Occasional Paper

Contractorisation of UK Defence
Developing a Defence-Wide Contractorisation Strategy and Improving Implementation

Jay Edwards
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Foreword

Trevor Taylor and John Louth

In both the generation and use of military capability, the British Ministry of Defence (MoD) outsources the provision of goods and services more than any other advanced industrial country: contractors are to be found in almost every area of defence, reflecting beliefs that the risks and transaction costs of relying on external organisations are tolerable, and that the private sector is almost invariably less costly and more efficient than government bodies. Currently we calculate that the MoD spends around two thirds of its budget with the private sector. The UK has gone further than even the US, where at least half of depot-level maintenance for military systems must still be done in government installations, and of course the MoD operates dozens of Private Finance Initiatives. Arguments can be made in two directions: that the privatisation of defence has not yet gone far enough and that in some fields it has gone too far.

The Modernising Defence Programme (MDP), underway in 2018, should address this issue with two of its four workstreams relating in part to outsourcing issues:

Workstream 2 – Efficiency and business modernisation: providing confidence in the MoD’s ability to realise existing efficiency targets, and a set of options for future efficiency and business modernisation investments.

Workstream 3 – Commercial and industrial approach: assessing how the MoD can improve on commercial capability and strategic supplier management.

It is in this context that the Defence, Industries and Society programme at RUSI is pleased to support this personal contribution by Jay Edwards. While RUSI does not hold institutional positions, it is publishing this paper because the reasoning and evidence it contains make it a valuable contribution to the ongoing debate. This is not least because it addresses the ‘inherently governmental’ aspects of defence, a topic much analysed in the US but rarely mentioned here in the UK. Yet, it is a topic, by definition, which needs to be addressed substantively by the MDP. In this regard, Edwards’s work will allow us to critique the MDP when first principles are announced by the MoD. His work, consequently, is timely and important.
Executive Summary

- Contractorisation in defence has steadily grown since the 1980s, driven by the need to reduce costs, maintain expeditionary capability and invest in equipment and infrastructure.
- The National Security Strategy and Strategic Defence and Security Review (NSS and SDSR) 2015 stated that Ministry of Defence (MoD) civil servants and contractors should be used to support the front line and deploy forward when required. However, there is no publicly available contractorisation strategy for driving best practice and defining which parts of defence are inherently governmental and which parts should be contractorised.
- The main rationale for contractorisation is that a contractor can deliver outputs at a lower cost than in-house military or civil service providers. Contractors can theoretically reduce costs by up to 30% through competitive tendering, lower staff costs, specialisation, multi-skilling and revenue generation. However, this is a broad estimate and each contractorisation project will have different benefits, costs and risks depending on the circumstances.
- Despite the prevalence of contractorisation across defence, there remain a number of challenges that need to be tackled to maximise value. These challenges span the contract lifecycle from high-level contractorisation strategy to implementation, including running a tender process and managing contracts over their lifecycle.
- At a high level, defence could be defined by four inherently governmental areas:
  - **Policy and Requirements** – Policy and requirement approval roles within Head Office and the Front Line Commands are inherently governmental, although non-inherently governmental support roles could be contractorised further if this is cost effective. This could include contractors defining and analysing requirements that are reviewed and approved by government employees.
  - **Direct Participation in Hostilities** – Roles in the Front Line Commands involving the operation of weapons and platforms and the direct support of operations through planning and intelligence gathering have been largely untouched by contractorisation. These roles are at the core of the MoD’s mission and operations, and are likely to always be inherently governmental.
  - **Enforcing Military Discipline** – The enforcement of military discipline carried out by the service police is inherently governmental; however, support roles could be contractorised if this is cost effective.
  - **Committing Public Expenditure** – Defence Equipment and Support and Information Systems and Services (DE&S and ISS) are both partially contractorised, with many support functions carried out by contractors. If further contractorisation is carried
out it should be accompanied by a review of which decision-making roles are inherently governmental.

- Contractorisation of support functions that are not inherently governmental could go further if this is cost effective, particularly those based in the UK. Deployable support functions could be provided by a Whole Force Approach model whereby, on enduring operations, high-readiness military personnel are followed by contractors once an overseas base has been secured. However, this deployment model is based on war fighting against a low-technology, asymmetric enemy where bases in enemy territory can be made relatively secure. The Sponsored Reserves model enables contractor staff to deliver a service to the military or commercially in peacetime, and during operations to change into military uniform and operate under military terms and conditions. Further research is required to understand the cost-effectiveness of these contractor deployment models.

- There are improvements that need to be made across the areas of Strategy, Process, Performance Monitoring, Benefits, Technology and People to ensure the full value of contractorisation to defence is realised while keeping operational risks as low as possible.

- It is vitally important that a detailed contractorisation strategy is created and improvements to implementation are made to underpin the Whole Force Approach. This would ensure that inherently governmental roles are protected and that the full benefit of cost savings is achieved from support roles.
Introduction

In this paper, contractorisation is defined as the provision of a service by an external contractor that was previously provided by military or civil service personnel. Contractorisation is also referred to as civilianisation, outsourcing or privatisation. The high-level scope of contractorisation considered in this paper includes organisations within the current defence operating model, and defence organisations that were contractorised in some form from the 1980s onwards, excluding the design and manufacture of equipment. The Ministry of Defence (MoD) budget in 2016–17 was £35.3 billion, of which £24.1 billion was spent externally, £6.4 billion of this on the equipment procurement programme. This leaves approximately £11.2 billion of internal annual spend on military and civil service personnel, which could be protected or contractorised further, and the remaining external spend, which could potentially be managed better.

