FINANCE COMMITTEE CALL FOR EVIDENCE

PROCUREMENT REFORM (SCOTLAND) BILL: FINANCIAL MEMORANDUM

SUBMISSION FROM SCOTTISH FEDERATION OF HOUSING ASSOCIATIONS

Introduction
1. As the national representative body for housing associations and co-operatives in Scotland, the SFHA is taking the opportunity to respond to the Finance Committee’s questionnaire sent out on 16th October 2013 as part of its duties to examine the cost implications of the Procurement Reform Bill.

2. To provide context, housing associations and housing co-operatives in Scotland own and manage 46% of the country’s affordable rented housing stock. This represents 274,996 homes across Scotland, concentrated in some of the poorest communities in our country.

3. There are some important and distinctive features of associations which differentiate us from other public bodies. Our members are:
   - Independent businesses with goals aligned to the Scottish Government in providing and managing high quality affordable accommodation and housing services;
   - Responsible for accessing and managing some public resources for house building, but mostly reliant on our tenants rents for income and expenditure.
   - Managing businesses imaginatively and inventively to benefit housing and communities through our not for profit and community based ethos.
   - Accountable to our members and tenants, who live or have other interests in the communities and places which they create;
   - Regulated by an independent Scottish Housing Regulator
   - Able to demonstrate added value in terms of care and support, wider role and financial inclusion;

4. At the same time, housing associations and co-operatives face a number of significant challenges: welfare reform is likely to lead to reductions in revenue income and increases in operating costs for landlords; increased hardship for tenants and higher levels of bad debt while financing new house building is increasingly difficult and costly. Any overhead cost which adds to demands on rental income without producing benefits is not a welcome prospect.

Executive Summary
5. We have advocated in our original evidence during the consultation on the Procurement Reform Bill, for the removal of our sector from the public sector procurement regime. We understand the complex legal reasoning behind why the Scottish Government considers its hands are tied by Europe. We would argue that including our sector in requirements for public contracts below EU thresholds is costly, will result in increased bureaucracy and overhead for our members and bring
little benefit to the private SME sector which relies heavily on small local spend within communities.

6. We think it is significant that housing bodies have been overlooked in terms of consultation on the Financial Memorandum. Our members are not large local authorities, NHS trusts or universities, but small third sector organisations which do not currently consistently use other public sector procurement tools such as Procurement Capability Assessments.

7. We cannot concur with the assertion that there will be no net impact on costs stated in the Financial Memorandum on the impacts of the Bill. We could anticipate an increase on average of £50,000 per association in additional cost in ensuring compliance with the Bill requirements, which could be a further £8.5M in total cost.

**Specific Questions on the Procurement Reform (Scotland) Bill**

8. The Finance Committee questionnaire was sent to a number of public contracting bodies and other private sector representatives for views, but not specifically to any public housing bodies. We feel it is extremely important to respond to the Finance Committee and to comment on the likely additional cost and resource requirements which the Bill’s provisions will burden our sector with. The Financial Memorandum (FM) accompanying the Bill as embedded in the Explanatory Notes at Item 89 Table 2 states:

“No net impact on costs is anticipated. The Bill provides a statutory basis for what is already a routine and on-going cost for local authorities and other contracting authorities who re involved in procuring goods, services or works.”

We do not think that the Bill and the FM take any real cognisance of the position of “other contracting authorities”.

9. As we respond to the individual questions posed by the Finance Committee, we also intend to make comment on some wider principles in relation to our sector’s participation in public procurement in Scotland.

**Did you take part in the Scottish Government consultation exercise which preceded the Bill, and if so did you comment on the financial assumptions made?**

10. The SFHA submitted evidence in November 2012 and specifically highlighted the potential additional costs to our member businesses – p.2, Item 2.3. Our submission explained in detail why associations do not consider themselves to be public contracting authorities. However, many associations have had to accept the application since 2004 of the decision in the European Court of Justice which went against France and resulted in the UK defining all registered social landlords (RSL’s) and including Scotland’s housing association sector as subject to public procurement legislation.

