improvement and efficiency. To reflect this, one clause stipulated that costs could fall by up to 10 per cent over the contract period from the initial £3.3 million.

By 2011, the contract was performing well, but costs were unchanged. Following the 2010 Spending Review, members sought savings from contracts, but without lower performance.

Before discussing this with the contractors, the council's contract monitoring team spent six months examining how the supplier achieved the desired outputs, to identify potential efficiencies.

The council was open with the supplier about the need for savings, but it was reluctant to invoke the clause that entitled them to 10 per cent reduction in contract costs. Their aim was to strike a balance between achieving savings and keeping the supplier motivated to deliver high performance.

The council presented savings as a joint challenge for themselves and the supplier to overcome. Together, they trialled changes to assess impact. They achieved lower costs by releasing efficiencies for the supplier; for example, releasing equipment the supplier could use on other contracts. This helped the supplier to minimise the impact on its business.

The council and the supplier worked together to reduce costs by 12 per cent. This saved the council around £425,000 over the remaining two years of the contract, without damaging service quality.

Source: Audit Commission

Other examples of councils using negotiation to gain better contract terms include:

- the London Borough of Camden, which led negotiations on behalf of London councils to secure standard prices for an ICT software package, after a data sharing exercise exposed a range in prices paid
- Allerdale District Council, which made substantial savings by renegotiating contracts with the support of a consultant (see Case Study 10 for full details).

Incentives

Not all councils in this study found renegotiation easy. The timing of discussions can help. Suppliers may be more willing to contemplate changes as contract review or renewal approaches. But even then, renegotiation will be more effective when the supplier has incentives.

For example, one council tendered for an integrated waste handling contract lasting 8.5 years, plus a 6.5 year extension, depending on performance measures including Continuous Improvement (EU rules allow past performance to be evaluated when considering an extension or new award). This created a more professional relationship with the contractor, which now has an incentive to develop a longer term relationship.

Price performance mechanisms can be a powerful incentive. Sheffield City Council pays contractors according to their performance against KPI targets in the service level agreement. Where targets are not met, the council will make financial adjustments.

But Sheffield also shares profit with contractors that results from innovation and efficiency. For example, in one arrangement, the supplier can keep half the profits from efficiency savings, where the idea or action that results in savings is generated by the supplier, not the council. The council keeps all the profit generated by its own ideas.

Solihull Metropolitan Borough Council has a pain/gain arrangement in its property services repairs contract. It is based on reducing overall costs, not margins, and the council uses open book accounting and is able to access the partners IT and financial systems to gather the relevant information. This includes further details of invoices from the partners, their subcontractors and suppliers, and time sheets for their direct labour workforce.

Case study 9

Solihull Metropolitan Borough Council: incentive mechanisms in a property services repairs contract

The council's maintenance and repairs partnering contract guarantees the partners payment for all works undertaken plus an agreed overhead and profit figure based on a forecast annual turnover. The turnover is reviewed on a quarterly basis to enable the partnership to adjust to the level of resources required. At the end of the financial year, any recovery of excess overheads is reimbursed. This has resulted in a reimbursement of £138,000 to the council over the seven years that the contracts have been operating.

The contracts also include a pain/gain arrangement for specific projects which enables the council and partners to agree a target cost for each project. If the projects come in below the target cost, then the savings are shared equally between the council and partners. Conversely, if a project comes in over the target cost, additional costs are also shared equally between the council and the partners. The council also provides the customers an option to buy into this arrangement.

Between 2007 and 2012, the partnership delivered works under budget by £516,318 resulting in savings of £258,159 for the council.

Overall savings summary (£000)

	Reactive works	Planned works	All works
Reactive works savings	731		731
Pain/gain savings		516	516
Staff savings*	45	68	113
Administration efficiencies*	74	111	185
Reduced overheads*	55	82	137
Total savings	907	778	1685
Contract costs 2007/08 – 2011/12	4679	12007	16686
%savings	19%	6%	10%

*figures as a notional 40/60 per cent split between reactive and planned works

Source: Audit Commission

Improving data

Improving data will enhance councils' ability to manage change and obtain continuous improvement over the life of the contract. The Government Procurement Service (GPS) is active in promoting Spend Analytics. Several consultants are active in this field, which aims to help councils monitor costs and performance.