Contractorisation within the military has grown relatively organically from base support functions in the UK in the 1980s to significant support on the front line in Iraq and Afghanistan in the 2000s. The first significant move towards contractorisation was the MoD’s competitive procurement policy, introduced in 1983 as part of the Conservative government’s defence policy aimed at improving efficiency and achieving value for money. As a result, defence support functions were undertaken by the private sector unless it was operationally essential or more cost effective to keep them in-house. This policy was followed in 1991 by the Competing for Quality White Paper, which led to further contractorisation in logistics support and facilities management where tasks did not impinge directly on the services’ operational roles. In 1998, the Better Quality Service initiative led the way for large-scale, multi-activity contracts and Private Finance Initiative (PFI) schemes for equipment and infrastructure. In the same year, the Strategic Defence Review stated that, where appropriate, the MoD would consider the use of contractors to assist with logistics support, and this was followed by the extensive use of contractors during UK military operations in Iraq and Afghanistan. More recently, the Whole Force Concept in the 2011 Levene Report recommended that defence be supported by the most

cost-effective balance of regular military personnel, reservists, MoD civilians, and contractors.\(^8\) The Whole Force Concept was upgraded to the Whole Force Approach in the National Security Strategy and Strategic Defence and Security Review (NSS and SDSR) 2015,\(^9\) which stated that MoD civil servants and contractors should be used to support the front line and deploy forward when required.

In January 2018, the Modernising Defence Programme was announced with the aim of delivering better military capability in a sustainable and affordable way. A large part of the programme will involve identifying further efficiencies and ways to be more productive, including an aggressive programme of business modernisation.\(^10\) If further efficiencies are to be found, the MoD will need to consider how external spend (approximately 70% of the annual budget)\(^11\) can be managed more effectively and whether further contractorisation of in-house spend can reduce costs while maintaining outputs.

Contractorisation has touched almost every part of defence, from back office and support functions in the UK to the operation of drones in Afghanistan.\(^12\) In many cases, it is an effective way of maintaining defence outputs while reducing costs. However, it has not always been successful, with some major contractorisation projects falling short of expectations. The problems arguably stem from the lack of a defence-wide strategy to drive best practice and define which parts of the defence enterprise are inherently governmental and which parts can be contractorised. The current approach is piecemeal, with different and often overlapping parts of defence contractorised in isolation using differing procurement and contract-management methods. This results in the full value to defence not being realised and the risk that operational capability could be compromised. This paper will begin to develop a high-level, defence-wide contractorisation strategy and define how implementation could be improved to underpin the Whole Force Approach.

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I. Rationale and Challenges of Contractorisation

Rationale of Contractorisation

During the twentieth century, the UK defence enterprise was characterised as a model of self-sufficiency, with uniformed personnel providing the majority of support services at home and on operations such as logistics, engineering, and catering. This was mirrored in the commercial environment, where vertical integration was popular and ensured a company had complete control over its supply chain. This allowed quality, cost, and delivery to be tightly controlled, but was found to be a costly strategy when demand shifted and restructuring was required.

UK defence at the end of the twentieth century and first part of the twenty-first century has been characterised by budget pressures and highly expeditionary warfare. The need to both reduce costs and maintain expeditionary capability has driven defence towards contractorisation. Again, this model mirrors the ‘core competence’ model first popular in the commercial environment, where companies protect and invest in the core competencies that are unique in the market and outsource any support areas outside of these.

The main rationale for contractorisation in defence has undoubtedly stemmed from the need to reduce costs while maintaining outputs. The cost reduction associated with contractorisation of public services in the UK is reported to be between 10% and 30%, and, in line with this, the contractorisation of military functions in the US is reported to achieve a cost reduction of around 30%. However, these are broad estimates, and each project will have different benefits, costs and risks depending on the circumstances.

There are five key reasons why contractorisation in defence can, theoretically, achieve significant cost savings:

1. Competitive Tendering – Contractors are generally considered more cost effective than in-house military or civil service provision because competitive tendering and the need to generate profits exert a powerful discipline on private sector management and employees to maximise efficiency. A contractor is financially incentivised to analyse

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working processes and identify opportunities to reduce inputs such as personnel, equipment or infrastructure while maintaining outputs. Under a government-delivered monopoly-supply arrangement, there are few incentives for in-house units to seek lower-cost methods of work because operating costs are met from defence budget allocations, and policymakers lack comparative cost data on alternative sources of supply.¹⁵

2. **Specialisation** – Military personnel frequently rotate between roles, follow harmony guidelines in the deployed environment, fulfil a number of additional roles, such as guarding or ceremonial duties, and have significant training outside their main role. Contractors are able to specialise in a permanent role or roles so that there is only one learning curve and distractions are kept to a minimum. Current estimates indicate that military personnel spend approximately 60% of total work hours in their main role compared to approximately 90% for contractors.¹⁶

3. **Cross-Skilling** – The military has an internal trade structure that creates trade groups within each of the services. This often makes it difficult to cross-skill military personnel to increase efficiency and results in large numbers of personnel being required to cover surges in different trade areas. A contractor does not have these artificial barriers and can cross-train staff to ensure a smaller number of personnel can manage surges in different trade areas. For example, the RAF has one trade group to drive fuel trucks to an aircraft and another trade group to fit the fuel hose. This results in two military personnel being required for a task that typically one contractor would perform.