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1 SFHA response to the Procurement Reform Bill Consultation November 2012  
http://www.sfha.co.uk/index.php?option=com_docman&task=search_result&Itemid=340  
2 Commission v France (C-237/99)
11. Our submission highlighted the additional cost to English RSL’s of contract compliance – estimated at £30M\(^5\). When our members are fewer and contracts less sizeable, we believe that public procurement activity will delivering few benefits in savings to them. Longer timescales for contracts, the small size of our member businesses with a few exceptions, the attitude to risk as voluntary organisations and the scale of our construction industry adds disproportionately higher costs. There is also significant concern over the application of public sector procurement principles to housing care and support services provided by our sector.

12. Turner Townsend reported in March 2011 on Procurement in the Affordable Housing Sector and identified £530 M of activity within our sector which may result in £26 M/£42M of savings\(^4\). As yet no clearly identified route to delivering these savings has come from the report’s recommendations and while our members are actively collaborating, using Public Contracts Scotland and adopting best practice, substantiating savings and efficiencies are extremely difficult. On the other hand additional legal costs, salaries of specialist procurement staff and the costs of delays in services and construction contracts can be quantified as significant, potentially adding £50,000 per annum (cost of one post and a average legal bill of £10,000 for advice) per association or £8.5M of overhead over 170 associations.

**Do you believe your comments on the financial assumptions have been accurately reflected in the FM?**

13. We do not feel that sufficient cogniscence has been taken of the cost burden to our members and the statement in the FM that there will be “no net impact on costs” as quoted previously, to contracting authorities certainly does not apply to our sector. We are concerned at the likely burden to be born by tenants and community based organisations. This burden will also be born by small local businesses which rather than benefit from increased opportunity and transparency, will find the information requirements increased to show compliance with community benefit and sustainability criteria.

**Did you have sufficient time to contribute to the consultation exercise?”**

14. We did not find that time was an issue to contribute to the original consultation. However, we do feel that time needs to be taken to investigate potential costs to our members. Our original submission was made to advocate the case for associations to be removed from the category of public contacting authorities. Since this case has been consistently rejected as not being within the gift of the Scottish Government, inclusion has profound cost and other implications for members. We still maintain our position that we do not have the characteristics of public contracting authorities as defined in the Public Contract (Scotland) Regulations 2012 at section 3 (b)(b)\(^5\), and in particular the provisions of finance and supervision by another public authority.

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\(^3\) NHF (March2011), Response to the Commission’s Green Paper on the Modernisation of Procurement – pp3 –

\(^4\) Procurement in the Affordable Housing Sector
http://www.scotland.gov.uk/Publications/2011/03/11120322/0

\(^5\) http://www.legislation.gov.uk/ssi/2012/88/made
**Costs**

*If the Bill has any financial implications for your organisation do you believe that these have been accurately reflected in the FM? If not, please provide details*

15. The FM is written from the perspective of Local Authorities and other large public bodies. The argument is that these bodies will have participated in standard Procurement Capability Assessments (PCA's), a tool used by Scottish Government’s Procurement Unit (5) for at least four years. Section 31 of the FM states that 98% of the 126 contracting authorities who were subject to PCA’s, will have a current procurement strategy. With respect, our members have not undertaken PCA’s as part of the Procurement Reform Programme. It has been acknowledged by Scottish Government within the recently published Construction Procurement Review that they are not useful for associations, Therefore we cannot agree that the overall anticipated net impact to local authorities and other contacting authorities will be zero. There will be additional costs which will fall on organisations as a result of the Bill’s provisions.

16. Several provisions impose requirements on contracting authorities and although these practices may well be current amongst local authorities, they are not necessarily prevalent amongst housing associations in the prescribed form.

