



Public procurement: small businesses and savings

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This Standard Note has been superseded. For the latest Standard Note on procurement, including information on small businesses and savings, please see [here](#) (Public Procurement SN/EP/6029).

The public sector's general approach to procurement is to seek value for money. In 2011/12, the public sector spent a total of £227 billion on procurement of goods and services (including capital assets); this accounted for 33% of total managed expenditure.

The Government is attempting to centralise much of its procurement in order to achieve savings through economies of scale and is renegotiating some contracts to achieve more favourable costs. They state that they have achieved savings of £3.8bn in relation to central government procurement in 2012/13, consisting of £1.0bn saved from the centralisation of procurement for common goods and services, £0.8bn from the central renegotiation of large government contracts and £1.9bn from limiting expenditure on marketing and advertising, consultants and temporary agency staff.

The Government has also pledged to promote small businesses through its spend on procured goods and services. It has set an "aspirational target" that 25% of central government contracts should be awarded to small and medium sized enterprises (SMEs) by 2015. In 2011/12 around 16% of spending was with SMEs. In order to encourage SMEs to bid in public procurement exercises, the Government has put various measures in place aimed at making it easier for small and medium-sized businesses to do business with government, for example the creation of [Contracts Finder](#), a website that provides free access to public sector contract opportunities worth over £10,000; the abolition of Pre-Qualification Questionnaires (PQQs) for contracts under £100,000 in value; the appointment of a Crown Representative for SMEs; and the introduction of a Mystery Shopper service to suppliers to raise concerns about public procurements, including issues relating to unfair practices in the supply chain.

This note briefly sets out the European and domestic public procurement rules before summarising Government efforts to use its procurement spend to support small businesses.

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It also sets out reforms to procurement processes which have aimed to drive down costs.

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1 Introduction

The public sector's general approach to procurement is to seek value for money.¹ This is generally done through competitive tender. Public procurement for certain goods and services above certain monetary thresholds has to follow EU rules.

In 2011/12, the public sector spent a total of £227 billion on procurement of goods and services (including capital assets); this accounted for 33% of total managed expenditure.² It is often suggested that the Government could use this considerable spending power to pursue a variety of other public policy aims, such as environmental policy and supporting small and medium sized enterprises (SMEs). Certain policy aims can be considered and incorporated into public procurement exercises as long as this is compatible with EU rules and national law; they must not prevent procurement exercises from being non-discriminatory and transparent, for example.

Value for money for the public purse remains an imperative in procurement exercises. The Government is attempting to rationalise aspects of its procurement to achieve savings.

2 The legal framework

The Treasury document, *Managing Public Money* sets out what is meant by "value for money" in procurement exercises:

It means securing the best mix of quality and effectiveness for the least outlay over the period of use of the goods or services bought. It is not about minimising upfront prices.³

The EU public procurement directives regulate the publication and organisation of tender procedures for many public sector contracts over minimum thresholds. The rules are intended to ensure transparency and non-discrimination with a menu of procedures for

¹ HM Treasury, *Managing Public Money*

² HM Treasury, *Public spending statistics: April 2013*, Table 9

³ HM Treasury, *Managing Public Money*, Annex 4.4

procurement exercises leading to outcomes which represent good value for money. The EU directives are available on the Commission's website [here](#) along with the relevant thresholds (which were last updated in 2012). The two main Directives were adopted on 31 March 2004. In the UK, the Directives were implemented into national law by the following regulations which came into force on 31 January 2006:

- Public authorities (the State, regional and local authorities and other public bodies): [The Public Contracts Regulations 2006](#) (SI 2006 No.5);
- Utilities (i.e. certain operators in the water, energy, transport sectors): [The Utilities Contracts Regulations 2006](#) (SI 2006 No.6).

The document [An Introduction to Public Procurement](#) sets out the basic principles of public procurement and the stages which procurements must go through to be within the relevant EU and UK regulations, in more detail. Further background information about the procurement rules is available in the Library Standard Note, SN/EP/6029, [Public Procurement](#).