4. **Remuneration** – Contractors sometimes have lower staff costs compared with military personnel because the military offers a number of expensive benefits. Military personnel are entitled to a final salary pension, comprehensive training and subsidised housing, meals and travel. There are cases where contractors have higher staff costs, such as in the replacement of military personnel with contractors in highly skilled engineering roles, because the skills are scarce in the commercial sector. The use of contractors on a hostile deployment is an area where cost savings may be minimal (unless the staff are local) due to the cost of attracting them to remote and potentially dangerous locations.

5. **Revenue Generation** – The MoD owns a significant amount of equipment and infrastructure that, due to the nature of defence, is heavily utilised during operations and could be underutilised during peacetime. These assets may be valuable to the commercial sector, but the MoD might not have the commercial expertise to exploit this opportunity. Contractors can operate these assets under terms that ensure capacity is available for operations while maximising revenue creation opportunities for the MoD and the contractor. For example, Solent Gateway Ltd won a 35-year contract in 2016 to run Marchwood Military Port, near Southampton.¹⁷ The company must ensure the port is available for operations in a pre-determined timeframe but can use spare port capacity for commercial opportunities.

For these reasons, a contractor is able, in certain circumstances, to provide the same service at a significantly lower cost than military provision. This is despite the contractor needing to make a profit and the MoD needing to fund a contract management team. With the defence budget under constant pressure, this is an attractive proposition for defence chiefs and many services have already been contractorised. However, cost reduction has not been the only driver for contractorisation; there are other key reasons:

1. **Operational Pressure** – The wars in Iraq and Afghanistan were significant enduring operations that imposed a great deal of stress on military numbers. As a result, contractors were used in the deployed space in greater numbers than ever before, providing core services in support of operations. For example, KBR carried out a number of support functions for British forces in Afghanistan, including construction, catering, vehicle maintenance and facilities management.18

2. **Technical Skills** – The military is increasingly dependent on advanced technology that is developed and supplied by industry. If technology is matured to a sufficient level and brought into service, a contractor can train military or civil service personnel to operate and maintain it. However, despite this knowledge transfer, the complexity of the technology means that the contractor is likely to be heavily involved during the entire CADMID (Concept, Assessment, Development, Manufacture, In-Service, and Disposal) lifecycle.

3. **Policy** – The NSS and SDSR 2015 stated that the MoD would continue to be reformed to make it leaner and more efficient and that key functions would be outsourced where the private sector could improve delivery. This was reinforced by a target to reduce the number of civilians employed by the MoD by almost 30%.19 SDSR 2010 had set targets to reduce the number of MoD civil servants by 25,000 and service personnel by around 17,000.20 These targets are difficult to achieve with efficiency savings alone and contractorisation offers a way to achieve the cost reductions and personnel reductions set in policy.

4. **Investment** – Contractorisation can also be used to fund investment in new equipment and infrastructure. PFIs21 and similar mechanisms are sometimes controversial and their value for money has been widely questioned. However, PFIs can result in investment years before traditional MoD funding routes. For example, under a £1.1-billion PFI, the UK Military Flying Training System contract established with Ascent in 2008 is providing modern training aircraft, ground-based training devices and infrastructure for flying training across the three armed services until 2033. The investment in aircraft and infrastructure would have arguably taken longer to achieve under an MoD-financed scheme.

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21. A Private Finance Initiative (PFI) is a method of providing funds for major capital investments where private firms are contracted to complete and manage public projects. Under a PFI, the private company, not the government, handles the upfront costs. The project is then leased to the public, and the government authority makes annual payments to the private company.
The combination of cost reduction, operational pressure, technology, policy and opportunities for investment has created the momentum for a powerful shift towards contractorisation in defence since the 1980s. However, contractorisation sometimes does not meet cost reduction or performance expectations and problems can occur throughout the life of a contract.

Challenges of Contractorisation

Despite the prevalence of contractorisation across defence, there remain a number of challenges that need to be tackled to maximise value. These challenges span the contract lifecycle from high-level strategy to implementation, including running a tender process and managing contracts.

Strategy

Currently, contractorisation across defence is on a case-by-case basis rather than the result of an enterprise-wide strategy. This can lead to inefficiencies when new contracts overlap with existing contracts or military capability. For example, RAF Brize Norton has duplicated aircraft ground-handling capabilities, which are provided by both the RAF and contractors due to the AirTanker contract.\(^\text{22}\) This has created a surplus of equipment and trained personnel at RAF Brize Norton, but it is time-consuming and expensive to try to alter existing long-term contracts to achieve further efficiencies. As more defence functions are contractorised, a patchwork of contracts with multiple interfaces and dependencies is created. It is unlikely that these contracts are aligned or optimised to achieve the greatest value for money for defence, and there is a risk that operational capability is compromised by contractorised services that are later identified as core competencies of defence.