Good data helps councils with the basics. Essex Council's e-procurement system (Ariba) requires colleagues to register all contracts. A recent project has identified up to 850 suppliers, including 700 providers of social care. This exercise demonstrated that the council spent about £38 million on 600 suppliers of adult social care services. The contracts varied in size from £500,000 to £1.5 million. Relatively small individually, in aggregate the sums amount to a substantial amount of money.

Comparative information about prices and performance is not widely available. The LGA is playing an active part in helping councils to benchmark their spend and performance on contracts through the following activities:

- Funding eight collaborative procurement projects, of which one is to analyse procurement spend among the twelve councils in the north-east.
- Working with councils to promote a better understanding of spending in three important categories: Construction, Energy and ICT. The ICT initiative is led by the London Borough of Camden. Initially a pan-London project that reported indicative savings from ICT purchases of £2.45 million in its first year, it has now been extended to cover the whole country.

- Launching LG Inform, a service that contains comparative financial data, and which could be a platform to collect data about contracts in the future.

Improving data will help councils to achieve all the savings and other benefits from contract management. The next chapter explores this in more detail.

Chapter 4

Realising benefits from contract management

The high volume and value of third party contracts suggests councils have scope to achieve savings and other benefits from contract management. This requires investment to obtain returns.

Councils are increasingly looking to achieve savings from contracts post-award. A survey in 2013 (Ref.13) found that 60 per cent of councils had achieved savings by reviewing and improving existing procurement contracts and just over half this proportion from better compliance on existing procurement contracts.

Councils mean different things when they talk about savings. Our analysis suggests financial benefits from contract management come from generating extra income, avoiding unnecessary costs (for example, duplicated tasks and processes) and from penalising poor performance. They also come from changes to:

- the scale of the contract (doing less, without affecting quality)
- the scope of the contract (doing fewer things, without affecting quality)
- cashable and non-cashable efficiencies (for example, reducing invoicing and increased productivity)
- avoiding unnecessary costs (for example, de-duplicating provision).

In this research, not all councils could quantify the savings they had achieved. Table 3 suggests that this varied from three to 15 per cent of the contract value.

Table 11: Assessed savings from contract management

	Contract cost	Contract length	Contract management savings (p/a)	Savings as a proportion of cost
Council A	c. £1.5m	4 years	c. £0.15m	10%
Council B	£9.0m	28 years	£0.25m	3%
Council C	£60m	20 years	£9.1m	15%
Council D	£30m	25 years	£2.7m	9%
Council E	£4.5m	30 years	c. £0.22m	5%

Source: Audit Commission

These examples should not be taken to mean that all councils could achieve savings of a similar magnitude. Each council, and each contract within its different services, will be different. The amount councils can save will depend on:

- the contract base price
- market conditions
- how changing needs affect the original scale or scope in the contract
- whether the council is in partnership with others in the contract.

However, our research suggests that contract benefits only come about if councils are willing to invest in contract management.

Return on investment

The benefits from investing in contract management can be difficult to foresee. Councils are sometimes understandably reluctant to invest the necessary resources.

Sheffield City Council uses a 'benefits tracker' that records all the financial and non-financial benefits they gain from contract management. This creates an audit trail and a means of quantifying their return from contract investment.

Table 12 shows Sheffield City Council's annual savings for seven major contracts in 2012/13. It shows contract savings from 2 to 31 per cent of the annual contract cost, across the seven contracts.