3 Public Procurement and Small and Medium Sized Enterprises

3.1 Coalition Government policy on SME procurement

The Coalition's [Programme for Government](#), published in May 2010, stated that the Government would "promote small business procurement" by

... introducing an aspiration that 25% of government contracts should be awarded to small and medium-sized businesses and by publishing government tenders in full online and free of charge.⁴

The main changes made by the Coalition Government to procurement processes were announced on 11 February 2011 and have been summarised by the Cabinet Office as follows:

- The launch of a [Contracts Finder website](#). The new online facility, which is available from today, will become the place to find public sector contracting opportunities over £10,000 and will make the Government's procurement process totally transparent. From now on, all organisations need to do is to specify which contracts they are interested in and details will be emailed free of charge.
- The appointment of Stephen Allott as a new Crown Commercial Representative (CCR) for SMEs. His task will be to build a more strategic dialogue between HM Government and smaller suppliers – giving those suppliers a strong voice at the top table.
- The launch of SME (Small Medium Enterprise) product surgeries. These events will be led by the new CCR and will give SMEs the opportunity to pitch innovative products and services direct to a panel of senior procurement and operational professionals from central government and the wider public sector.
- A completely new approach to assessing companies and organisations who want to do business with Government, so that SMEs are not disadvantaged including:
 - Seeking to eliminate PQQs (Pre-Qualification Questionnaires) for all central government procurements under £100,000. This represents a radical change in the way pre-qualification is carried out and means that from now on

⁴ HM Government, [Programme for Government](#), May 2011, p10

procurers will be free to choose the best route to market for their individual circumstances.

- Allowing firms to submit their prequalification data once for all procurements in common commodities. This will put an end to companies having to submit the same data time and time again, saving time and money for the suppliers and for government.
- Publication of the findings of the Cabinet Office's LEAN Review into procurement processes. This will show the Government is doing all it can to reduce waste, tackle bureaucracy and lower the cost of doing business with government.⁵

An interchange programme to allow civil servants to get commercial experience and bring private sector expertise into the public sector was also launched in February 2011, as was a Mystery Shopper exercise and SME panels to allow small businesses to contact the Government with details of tenders that they find difficult to understand.⁶

In March 2012 the Cabinet Office minister, Francis Maude, [restated](#) the Government's aim to increase SME procurement.⁷ A further set of initiatives to encourage SME procurement was announced:

- **New commitments from large private sector players.** Nine companies: Hewlett Packard, Airwave, Amey, Balfour Beatty, CapGemini, Capita, Level 3, Logica and Serco are the first to sign up to publish their government subcontracting opportunities on the Government's searchable and transparent website, Contracts Finder. This gives SMEs more visibility than ever before on the government subcontracting work available.
- **A new approach to IT contracts** – in future, Government IT contracts will be more flexible, starting with two areas (application software and infrastructure IT). The Government is introducing set breakpoints in IT contracts so there is less money locked into large lengthy contracts. The Government will look to disaggregate future contracts and deliver flexible, cheaper solutions. This opens up opportunities for SMEs and reduces the cost to taxpayers.
- **Prompter payment for SMEs.** Timely access to cash is critical for the survival of many SMEs. The Minister will announce that new ways of paying SMEs are being explored to ensure SMEs within the supply chain receive payment at the same time as the prime suppliers. This will include rolling out Project Bank Accounts, which are already being used successfully in the construction sector to sectors such as defence and considering the role of structured finance to facilitate faster payments.
- **Greater transparency.** Departments will be judged by smaller businesses and given a star rating to show how effective they are at working with smaller players. The first department to be rated by smaller businesses will be the Cabinet Office in May.
- **Extending the investigative Mystery Shopper service.** Following the success of the Cabinet Office's Mystery Shopper service where SMEs can complain about procurements and trigger an investigation, the Cabinet Office will now investigate complaints about unfair practices in the supply chain of government contracts. By

⁵ Cabinet Office, [Government opens up contracts to small business](#), 11 February 2011

⁶ *Ibid*

⁷ Cabinet Office, *SME procurement event – Francis Maude speech*, 9 March 2012

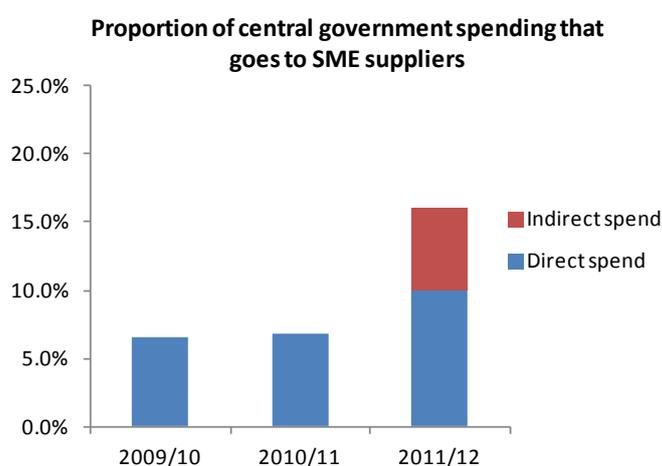
mid-February 2012 the existing system had received 151 cases, of which 111 had been closed with 75% of them resulting in a positive outcome.