Implementation

Tender Process

Running a tender process for the contractorisation of complex services is difficult and, if carried out incorrectly, can result in poor outcomes for both sides, with the MoD paying too much or receiving a poor service and the contractor struggling to make a profit and receiving reputational damage. There are a number of key areas where the MoD struggles during the tender process:

1. **Data and Process** – To contractorise an organisation, a contractor needs to understand in detail the services that the organisation delivers. The problem in defence is that, because process capture and data collection are patchy, it is difficult to accurately and numerically describe the services that are required. This can result in contractors making estimates that either cost in additional risk, potentially resulting in additional profits,

\(^{22}\) AirTanker is the joint venture appointed in 2008 to deliver RAF Voyager under the 27-year Future Strategic Tanker Aircraft contract. AirTanker is made up of Airbus Group, Rolls-Royce, Cobham, Babcock and Thales. Babcock’s responsibilities include buying and maintaining aircraft ground-support equipment and supporting the see-in, turn-around and see-off of the Voyager flights.
or miscalculate the extent of the service required, leaving them struggling to deliver profitably. Ultimately, the lack of data and process means the MoD cannot accurately match a contractor’s price to the service required and value for money cannot be evaluated effectively. This may create opportunities for a contractor to take advantage. For example, a National Audit Office report estimated that Capita’s profit margin on a defence estate transformation contract was nearly 50%, which is questionable value for money for the MoD.\(^23\) The lack of process and data also means that contracts are often based on numbers of people or hours rather than an output-based measurement. This can result in inefficiencies being contracted out and the full value to defence not being realised.

2. **Demand** – Defence is characterised by fluctuating demand based on the threat level and number of global operations. To deal with this, contracts are flexible and often include an output fluctuation of ±10%, which is absorbed by the MoD or the contractor. Outside this, the contractor can make additional charges. Although demand does fluctuate, a fixed ±10% opens the possibility of increased profit for the contractor if demand is lower than expected. There is often the perception that defence is special and demand is difficult to forecast. This is true to some extent, but much more can be done to numerically understand historical demand, planned training (often a significant portion of demand) and defence policy (which states maximum expected levels of operational demand).

3. **Deployability** – The nature of defence means that certain functions need to deploy globally for training and in response to crisis. Contractorising a deployable function often results in a minimum military force working alongside a contractor. This retains a rapidly deployable force and ensures that the military maintains skills. Calculating the right blend of contractors and military can be challenging and results in a significant dependency for the contractor on military personnel to carry out services. In some cases, logistical functions can be completely contractorised, with a contractor supplying a service in a deployed environment – such as KBR in Afghanistan. The problem is that the market for these services is relatively small, which can result in expensive single-source contracts. To resolve this, the MoD is attempting to create a competitive market by encouraging suppliers to increase deployable capability. The Single Source Procurement Framework was also introduced to cap contractor profits at 8.95% where there is no competition for contracts.\(^24\) However, there are wide-ranging exclusions to this regulatory framework, including contracts with a foreign government and contracts for the management and maintenance of land or buildings.\(^25\)

4. **Transfer of Risk** – After a military function has been contractorised, the assumption is often made that the risk of failing to deliver has been transferred from the MoD

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to the contractor. This means that if the cost of delivery is higher than expected or problems occur, the contractor will continue to honour the contract. However, this is not necessarily the case. For example, the collapse of Carillion in 2018 left many public sector projects and services at risk, with the government stepping in to bring work in-house or find new providers. CarillionAmey, which delivers facilities management at many military bases, was unaffected because it is a separate legal entity operating almost entirely independently from the parent companies. It is important at the tender stage to review contractor health in detail, including the extent of the company’s dependence on UK government spend, and to consider the use of consortiums to spread risk across a number of suppliers. This can be challenging for the MoD when there is a limited pool of suppliers focused on defence work. For example, in 2016–17, 62% of QinetiQ’s revenues were derived from contracts with the MoD. In reality, the risk of failing to deliver is never completely transferred to the contractor, and the MoD’s ability to carry out effective contract and supplier management is vital.

**Contract and Supplier Management**

After a contract has been placed, a contract management team manages the contract through its life to ensure compliance, negotiate savings and monitor risk. The aim is for a positive relationship between the MoD, contractors and sub-contractors, where all parties work closely together to increase performance and accurately match contractor reward to results on the ground. However, the challenges faced during the tender process often result in difficulties for the contract management team in the following areas:

1. **Transition** — The handover of a service to a contractor is a difficult period when experienced military and civil service personnel may be lost, and the contractor has the first opportunity to gauge the accuracy of its estimation of the scale and scope of the service. This may be the point where the contractor realises that the patchy data received during the tender process has hidden major operational issues, such as an ageing and inefficient IT system. The outcome is often a period of poor performance, where the contractor and contract management team work through the issues together and apply penalties or, if necessary, renegotiate the contract.

2. **Performance Monitoring** — Once the transition period is completed, ongoing performance monitoring is vital to hold a contractor to account. Contracts are often not managed as closely as they should be, which can result in missed savings or poor performance, such as CarillionAmey’s maintenance of service family accommodation. However, contract management teams can be handicapped by pain/gain share contracts that are overly complicated and difficult to measure, or contracts that are overly simplified and not based on outputs. Contract management teams may also lack technology based tools

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such as supplier relationship management (SRM) software, which can support the collection and analysis of performance data. In addition to SRM software, a defence-wide virtual repository of historical cost models, business cases, contracts, and contract management documents would allow teams to analyse and learn from other projects.

3. **Dependencies** – Contractorisation results in a contractor having dependencies on the MoD and other contractors. Contractor performance can be difficult to measure if poor MoD-owned equipment and infrastructure or poor performance on other contracts have prevented a contractor from carrying out a task. For example, BAE Systems may be able to achieve positive key performance indicators on the maintenance of Type 45 destroyers despite poor availability because systems maintained by Rolls-Royce have not functioned. Contractors may also be reliant on recruiting ex-forces personnel with the right skills and experience. If the MoD reduces the number of military personnel, there will be a smaller pool from which a contractor can recruit, which may affect its ability to meet outputs. The contractor must then invest in recruitment, training and security clearance, which may increase costs for the MoD in the long term.