Table 12: Sheffield City Council contract management savings 2012/13 (£'000s)

	Contract A	Contract B	Contract C	Contract D	Contract E	Contract F	Contract G	Total all contracts
Annual contract cost	800	8,000	60,000	26,000	75,000	28,000	4,500	202,300
Savings category								
Cost avoidance	0.5	936	183	640	1,261	246	113	3,378
Efficiency	25	502	457	1,447		780	30	3,241
Income			39	1,599				1,638
Negotiation			2,194	187		10	85	2,475
Penalties	8	1	25					34
Scale		1,067		558		2,222		3,847
Scope		8				858	18	883
Total contract savings	33	2,514	2,897	4,430	1,261	4,115	245	15,496

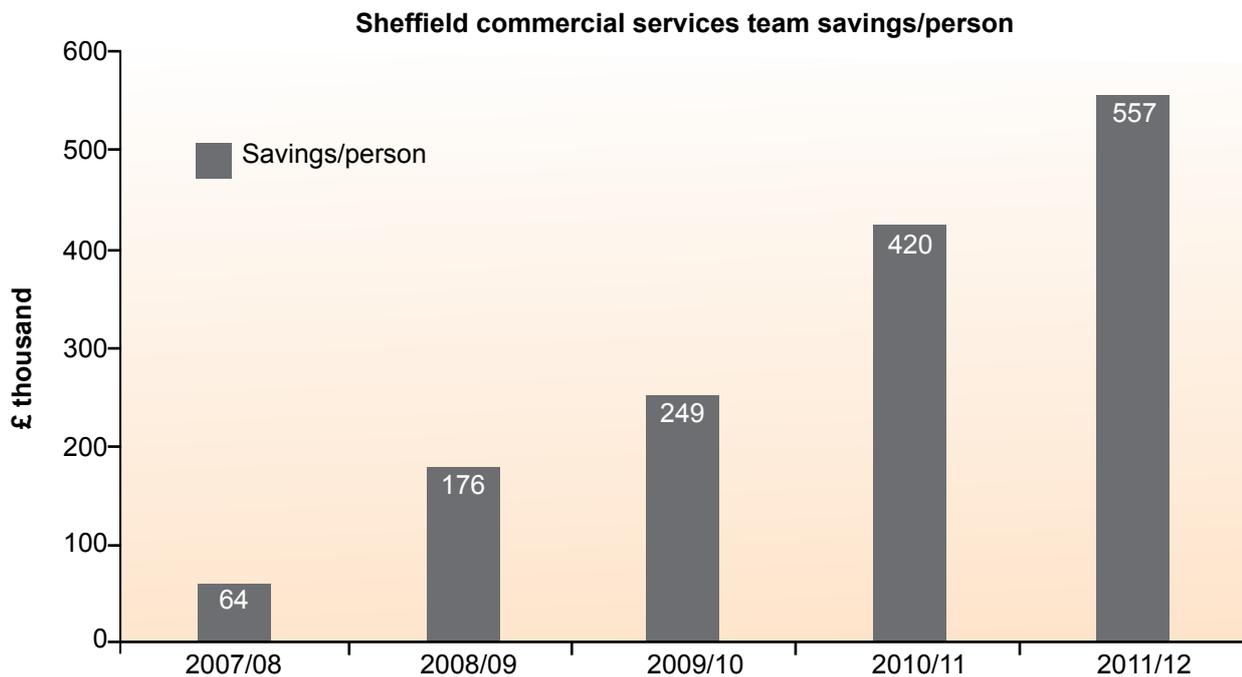
Source: Audit Commission analysis of Sheffield City Council Benefit Tracker

The table shows that for seven contracts, Sheffield City Council saved £15.5 million through contract management, which represented 8 per cent per cent of total contract costs. Nearly £4 million (2 per cent) of savings were achieved by reducing contract scale and about the same amount (£3.4 million) from cost avoidance.

The savings categories that produced the greatest proportion of contract savings are reducing contract scale (25 percent), cost avoidance (22 per cent) and efficiency savings (21 per cent).

Sheffield City Council has calculated the savings attributable to each member of the Commercial Services team. Figure 10 shows how these savings have grown over time. The council calculates that the savings achieved are equivalent to eleven times the average salary of a contract manager.

Figure 13: Sheffield City Council – average contract management savings per commercial services team member



Source: Sheffield City Council

Essex County Council has contributed its experience in achieving savings targets (over £150 million over three years from procurement and contract management) to the development of the Government’s Commissioning Academy (Ref. 14).

Essex achieved its savings in part from simple measures such as consolidating contracts. For example, it used to have about 80 separate suppliers for all aspects of highways maintenance, ranging from grass-cutting to design. It has re-tendered these in a single contract, where one supplier manages all the others.