- **Better dialogue between Government and smaller businesses.** From April, a new online tool will help government buyers to engage earlier with SMEs by allowing them to put informal postings about what they need to buy in future online and for SMEs to respond and explain what they can offer.⁸

Further information is available from the government's webpage on '[Making sure government gets full value from small and medium-sized enterprises](#)'

3.2 Monitoring progress

The government's "aspirational target" is interpreted to mean that 25% central government procurement spend should be with SMEs by 2015 – this includes both direct spend with SMEs and indirect spend (where government suppliers are themselves supplied by SMEs, for example). SMEs are enterprises with less than 250 staff and with either less than a certain level of turnover or less than a certain amount on their balance sheet.⁹



In 2009/10, 6.5% of government departmental (procurement) spend was directly with SMEs – this increased to 6.8% in 2010/11 and 10.0% in 2011/12. In addition in 2011/12, an indicative estimate suggests that 6% of central government procurement spend was indirectly with SMEs, based on figures from major government suppliers – giving a total of around 16% of spend going to SMEs in 2011/12, against the 25% target for 2015.

The proportion of direct spending that is with SMEs varies by department, as shown in the table. Note that this data is for direct spending only, so cannot be compared directly with the 25% target.

⁸ Cabinet Office, *A better deal for small businesses*, 9 March 2012

⁹ European Commission, *Small and medium-sized enterprises (SMEs): What is an SME?*

Proportion of central government spend with suppliers that goes directly to SMEs - does not include indirect spending

Department	2009/10	2010/11	2011/12
Business, Innovation and Skills	22%	25%	27%
Communities and Local Government	14%	12%	21%
Cabinet Office	8%	7%	12%
Culture Media and Sport	27%	26%	18%
Energy and Climate Change	1%	1%	0%
Environment, Food and Rural Affairs	11%	19%	16%
Education	25%	24%	18%
International Development	-	39%	31%
Transport	3%	2%	3%
Health	18%	7%	9%
Work and Pensions	12%	15%	11%
Foreign and Commonwealth Office ²	-	6%	5%
HM Revenue and Customs	11%	0%	0%
HM Treasury	14%	13%	6%
Home Office	2%	7%	6%
Defence ³	4%	3%	5%
Justice	9%	9%	34%
Total	6.5%	6.8%	10.0%

Source: Cabinet Office, *Direct and Indirect Spend with SMEs* (Feb 2013)

Notes:

1. Figures are generally for central government departments and their arms length bodies.
2. Data for FCO is based on spend with UK based SMEs only, understating the total.
3. Figures for the Ministry of Defence are for the core department only, excluding arms-length bodies.

3.3 Labour Government policy on SME procurement

The Labour Government also aimed to encourage SME procurement. Most recently, in the 2008 Budget, the then Chancellor of the Exchequer invited Anne Glover to lead an advisory committee on action to reduce the barriers small and medium sized firms faced when competing for public sector contracts.

The [Glover Report](#) was published in November 2008.¹⁰ The Committee considered the practicality of an aspirational goal of small and medium enterprises winning 30 per cent (or more) of all public sector business. The Committee stated that the “strong view” of SMEs consulted was that, “...the overriding priority for Government was to tackle the three issues of transparency, simplicity, and making procurement strategic rather than establishing a target”.¹¹ The Committee concluded that a goal would not be effective, but that there was merit in requiring public sector bodies to report on the value of contract spend with SMEs in order for the Government to monitor the success of its policies and to provide evidence for future policy decisions. The Committee made a total of twelve recommendations, under the headings of “transparency”, “simplicity”, “strategic procurement” and “measurement”.

The 2008 Pre-Budget Report announced that the Government accepted all the Glover Report’s recommendations. It stated that the Government would:

¹⁰ [Accelerating the SME economic engine: through transparent, simple and strategic procurement](#), November 2008

¹¹ *Ibid*, p3

...advertise Government contracts worth more than £20,000 in a single free online portal, it will introduce measures to reduce bureaucracy and will make opportunities more transparent for small businesses. In addition, it will standardise qualification criteria and encourage innovation by increasingly specifying outcomes rather than prescribing solutions. It will also help SMEs get a fair deal when they are sub-contractors.¹²

The March 2010 Budget also announced a number of measures to help small and medium sized firms gain public procurement contracts. It said:

Based on current spending levels, if the whole public sector increased the amount of procurement that went to SMEs by 15 per cent throughout the supply chain, this would mean up to an extra £15 billion of business for SMEs. The Government will deliver this change in central departments by agreeing departmental targets to increase the proportion of central government procurement spend that goes to SMEs by 15 per cent throughout the supply chain. This summer, the Government will publish for the first time the level of spend that goes to SMEs, which will be used as a baseline for these targets.