4. **Vendor Lock-In** – One of the drivers for the cost savings associated with contractorisation is that competitive tendering and the need to generate profits exert a powerful discipline on private sector management and employees to maximise efficiency. This relies on the MoD’s ability to retender contracts regularly to ensure that incumbent suppliers are incentivised to reduce costs and improve performance as a contract progresses. However, due to the limited pool of companies involved with defence and the complexity of services being contractorised, the MoD is often locked into using one contractor on long-term, recurring contracts.

Despite the challenges across the contract lifecycle, huge pressure on the defence budget has meant there has been no reduction in the pace of contractorisation. Many of the challenges can be resolved by creating a defence-wide strategy and resolving implementation issues across tendering and contract management. The first step is to define the limits of contractorisation, then decide what should be contractorised and which core competencies of defence should be protected.
II. Defining the Limits of Contractorisation

Defining Contractorisation

IN THIS PAPER, contractorisation is defined as the provision of a service by an external contractor that was previously provided by military or civil service personnel. However, contractorisation is often not clear cut and, as shown in Figure 1, there are different levels of contractorisation depending on the scale of the task and the responsibility taken on by a contractor.

**Figure 1: Different Levels of Contractorisation**

<table>
<thead>
<tr>
<th>Fully Government Provided</th>
<th>Partial Contractorisation</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Government-managed and government-staffed organisation</td>
<td>• A limited number of roles are contractorised within a government-managed organisation; the roles could be temporary (manpower substitution)</td>
</tr>
<tr>
<td>• For example, the operation of weapons and platforms on offensive deployments</td>
<td>• For example, DE&amp;S has a Commercial Resourcing Solution partner to provide commercial staff to temporarily fill vacancies</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Specific Roles</th>
<th>Specific Activities</th>
<th>Fully Contracted</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Specific measurable activities carried out by a contractor for a government-managed organisation</td>
<td>• A contractor is responsible for delivering a significant and bounded service possibly with support from subcontractors and government assets</td>
<td>• Contract is output based and monitored by a contract management team</td>
</tr>
<tr>
<td>• For example, Amec Foster Wheeler provides nuclear regulatory services to the Defence Safety Authority and Dstl regularly contracts out packages of research</td>
<td>• For example CarillionAmey delivers facility management at many bases</td>
<td></td>
</tr>
</tbody>
</table>

Source: The author.

The switch from partial to full contractorisation occurs when a significant part of the management and delivery of an organisation’s outputs moves from government to a contractor. However, full contractorisation will always require touchpoints and dependencies with government...
teams and potentially other contractors. In defence, it is often necessary for contractors to work with Government Furnished Assets (GFAs). This could include working with equipment and infrastructure owned by the MoD or embedding a team of military personnel within the contractor team to maintain deployable skills.

As the level of contractorisation increases, the importance of the government contract management team grows. This team will contribute to running a tender, monitor contractor performance using key performance indicators, and negotiate any changes to the contract. This role is vitally important to ensure that contractorisation delivers the expected value to defence throughout the life of the contract.

Inherently Governmental Functions

The term ‘inherently governmental’ comes from the US and refers to a function so intimately related to the public interest that it must be undertaken by government employees. The term was developed following recognition that some contractorisation had resulted in the loss of institutional memory and a lack of clarity over whether decisions were being made in the public interest or in the interest of the contractors performing the work. The US Department of Defense is required to minimise reliance on contractors performing functions closely associated with inherently governmental functions and to ensure institutional knowledge is maintained by personnel with the training and experience to oversee contractor effort.

The UK MoD recognises the need to maintain its status as an intelligent or expert customer, and the term ‘Crown authority’ is used to describe functions or roles reserved for Crown servants. However, despite extensive contractorisation of defence in the UK, there has been little explicit discussion of what responsibilities the government cannot contractorise.

The state is the only entity with the exclusive right to use, threaten or authorise physical force domestically and internationally. To effectively enforce this right, the state must retain the

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capability to maintain control over the core functions of the MoD’s mission and operations. At a high level, this could be defined in the UK by four inherently governmental functions:

1. **Policy and Requirements** – A state must be able to review and approve the policy and requirements that define how military force is developed and used. The Head Office supports the Defence Board in making strategic and financial decisions and the Front Line Commands in delivering the strategy with the resources at their disposal. Policy and requirement approval roles within the Head Office and Front Line Commands are inherently governmental. However, it could be argued that certain support roles are not inherently governmental and could be contractorised if deemed cost effective. This could include the definition and analysis of policy or requirements, which would then be reviewed and approved by government employees. This requires careful management and the separation of client and supply-side contractors to ensure a contractor does not make recommendations that may favour it.

2. **Direct Participation in Hostilities** – A state must control and be directly accountable for the actions of its military forces against hostile forces. The Red Cross defines direct participation as acts of war that by their nature or purpose are likely to cause actual harm to the personnel and equipment of the enemy armed forces. The narrow interpretation of this definition assumes that preparing or enabling someone else to directly participate in hostilities is not included and that it is only the individuals personally carrying out hostile acts who are participating directly. The interconnected and data-driven nature of modern warfare means that direct participation needs to be defined more broadly as both the operation of weapons and platforms and the direct support of operations through planning and intelligence gathering. The use of private security companies is an exception and includes companies that provide armed defensive security services for the protection of personnel and assets worldwide (but not in the UK). The MoD does not use contractors for any armed offensive operations which are considered inherently governmental.