To achieve its savings target of £50 million over the next two years will be difficult and savings from traditional tendering will yield reduced benefits going forward. Rather, the council will focus on obtaining savings through sophisticated category management activity alongside driving continuous

improvement from actively managing existing contracts and suppliers. For example, it recently agreed with a supplier to reduce the number of invoices generated, which ran at over 3,000 per month (as stipulated in the original contract).

Essex also wants active contract management to meet its wider corporate social responsibility objectives. These include such provisions as support for local charities (eg work experience placements for the Essex Coalition of Disabled People), volunteering opportunities, apprenticeships and providing ‘world of work’ days in local schools.

As well as savings, contract management will bring other benefits, although these are hard to quantify. One example includes better dialogue with suppliers through an engagement forum that jointly agrees improvements.

Supplier relationship management

Supplier relationship management (SRM) seeks to ensure councils receive the best possible deal, while recognising the risks to, and needs of, their suppliers. A good working relationship with a supplier should combine trust and flexibility with robust discussions about performance and changing needs where necessary.

“We need to deal with the myths of the past: ‘self managing contracts’ and ‘not upsetting the provider’.”

**Barry Mellor, Commercial Director
Sheffield City Council**

There is a difference of view about SRM among the councils we visited. Some believe it is an integral part of contract management, enabling councils to maximise the benefits they achieve from contracts by building a professional relationship based on trust. Others thought that contract management was better understood more narrowly as contract monitoring.

But all want flexibility in relationships. Some referred to ‘give and take’ in dealing with their supplier. They preferred not to invoke sanctions for relatively minor lapses in performance. One said it was important “not to take a hard approach – sometimes it is enough to let them know that you know what’s been going on”.

Essex County Council faced real problems in renegotiating contracts. Rather than ‘wield the big stick’ with suppliers, they encouraged an open and mutually beneficial discussion with them. Negotiations were productive because they had taken the time to explore problems and process improvements with them. Its SRM programme includes a 360 degree relationship survey of both sides to identify gaps and synergies.

For example, with one supplier, which runs several care homes, the council had traditionally used spot purchasing and had no meaningful relationship with them. The supplier’s staff didn’t know who to talk to in the council, or what the council’s embargo process was. In a workshop discussion, they agreed on solutions and how to communicate better, including creating a single point of contact.

Chapter 5

Skills for contract management

Ensuring people with the right skills are in place to carry out contract management is essential to release more value from contracts.

“Contract management requires specialist skills which councils often fail to recognise.”

Liz Welton, Society of Procurement Officers

A good contract manager will look at detail, but also consider the overall picture to identify risks, solutions and opportunities. Their work requires them to build relationships with every area of the business, including back-office and front-line staff at all levels. Most importantly, the contract manager should have strong commercial awareness of costs and pricing (Ref. 15).

Commercial acumen

Commerciality is a key skill. It involves not just an understanding of costs and the market, but also the contractor’s business model. It also requires a questioning approach to the prices charged.

One corporate contract manager told us that colleagues in service departments did not universally have this tradition of questioning quoted costs, or of understanding commercial issues. She gave two examples:

- A social worker commissioned specialist care for a child with special needs following a psychologist’s report. The care was excellent, but the social worker did not question the very high costs, being solely concerned with whether the care met the needs identified by the psychologist. A more commercial approach would have questioned and negotiated with the supplier over costs, without jeopardising the quality of services.
- Colleagues bought office goods and stationery from a local shop rather than using the corporate framework agreement. The justification – that local goods were cheaper – failed to take account of the bulk discounts the council achieves through proper procurement processes, or the cost of processing expenses claims and purchase orders outside of the council’s procurement system. In the long run, these add more costs than the perceived savings from buying locally.

This commercial acumen is important in contract management. Some participants in this study had a background in commerce prior to joining their council. They tended to believe that it was useful in price negotiations or in performance management discussions (“they know we know”).

Others acknowledged that they needed outside help and employed consultants to provide it.

Consultants

Some councils use consultants to negotiate savings from existing contracts, sometimes on a 'no-win, no-fee' service. In doing so, councils must balance their need to make savings against the risk that hard renegotiations of contracts may damage longer term relationships with suppliers.