The increase in central government spend going to SMEs will be achieved by agreeing targets with departments and continuing to deliver on the Glover Committee's recommendations:

- requiring departments to publish contracting and sub-contracting opportunities through a single portal that suppliers will be able to access free of charge from December 2010 (an SME has been awarded the sub-contract for the portal, which will be hosted on businesslink.gov.uk);
- challenging departments to make more use of SMEs, including flagging contract opportunities as SME-friendly and increasing training to institutionalise SME-friendly procurement practices;
- providing direct support to SMEs through the free-to-use training package, *Winning the Contract*; and
- working with main contractors to open up supply chains to SMEs.

To build further on recent prompt payment success, all central government departments will now aim to pay 80 per cent of all undisputed invoices within five days and will explore the option of moving to immediate payment, in time, through electronic invoicing for all suppliers. The Government will also encourage all NHS Trusts and local authorities to publish their prompt payment performance data on data.gov.uk. In addition, to ensure the benefits of procurement and payment improvements are shared with small businesses, all central government departments will be required to include a clause in their contracts with suppliers to ensure that suppliers pay their subcontractors within 30 days.¹³

3.4 EU Commission review of procurement rules

The European Commission launched a [review](#) of the EU's public procurement rules in January 2011. Amongst other issues, this considered whether changes were required to allow governments to use procurement exercises for a variety of purposes, including encouraging SME growth. The consultation paper asked:

¹² HM Treasury, *Pre-Budget Report 2008*, para 4.36

¹³ HM Treasury, March 2010 Budget

- How can we reduce red tape for economic operators, notably SMEs? How can bidding across intra-European borders be facilitated?

The UK Government's [response](#) stated that more could be done to simplify the EU rules:

The vast majority of procurement contracts continue to be awarded to domestic firms and many SMEs find that poor information, bureaucratic barriers and a false assumption that bigger is always better prevent them from winning procurement contracts.

It continued by stating that the Government would support a solution which would require submission and verification of evidence only by short-listed candidates or the winning bidder. They also agreed that administrative burdens could be alleviated by self-declarations. The also noted that:

...excessively strict turnover requirements for proving financial capacity are problematic for SMEs, but would be concerned that if a maximum ratio for turnover to contract value were to be set, that buyers would default to the maximum even if it was not actually proportionate (question 51). As a result, we would not want to see this included in legislation. UK businesses have complained that disproportionate turnover requirements in relation to contract value have meant that they are unable to proceed past the PQQ stage. This practice creates a barrier to potential new suppliers and can block innovation...¹⁴

The UK Government agreed with the Commission that a procurement quota where a percentage of contracts were reserved exclusively for SMEs would be in contradiction with the principle of equal treatment of tenderers, and would undermine the principle of value for money.

The European Commission published its proposals for revised public procurement directives in December 2011. They include a maximum ratio for turnover to contract value, the use of self-declarations and encouragement for contracting authorities to split large contracts into lots. The Commission explained:

Many companies, in particular, SMEs, complain that access to public contracts remains difficult in practice, because of high administrative burdens and sometimes disproportionate requirements set up by contracting authorities. Among the measures proposed to remedy this problem, the most important is the obligation for contracting authorities to accept self-declarations as a first step; only the winning bidder must then supply the documentary evidence for the selection criteria; documents which have already been submitted to the same contracting authority within the past four years and which are still valid shall not have to be re-submitted. This will particularly benefit SMEs, for whom the costs and time of supplying the documents is often a serious obstacle to participation in public tender procedures. Furthermore, the list of possible selection criteria is made exhaustive; yearly turnover requirements may not exceed three times the estimated contract value. This will hinder contracting authorities from imposing exaggerated turnover requirements which automatically exclude SMEs from participating in the procedure. Contracting authorities will be encouraged to split contracts into lots allowing for the participation of more bidders and will have to specifically explain when not doing so. Finally, Member States may foresee direct payments to subcontractors, so that these subcontractors – which are often SMEs –

¹⁴ Cabinet Office, [United Kingdom response to the European Commission Green paper on the modernisation of EU public procurement policy](#)

get paid quicker and do not suffer from bad payment practice of the prime contractors.¹⁵

The proposals will be considered by the Council and the European Parliament for negotiation and adoption.

4 Achieving savings through procurement

4.1 Spending on public sector procurement

The figures for the total public sector spend on procurement are available from HM Treasury's public spending statistics publications. In 2011/12 spend on procurement of goods and services amounted to £227 billion, 33% of total public sector spending.