3. **Enforcing Military Discipline** – A state must have control over its military forces and, if required, exercise immediate and effective justice to maintain control. Commanding officers are vested with statutory powers that allow them to enforce military discipline. The discipline is carried out by the service police, who, for this reason, are inherently governmental.

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governmental. However, there are several support roles that could be contractorised if this is cost effective.

4. **Committing Public Expenditure** – A state must maintain control over how taxpayers’ money is spent and ensure its military force is adequately equipped. Acquiring the equipment and services that support a modern military force is vital to ensure it can carry out its missions and operations. The procurement organisations within the MoD (Defence Equipment and Support and Information Systems and Services – DE&S and ISS) are already partially contractorised, and it is important to ensure there is a split between inherently governmental roles and support roles that can be carried out by a contractor. Decision-making roles that sign off requirements, award contracts and delegate spend could be classified as inherently governmental. Support roles could include market research, developing cost models and assessing contracts. The ability to spend can be delegated to a contractor, although overall accountability for this spend must remain governmental. Ultimately, government employees must retain decision-making power and be fully accountable for both acquisitions and holding a supplier to account through the life of a contract.

As well as the four inherently governmental areas, there are military roles that, although not inherently governmental, are carried out in hostile environments. For example, the logistics personnel who set up and run an airport in hostile territory at the start of an operation would be required to carry out their primary duty and defend the airport from attack if required. If the operation became enduring, it is likely that, after a period of time, the airport would be considered a secure environment within hostile territory, as with Camp Bastion during Operation **Herrick** in Afghanistan. It could be difficult and expensive to find contractors to carry out these logistical roles in the initial stages of an operation, but they would be an option when the area is considered secure.

The functions most suited to contractorisation are process driven, carried out in a secure environment, and contain skillsets readily found in the commercial sector, such as facilities management, logistics and certain types of equipment maintenance. Figure 2 summarises criteria for judging whether a government organisation is inherently governmental, or could be partially or fully contractorised.
Figure 2: Criteria for Inherently Governmental, Partial or Full Contractorisation

<table>
<thead>
<tr>
<th>Inherently Governmental</th>
<th>Could be Partially Contractorised</th>
<th>Could be Fully Contractorised</th>
</tr>
</thead>
<tbody>
<tr>
<td>• The majority of roles either set policy and requirements, directly participate in hostilities, enforce military discipline or commit public expenditure</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Roles could be carried out in a hostile environment</td>
<td></td>
<td></td>
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<tr>
<td>• There are limited commercial providers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Organisation is inherently governmental but there are certain roles that are not</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Organisation is not inherently governmental but there are limited commercial providers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Organisation is not inherently governmental</td>
<td></td>
<td></td>
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<tr>
<td>• Many cost-effective commercial providers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Mainly provided in the UK or in a secure overseas environment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Contractor could be supported by GFAs that provide certain capabilities</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: The author.

Partial Contractorisation

If an organisation is inherently governmental or could be fully contractorised, the extent of contractorisation that is possible is relatively clear cut. However, if an organisation could be partially contractorised (because it is inherently governmental, but includes roles that are not), the possibilities for contractorisation are less clear.

Information Systems and Services (ISS) is an example of an inherently governmental organisation that commits public expenditure but which is already partially contractorised and uses a number of contractors for day-to-day operations. Decision-making roles within ISS that review and approve requirements and sign contracts are inherently governmental and must be staffed by government employees. However, there are many support roles or activities that are contractorised at ISS in the following broad areas:

1. **Process-Driven Operations** – For every procurement, there are a number of business-as-usual, process-driven activities, such as requirements setting, market testing, technical solution development, writing a commercial strategy and running a tender. These are all activities that a contractor could carry out if the review and approval of documents and decisions remained governmental. Government employees must be involved enough to fully understand the decisions that are being made.

2. **Advice Provision** – Every organisation needs to review strategy and cope with change, such as new regulations that need to be analysed and implemented. This creates a brief surge in demand for information gathering, options’ development and policy implementation that would place significant strain on government employees with full-time roles. Contractorisation of advice provision and implementation roles is an effective way to deal with cyclical demand if the final decisions remained under government control.
3. **Back Office Functions** – This includes support that is not directly related to core functional operations (procurement and contract management in the case of ISS), such as HR, IT, finance, and facilities management. Back office functions have already been readily contractorised across the MoD and are often the least controversial and most cost effective to contractorise. However, contract management is important and governmental oversight is required to ensure that the contractor delivers the right outputs at the right cost.

Partial contractorisation in these areas is driven by the need to achieve cost savings and maintain outputs at an acceptable risk level. There is a balance between ensuring there are enough government staff to review work and approve decisions effectively and ensuring cost savings are achieved.

Some organisations, while not inherently governmental, are specialist, resulting in a lack of commercial providers in the market. For example, research and training that is very specific to defence and not found in the commercial sector. In this situation, a market can be created if the government encourages companies to develop certain competencies by providing investment or promising future work. This strategy could be pursued if deemed cost effective in the long term.
III. The Extent and Future of Contractorisation

At a high level, the defence enterprise can be mapped against the criteria for inherently governmental, partial or full contractorisation, and any contractorisation that has already occurred. Figure 3 (see page 20) is based on the defence operating model and creates a high-level view of where contractorisation has occurred and where further contractorisation could take place.\(^{36}\)

Direct

The Direct part of the defence operating model is made up of the Defence Board and Head Office, which direct policy, and the contribution of defence to national security at the strategic level. This is fundamentally an inherently governmental function.