This is borne out by Allerdale Borough Council's experience. The corporate director with responsibility for managing contracts realised on joining the council that the four main contracts had not been actively managed for some time. He sought expert help to review and renegotiate them.

Case study 10

Allerdale Borough Council: using consultants

The council has four main contracts with an annual value of £6.4 million, within a total budget of £15 million. These delivered high quality services, but at a high cost. Aiming to cut £1 million from contract values over three years to help meet the savings target, the council won £9,000 funding from the LGA's Productivity Expert Programme to employ an independent consultant to review and renegotiate the contracts.

In two meetings with the contractor for the two main contracts in refuse and waste management worth £4.6 million per year, the consultant set out the council's financial position and the savings needed. The first meeting did not produce agreement, but the contractor understood the council was serious and that contract termination was a possible outcome.

The consultant appointed through the expert programme had extensive experience working with blue chip clients in the private sector. His knowledge of negotiation tactics and processes and contract law ensured that the council was in a stronger bargaining position than it had believed.

The second meeting resulted in agreement to save over £300,000 in each of the remaining years of the contract. A further agreement for additional income from trading waste and recycling services did not come about, but enabled the council to negotiate higher prices with existing suppliers.

The council now has a better appreciation of the importance of:

- understanding the detail of the contract
- developing good relationships, based on an understanding of each other's position
- being aware of legal issues in procurement and renegotiation, without being risk-averse
- being aware that negotiation is a specialist area requiring a skill set more commonly found in the private sector.

Source: Audit Commission

In Birmingham, consultants have also played a part in negotiating savings, even though it has a well established procurement and contract management team in place. For an investment of £30,000, Birmingham obtained independent advice on current energy and commodity prices and future trends. This commercial market expertise enabled the council to build a strong case for renegotiation, based on developments since the contract award. Negotiations were intensive, but they reached agreement with the contractor on savings worth £2.7 million for the remaining seven years of the contract.

While some councils in our research had used consultants successfully, others believed they would damage relationships with contractors and would not deliver value for money in the long term. Where consultants are not used, councils have to appoint people with relevant experience. And all do or plan to provide training.

Training in contract management

In 2012, Sheffield City Council took part in the LGA collaborative procurement pilots. The LGA awarded Sheffield a small grant to disseminate its training toolkit more widely, and to offer training to other councils in its use. Sheffield's approach has recently won a national award.

Sheffield City Council commercial services directorate

Winning awards for contract management training

Sheffield's approach to developing contract management skills has won national recognition. The Chartered Institute of Purchasing and Supply (CIPS) awarded the council's commercial services directorate the award for Best People Development Initiative in September 2013.

The council says: "This award is in recognition for what we have been doing in the profession to promote contract management and to give people the world class tools to become effective contract managers. This has included the development of the Intelligent Client Model, the Contract Management Toolkit, the roll out and training delivered to all the contract managers (some 200 people) in Sheffield and the tangible results which have been achieved (£38 million over the last four years) and also the superb work which we are leading across England with some 20 local authorities either already using the Contract Management Toolkit or in the process of implementing it".

The CIPS judges said "The clear tangible and sustainable benefits of this focus on contract management address an area that is often overlooked when it comes to staff development".

Source: Sheffield City Council

The toolkit underpinning the Intelligent Client approach (see Chapter 2) has three broad themes, each with several parts:

Figure 14: Sheffield City Council, contract management toolkit processes

Contract Process Management Processes	Contract Performance Management Processes
Asset Management	Benchmarking / Market Testing
Business Continuity	Benefits Realisation
Change	Performance Management
Contract Activity Timelines	Quality Audit
Contract Health Checking	
Dispute Resolution Procedure	Strategic Relationship Management Processes
Exit	Governance
Financial Strategy	Relationship Management
Financial Updates and Modelling	Stakeholder Management and Communications
Notice / Termination	
Operational Contract Manual	
Payment	
Project Management	
Resource Planning	
Risk Management	
Service Review and Planning	
Step In	
Transition / Mobilisation	

Source: Sheffield City Council

Essex County Council has an integrated approach to training in contract management. Its training programme includes a learning and development on-line tool, that allows staff to self-assess competencies on a scale from Level 0 (no experience) up to Level 4 (expert). The modules cover a range of skills, including communication, problem solving, and managerial skills.