Public sector expenditure on procurement, 2007-08 to 2011-12

£billion

	2007-08	2008-09	2009-10	2010-11	2011-12
	outturn	outturn	outturn	outturn	outturn
Gross current procurement	172.8	185.7	193.8	188.1	188.8
Gross capital procurement	39.2	42.3	44.9	42.5	37.9
Total procurement spend	212.0	228.1	238.7	230.6	226.7

Source: HM Treasury, Public spending statistics: April 2013, Table 9

4.2 The Coalition Government and procurement savings

The Coalition Government has made achieving savings through procurement a key part of its strategy to reduce spending. The Government appointed Sir Philip Green to review Government Efficiency. His key findings, published in August 2010, were as follows:

The Government is failing to leverage both its credit rating and its scale

- Basic commodities are bought at significantly different prices across Government departments.
- Multiple contracts have been signed with some major suppliers by different departments at different prices.
- The Government is the largest tenant/owner in the country, yet the use and management of space is wholly inefficient.
- Expensive IT services are contracted for too long with no flexibility.¹⁶

Sir Philip found that Government acted as a series of independent departments rather than as one organisation, and that there had been no mandate for centralised procurement.

In addition, on 1 November 2010, Francis Maude, Minister at the Cabinet Office, announced a "Lean Review", to "uncover wasteful practices and unnecessary complexity in the procurement process and to suggest actions to rectify them". The Review was published in February 2011. It found that there were:

¹⁵ European Commission, *Commission proposals to modernise the European public procurement market – Frequently Asked Questions*, 20 December 2011

¹⁶ *Efficiency Review by Sir Philip Green*, August 2010

...significant opportunities to reduce turnaround times, resourcing and processing costs on complex government procurements, whilst being able to encourage and nurture innovation through the increased involvement of SMEs.

To achieve these benefits will require radical changes in the approach to planning procurements, the upskilling of procurement and commercial professionals, the allocation of resources to complex procurement projects, and the effective sharing of 'best practices' across government departments.¹⁷

Efforts have since been made to centralise many aspects of government procurement and to make other savings. These were summarised in response to a Parliamentary question in June 2011 as follows:

Nicola Blackwood: To ask the Minister for the Cabinet Office what steps he is taking to reduce (a) costs and (b) inefficiency in the Government supply chain. [52846]

Mr Maude: Firstly, we are centralising the procurement of common goods and services. For each category of spend there will be a single supply strategy so we can significantly reduce spend through aggregation, standardisation and rationalisation.

Secondly, since July 2010 I have initiated a series of negotiations with over 50 of its major suppliers. These discussions identified and delivered savings of over £800 million in 2010-11. High level negotiations are being undertaken on a 'once for government' portfolio basis, taking account of other work to achieve savings eg the Major Projects Review, the ICT moratorium, and the curtailment of discretionary spend.

Thirdly, the Cabinet Office has appointed a network of Crown Representatives to manage relationships with major suppliers who hold a portfolio of contracts across central Departments and ensure Government acts as a strategic 'single' client. Crown Representatives will be able to challenge suppliers where there is duplication across these contracts and spot opportunities for synergy and cost removal.

Fourthly, to address inefficiency in the procurement process, which adds to costs for both Government and suppliers, we undertook a Lean review of the procurement process, which has suggested actions to tackle wasteful practices and unnecessary complexity. We are now engaged on an implementation programme to apply lean' thinking and techniques to a number of new projects in central Government procurement in order to test these findings to achieve time and cost savings for the benefit of both bidders and the public purse. We will roll out the new approach once the route is proven.¹⁸

The government state that savings of £3.8bn were generated in relation to central government procurement in 2012/13, up on £3.0bn the year before. The £3.8bn consisted of £1.0bn saved from the centralisation of procurement for common goods and services, £0.8bn from the central renegotiation of large government contracts and £1.9bn from limiting expenditure on marketing and advertising, consultants and temporary agency staff.¹⁹

The Labour Government also had a policy of collaborative procurement to achieve efficiency savings. Sir Peter Gershon was commissioned to produce a "Review of Civil Procurement in Central Government" which led to the establishment of the Office of Government Commerce (OGC) in 1999. OGC provided policy standards and guidance on best practice in

¹⁷ Cabinet Office, *Accelerating Government Procurement: Management summary*, February 2011, p9

¹⁸ HC Deb 7 Jun 2011 c290W

¹⁹ Cabinet Office, *Efficiency and Reform 2012/13 summary report* (June 2013)

procurement and encouraged collaborative procurement across various product ranges to deliver better value for money.²⁰

²⁰ For more information see the [OGC archived pages](#) on the National Archives website