- **Defence Board** – The board, made up of senior decision-makers, is inherently governmental.
- **Head Office** – Senior decision-making roles at Head Office are inherently governmental. However, it is likely that demand for work at Head Office is cyclical, in line with the production of documents such as the SDSR. It could be cost effective to have a streamlined inherently governmental workforce supported by contractors carrying out support roles or specific packages of research during surges. A contractorisation plan for Head Office would need to be created to ensure that inherently governmental roles and functions were identified and protected and value for money was achieved.

Enable

The Enable part of the defence operating model provides supporting services to ensure the defence enterprise works properly. The majority of the functions within Enable are not inherently governmental, although a limiting factor for contractorisation might be the number of commercial providers for some of the more defence-specific functions.

- **Ministry of Defence Police (MDP)** – The MDP provides investigatory services and acts as an armed force to guard sensitive MoD sites in the UK, such as atomic weapons sites at Aldermaston and Burghfield.\(^{37}\) The UK Firearms Act does not currently allow private

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security guards to carry a firearm,\(^{38}\) ruling out contractorisation of armed guarding duties. However, unarmed support roles could be contractorised. If the Firearms Act were relaxed to allow security guards from firms such as G4S to be armed in the UK (as they are in Iraq and Afghanistan),\(^{39}\) it would be difficult to argue against MDP armed guarding duties being contractorised.

- **Defence Safety Authority (DSA)** – The DSA regulates safety across defence, investigates accidents and is the defence authority for health, safety and environmental protection. There has been partial contractorisation. For example, Amec Foster Wheeler provides independent regulatory services for the Defence Nuclear Safety Regulator, which is part of the DSA.\(^ {40}\) A review of the DSA organisation would be required to understand if further contractorisation could create savings, depending on the number of commercial providers for some of the more defence-specific services.

- **Defence Science and Technology Laboratory (Dstl)** – Dstl carries out research to ensure science and technology contribute to defence decisions. Dstl is partially contractorised and uses approximately half of its budget to contract research to industry and academia.\(^ {41}\) There are defence research areas such as biological threats where cost-effective commercial providers may be limited. However, Dstl is constantly reviewing its partial contractorisation model and intends to increase the work contracted out.

- **Defence Business Services (DBS)** – DBS delivers HR, payroll, finance, information and vetting services across the MoD – all competencies found in the private sector. In 2012, DBS was partially contractorised, with Serco and Accenture brought in as management partners to transform the business over four years.\(^ {42}\) The contract was not extended and the MoD is looking at options to modernise processes and increase efficiency. Fully contractorising the DBS could contribute towards a 30% reduction in MoD civilian staff by 2020 – the target announced in the NSS and SDSR 2015.\(^ {43}\)

- **Defence Infrastructure Organisation (DIO)** – The DIO manages the building and maintenance of the defence estate, which are also competencies readily found in the private sector. In 2014, it was partially contractorised, with Capita, AECOM and PA

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Consulting brought in as strategic business partners to improve the DIO over ten years.\textsuperscript{44} This contract has been running alongside an operating model transformation, with infrastructure decisions and funding delegated to the Front Line Commands and the DIO acting as an expert estate manager and source of information and advice.\textsuperscript{45} When the strategic business partner contract and operating model transformation is completed, the possibility of fully contractorising the DIO could be reviewed.

**Acquire**

The Acquire part of the defence operating model buys equipment, logistical support and information services to deliver military capability. The organisations within Acquire are inherently governmental, although partial contractorisation is possible if senior decision-making roles are filled by government employees and contractors perform supporting roles.

- **Defence Equipment and Support (DE&S)** – DE&S works with industry to buy and support all the equipment and services that the Front Line Commands need. DE&S is already partially contractorised, with a significant part of the DE&S budget spent on contractor staff.\textsuperscript{46} In 2011, the Materiel Strategy programme was launched to assess the possibility of either a fully contractorised Government-Owned, Contractor-Operated (GOCO) model or a transformed DE&S+ remaining in the public sector.\textsuperscript{47} The GOCO option was halted in 2013 after only one commercial consortium was left in the competition. As part of DE&S+ and ongoing transformation it may be pertinent to clearly review which roles are inherently governmental and which can be contractorised.

- **Information Systems and Services (ISS)** – ISS is part of Joint Forces Command and is responsible for setting strategy and managing, acquiring and delivering information and communications technology (ICT) across defence, including defensive cyber operations. ISS is partially contractorised and further contractorisation should be accompanied by a review of which roles are inherently governmental.


Figure 3: Contractorisation Landscape

Source: The author.
Generate and Develop

The Front Line Commands have the main responsibility for developing and generating the units and formations that deploy on operations. Each Front Line Command includes a number of roles that can be split at a high level into those involving direct participation in hostilities, which are inherently governmental, and support roles, which are generally not.

- **Direct Participation in Hostilities** – This includes roles involving the operation of weapons and platforms and the direct support of operations through planning and intelligence gathering. These roles are at the core of the MoD’s mission and operations and are likely to always be inherently governmental.

- **Support** – This includes roles that are not normally directly related to hostilities, such as logistics, engineering and administration. Many of these roles are readily available in the commercial sector and already have some level of contractorisation. The challenge with full contractorisation is that many support roles are delivered in the UK and in the deployed space. Support roles carried out in a hostile environment may not be cost effective to contractorise. This means that, to move towards full contractorisation, a Whole Force Approach deployment model is required whereby high-readiness regular military personnel initially carry out support functions and reservists and contractors take over most tasks once bases have been secured, as shown in Figure 4.