The modules on improving technical skills include risk management, project management, procurement, relationship management, commercial acumen and contract management. The criteria for the self-assessments against these modules are shown in Figure 15.

Figure 15: Essex County Council assessment criteria

	Basic	Advanced
<p>Contract management: Able to identify, manage and negotiate contractual relationships. Demonstrates a broad range of commercial skills, and is able to resolve difficulties through negotiation and leadership.</p>	<ul style="list-style-type: none"> • Understands the role of key performance indicators (KPIs) and monitors supplier performance against these, identifying when corrective action needed • Identifies improvements required and supports negotiation of improvements in performance • Analyses and manages supplier performance using agreed performance measurement methods and informs stakeholders • Assesses effectiveness of contract and identifies whether it is still appropriate to meet variation in requirements from tender 	<ul style="list-style-type: none"> • Experienced in negotiating agreements in SLAs at Board level • Demonstrates the broad range of commercial skills and commercial awareness required to lead negotiations with strategic suppliers for major complex projects; • Engages effectively at Board level with key suppliers • Renegotiates fundamental contract terms or terminates contracts, appropriately and legally where necessary. Facilitates procurement process where appropriate • Identifies, develops and leads best practice in contract management across all levels of organisation
<p>Commercial acumen Takes an entrepreneurial approach, identifying and exploiting opportunities, with a broad understanding and appreciation of markets and commercial practices</p>	<ul style="list-style-type: none"> • Identifies local commercial opportunities and helps ensure they are exploited • Displays a basic understanding of common commercial practices relative to own service and the motivations of businesses providing services to us. • Has a positive attitude to risk taking • Helps promote specific marketing campaigns to customers 	<ul style="list-style-type: none"> • Develops and supports an entrepreneurial culture across the service • Anticipates market trends to strategically position service to fully exploit emergent/ future markets • Develops and leads on strategic marketing for service • Displays in depth understanding of commercial practices across a range of related sectors

Source: Essex County Council

Essex County Council has provided various tools to help staff acquire the necessary skills. For example, it has provided a negotiation template for planning for each meeting with a supplier. This enables a contract manager to assess whether negotiation is necessary, to be clear about the purpose of the negotiation, which roles the negotiating team should include (such as lead negotiator, financial/commercial specialist, legal specialist, technical specialist, summariser/note taker, and observer), and to identify the correct negotiating strategy.

It includes:

- opening statement (introductions and objectives from the meeting)
- different proposals the Council will put and accept, in order of priority
- supporting information (including performance history)
- identifying key questions, assumptions, information
- main issues and resolutions
- must achieve and must avoid objectives
- wish list of favourable outcomes
- possible concessions and scope for negotiation
- supplier objectives (what is important to them?)
- other considerations (eg sensitive information)
- strategy (best approach and approach to avoid)
- final outcome.

The London Borough of Camden is developing a framework which seeks to standardise contract management across the organisation. The framework aims to develop new and consistent ways of working by establishing contract management early in the procurement process, and embedding clear protocols for contract management once the contract has been let. The framework consists of 12 'mini guides' to help service managers address specific contract management issues. A key feature of the guides is 'plain English' language, which is used to better engage with service staff and support learning.

Conclusion

Councils have less money to spend, and the financial pressures they face mean that it is likely that many will outsource more services, in a variety of models. Getting as much value as possible from an increasing diversity of suppliers means contract management is vitally important.

Contract management is now rightly high on councils' agenda. And while it is better to get contracts right at the beginning, many are increasingly confident that they can renegotiate them. And confidence is key – with the right training and approach, councils will find many contractors are ready to discuss changes to contract terms and conditions. It is important to develop good commercial awareness and productive and professional relationships.

Building on the good practice identified in this research, we have set out five broad principles of good contract management, which are described in Appendix 1.

In different ways, councils in this study have demonstrated they meet all or some of these principles. They plan for contract management, they have invested resources in getting better at it, and the best have a corporate approach that integrates contract management within an overall commissioning model, while recognising its distinctive features.

Appendix 1: Principles of good contract management

Councils in this study have achieved efficiency savings and wider benefits from developing their approach to contract management. They have shown that taking an active approach to contract management helps to realise the gains that outsourcing can provide, and minimise the risks involved.

Their experience can help other councils that need to realise the efficiency and other gains from good contract management. Designing and managing contracts well will save councils money, achieve wider objectives and minimise risks.

They can follow these principles, based on our research in this study, to help them achieve their objectives.

1. Provide corporate support for contract management

- Councils can be intelligent clients. The more they outsource, the more contract management will help them achieve their objectives. A corporate approach:
 - recognises and values the role of the contract manager
 - ensures roles and responsibilities are clearly defined and resolves internal disputes
 - puts in place the structures, systems and processes to create effective accountability and reporting
 - integrates contract management within its commissioning model, ensuring that technical service expertise combines with procurement and contract management skills during the whole of the contract life
 - invests money and time in developing and sustaining a capacity for good contract management.

2. Aim to get continuous improvement in contractors' performance

- Councils can use contracts that:
 - contain incentives and levers to vary costs and service levels
 - encourage innovation
 - have rigorous change control
 - control costs and incentivise savings and other benefits.
- To achieve these outcomes requires active management over the life of the contract. Effective councils recognise that continuous improvement can benefit both parties and is more than a means to drive down prices.

3. Invest in developing commercial skills

- Effective councils understand that contract management requires specialist skills that are linked with, but different from procurement or service delivery.
- Commercial skills involve:
 - understanding costs and profit, and the market, as well as service quality
 - being on top of the contract detail, including review and renewal dates
 - being able to foster professional relationships with suppliers (supplier relationship management)
 - a robust approach to renegotiation, including any legal implications.
- Commercial skills are in short supply in local government. Councils can:
 - recruit staff from a commercial background

- appoint consultants
 - adopt or adapt the approaches developed by other councils
 - train their staff.
- There are now a number of useful training programmes and associated guidance developed by councils to improve contract management. They are available at small or no cost to others.

4. Collaborate to maximise gains

- Councils can work collaboratively:
 - internally across services to reduce the tension that can exist between central contract management staff and service managers
 - with suppliers and contractors to agree mutually beneficial outcomes from changing terms and conditions
 - with other councils to share information about prices and performance, learn of innovations and manage risks.
- Regardless of whether or not councils call their contracts partnerships, they can develop and sustain relationships that promote flexibility in managing change and a good understanding of the impact of change on each party to the contract.
- Collaboration has an unrealised potential to promote more transparency about prices and performance. Councils can extend the benefits from collaborative procurement to make supplier performance and costs more open and transparent.

5. Monitor and benchmark costs and performance

- Councils can put in place systems and processes that allow them to:
 - map how many contracts they have
 - measure how much of their spend is on contract
 - collect independent feedback on performance to help monitor contract compliance
 - measure the benefits, including savings, they obtain.
- Effective use of ICT, as in e-procurement, also enables councils to create organisational memory, so that when staff with key skills leave, they retain knowledge about contracts and agreements.
- Effective councils know their key customers (internal, external, end user, other stakeholders) and:
 - develop performance indicators that are important to them
 - align these indicators with business outcomes and review them regularly.
- Councils can benchmark their contract spending and outcomes internally over time and with other councils. This provides market intelligence about current and potential suppliers and emerging technologies. It informs their contingency planning and re-competition strategies.

Appendix 2: Methodology

The Local Government Association (LGA) and the Audit Commission worked in partnership on this project. It was overseen by Siobhan Coughlan, Programme Manager, Productivity at the LGA. Latterly, the study team at the Audit Commission comprised Mark Wardman (report author) and Emma MacLeod, while Sally Hammond provided project oversight. Other Commission staff involved in earlier stages included Kirsten Payne (while on secondment from the National Audit Office), Diane Ridley and Sarah Windress.

The Audit Commission carried out fieldwork for the study between February 2012 and March 2013. The study team used a mixed methods approach to:

- analyse the Department for Local Government's Subjective Analysis returns
- analyse the data published by local authorities on external spending over £500
- review literature from academic publications, and good practice guidance on contract management and government policy
- interview key stakeholders and experts in contract management
- carry out case studies in ten councils.