**Figure 4: Whole Force Approach Deployment Model**

The Whole Force Deployment model requires the calculation of the minimum military force that can initially deploy to every deployment in the most testing defence policy scenarios while continuing to meet harmony guidelines. Contractors would provide comprehensive services in the UK, on fixed overseas bases and in the deployed space for enduring operations, supported by the minimum military force retaining skills for hostile deployments. This model works well when fighting against a low-technology, asymmetric enemy in locations such as Iraq and Afghanistan. In this type of environment, deployed bases can be made secure enough for contractors to agree to work on them. However, in possible future war-fighting scenarios, a high-technology nation state may have the surveillance and precision strike capabilities to put any land base at serious risk. The assumption that forward bases can be secured for contractor staff might not hold true. Contractorisation of support roles in the deployed space needs to be carefully managed to ensure that cost effectiveness is balanced against operational risk.

The Sponsored Reserves model enables contractor staff to deliver a service to the military or commercially in peacetime, and during operations to change into military uniform and operate under military terms and conditions. Further research is required to understand the cost effectiveness of these contractor deployment models.

There are some support functions that are inherently governmental, such as policy and requirements approval and enforcing military discipline. These functions cannot be fully contractorised, but certain roles could be contractorised if deemed cost effective. There are probably a limited number of commercial providers that could deliver military medical functions and certain areas of military-specific training.

Operate

The operation of military forces abroad is core to the MoD’s mission and operations and is inherently governmental. Permanent Joint Headquarters commands joint and combined military operations and the Directorate of Special Forces commands discrete Special Forces operations. It is difficult to see either organisation being contractorised, other than back office functions such as facilities management, IT and HR.

Recommendations

Although significant contractorisation has occurred across defence, many more opportunities remain. Due to the current strain on the defence budget, contractorisation may be seen as a quick way to reduce costs and maintain outputs. Ensuring that the full value of contractorisation to defence is realised while keeping operational risks as low as possible is challenging. The following recommendations, which span strategy and implementation, could help the MoD achieve the desired outcomes:

1. **Strategy** – Contractorisation is not currently informed by a defence-wide strategy. To develop a strategy, inherently governmental functions must first be defined in the context of defence. Based on this, a high-level view of historical contractorisation and opportunities for future contractorisation can be developed. The opportunities that offer the greatest potential for savings and the lowest risk to operations can then be pursued. Current contracts could also be renegotiated to create a more integrated contractual landscape. This strategic process will ensure that the greatest value is achieved and inherently governmental functions are protected. The recommendations that follow are focused on improving the implementation of contractorisation.

2. **Process** – Accurate operational processes and data are required to numerically describe the services that are being contractorised. Often the detail required is lacking, resulting in contractors estimating the scale of the service and costing in additional risk. Before contractorisation occurs, there must be significant effort to numerically understand operational processes, historical demand, planned training (which often makes up a significant portion of demand) and defence policy (which states maximum expected levels of operational demand). This will ensure the scale and scope of services are fully understood so that they can be effectively communicated to potential contractors.

3. **Performance Monitoring** – Contract management teams play a vital role in reducing costs and improving performance but can be handicapped by poorly designed performance indicators. Performance indicators must be designed with careful consideration of operational processes, demand data and dependencies. They need to evolve over the contract’s life to take into account expected transition difficulties and the ability of the contractor to reduce costs and improve performance through the life of the contract. Poorly designed incentives can result in unexpected and undesired contractor behaviour; they must be modelled and developed with the contractor to achieve the desired outputs. Contract management teams may also benefit from access to supplier relationship management software, which can support the collection and analysis of performance data and spend.

4. **Benefits** – After a contract has been let, the benefits forecast in the original business case can be forgotten. To understand whether a contract has achieved the desired value it needs to be compared with the original benefit assumptions. This must become part of the contract management process to ensure there is a feedback loop that can improve
procurement processes. This feedback loop should be incorporated into the training of commercial teams.

5. **Technology** – Contractorisation currently occurs in silos across the MoD, and it is difficult for procurement and contract management teams to learn from other projects. A virtual repository of historical cost models, business cases, contracts and contract management documents would allow teams to track and analyse other projects. This would facilitate a collaborative approach across the MoD and ensure that innovative contractual models can be built on historical successes and challenges.

6. **People** – The skills and experience of the people that run tender processes and manage contracts are incredibly important. Training must include the analysis of historical contracts that achieved the desired outcomes and those that had problems. Standardised procurement and contract management methods must be constantly updated to cover changes in best practice, and this could be facilitated by an up-to-date virtual repository of contractual documents (covered in the Technology recommendation).

Many of these recommendations are relatively simple and inexpensive to implement and could result in significantly improved procurement and contract management practices in the long term. This is vital to ensure that contractorisation is carried out in an effective manner and does not affect core military capability.

This paper defines at a high level why a defence-wide contractorisation strategy is desperately needed and how the strategy could be developed and implemented to underpin the Whole Force Approach. It is vitally important that the MoD focuses on contractorisation strategy and implementation. This will drive best practice and ensure that inherently governmental functions are protected, and the full benefit of cost savings are achieved.
About the Author

Jay Edwards works with the UK Ministry of Defence to develop efficient and effective operating models. He previously worked at BAE Systems CORDA in Farnborough, the NATO Communications and Information Agency in The Hague and was a Visiting Fellow in the International Security Programme of Chatham House in London.