Subjective analysis return data

Since 1998-99 a sample of local authorities has completed the Subjective Analysis Return (136 local authorities from 2005-06). This shows how net current expenditure is broken down between pay and the procurement of goods and services. Procurement of goods and services is analysed to show goods and services purchased directly and services provided by external contractors (private contractors and voluntary organisations) or internal trading services.

Total expenditure on pay and the procurement of goods and services is consistent with Revenue Outturn data, but has been adjusted to exclude double counting of expenditure that has been recharged between service blocks within the General Fund Revenue Account, or between one local authority and another.

Due to the nature of subjective analysis returns, not all third party payments are captured under the 'Third Party Payments' section of the data, if they fall within other categories. For example, contract cleaning may fall within premises-related expenditure. The figure of £27.2 billion is probably an underestimate, but one we felt it prudent to use throughout the report.

Local authority £500 data

From January 2011, councils have published all items of external expenditure over £500 as part of the transparency agenda. There is no standard reporting structure and councils can decide how much information to publish.

The Audit Commission analysed these data for 330 councils⁸. The data cover the period April 2011 to March 2012. Any government organisations identified in the top suppliers were excluded from the analysis. The data were standardised to a single format and included data on date of transaction, supplier, and amount.

Suppliers were recorded in free-text and mapped to a consistent naming convention. This was completed for the 25 suppliers identified in the analysis with which councils had the highest spend. A similar approach for all suppliers would have been too time-consuming.

These data, and the conclusions based on them in the report, should be treated with some caution for these reasons: spend under £500 is not included; there may be inaccuracies due to inconsistent naming of suppliers across councils; there may be inconsistent treatment of VAT across councils; and payments comprise a mixture of capital and revenue.

Case studies

We collected documentary analysis and interviewed key stakeholders in 10 case study authorities. Case studies were selected mainly through suggestions from stakeholders but also included different types of authority.

- **Allerdale Borough Council**
Contact: Paul Shackley, Corporate Director
01900 702547
paul.shackley@allerdale.gov.uk
- **Birmingham City Council**
Contact: Nigel Kletz, Assistant Director – Corporate Procurement
0121 303 6610
nigel.kletz@birmingham.gov.uk
- **London Borough of Camden**
Contact: Darren Sivapalan, Procurement Strategy Manager
020 7974 8561
darren.sivapalan@camden.gov.uk
- **Essex County Council**
Contacts: Jane Quy and Jackie Gregory, Supply Chain Managers
jane.quy@essex.gov.uk
jackie.gregory@essex.gov.uk
- **Improvement and Efficiency South-East**
Contact: Keith Heard, Senior Programme Manager
01962 845903
keith.heard@hants.gov.uk

⁸ The remainder did not publish £500 data on their website.

- **Selby District Council**
Contact: Karen Iveson,
Executive Director (S151)
01757 292056
kiveson@selby.gcsx.gov.uk

- **Sheffield City Council**
Contacts: Barry Mellor, Commercial
Director
0114 205 3928
barry.mellor@sheffield.gov.uk

Andy Howells, Assistant Commercial
Director
0114 205 7303
andy.howells@sheffield.gov.uk

- **Solihull Metropolitan Borough Council**
Contact: Paul Evans, Corporate Property
Services Manager
0121 704 6494
pevans@solihull.gov.uk

- **Swale Borough Council**
Contacts: Dave Thomas, Head of
Commissioning and Customer Contact
01795 41 7263
davethomas@swale.gov.uk

Alan Turner, Contracts and
Procurement Manager
01795 417285
alanturner@swale.gov.uk

- **Trafford Metropolitan Borough Council**
Contact: Linda Harper, Director of
Commissioning and Service Development
0161 912 1890
linda.harper@trafford.gov.uk

We also interviewed key stakeholders from the following organisations:

- Local Government Association (LGA)
- Society of Procurement Officers
- Chartered Institute of Procurement and Supply
- Cabinet Office.

The LGA and the Audit Commission thank all individuals and organisations that took part in the study.

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