**Current procurement practice within our sector**

17. Housing associations and co-operatives which operate in Scotland are a very diverse sector. As well as different areas of operation – and some work across all of Scotland and England – associations vary in size from 20 unit Abbeyfields for elderly people to the 40,000 homes managed by Glasgow Housing Association. Associations tackle many different client groups from older people to community based regeneration of inner city neighbourhoods. A significant proportion of our work provides care and support services to vulnerable tenants.

18. The average association size is 1800 homes in management with a turnover of £5.5M. They will procure possibly £2-3M of repairs and maintenance work in a year, broken up into very small contracts usually undertaken by a wide range of local SME’s on a schedule of rates basis. This has been the cornerstone of sustaining many small local businesses through the current recession. While many associations have looked at collaborative contracts, use of frameworks and utilisation of the Public Contracts Scotland website, this has been on an individual basis as has suited their own requirements.

19. This is in contrast to Scotland’s 32 Local Authorities, which although they may vary in size and location, have similar practices and statutory duties in relation to procurement amongst themselves. Evaluation of sustainable procurement compliance, use of PCA’s, use of collaborative working tools and a common procurement culture as described in the FM would mean that the provisions of the Procurement Reform Bill require only the publication of existing local authority policies and procedures in terms of additional resource.

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6 [http://www.scotland.gov.uk/Topics/Government/Procurement/buyer-information/pca](http://www.scotland.gov.uk/Topics/Government/Procurement/buyer-information/pca)

20. Most associations do not employ specialised procurement departments and compliance with public procurement has been undertaken mainly by property staff or housing staff for care contracts. In relation to construction and major repairs contracts above European thresholds there is compliance with the 2004 designation of associations as public contracting authorities, in the absence of a response to our arguments against this designation as submitted in our previous evidence. (See footnote1) In comparison, as stated above, most local authorities have well staffed procurement teams headed up by specialist procurement personnel to deal with contracts administration at the scale of many hundreds of millions.

21. We would contend that the FM has in no way considered how the provisions will affect our sector, but only looked at prospective costs for local authorities and other large public bodies.

Financial implications of the Bill provisions

22. Considering some of the financial implications of the specific provisions of the Bill, in turn, we would comment as follows:-

- The requirement to publish procurement strategies and reports where spend is above £5M in any one year, is a significant additional burden to associations. While associations have buying and commissioning procedures, these are of varying complexity and there will be significant cost in revising and publishing compliant strategies. Evaluating spend and when thresholds have been reached is also not necessarily a simple matter as the association may commission a large repairs contract in one year which will bring spend above £5M, reducing to normal management and maintenance overheads in the next year. Most associations have no experience of PCA’s.

- Setting up systems to justify and monitor community benefit in contracts over £4M is an additional burden. The duty is imposed over the “area” within which the contracting authority operates, but this can vary from a few streets to the whole of Scotland for associations. Most associations are fierce advocates of using local businesses and supporting the SME sector. While guidance on further implementing Community Benefit clauses following on from the Scottish Government 2008 Guidance is very welcome, the guidance should provide absolute clarity about what is involved. For example, are there different standards for below EU threshold contracts, and how does an organisation then justify upholding EU treaty principles of transparency, equal treatment and non-discrimination, proportionality and mutual recognition? The uncertainty will involve our members having to take costly legal advice on multiple occasions in order to mitigate the risk of claims and challenges.

- Promotion of sustainability and environmental responsibility through procurement practices also imposes new duties and costs. In examples we

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9 http://www.scotland.gov.uk/Topics/Government/Procurement/policy/Legislation/ECTreatyobligations
have seen from local authority practice\textsuperscript{10}, administration of these duties is significant in providing audit information of compliance.

- The greatest burden will however be in simply administering thresholds and when it is appropriate to use one route for advertising and compliance rather than another. Procurement contract administration and audit for contracts between £50,000 and £173,000 for services and £2M and £4.3M for construction contracts is an additional substantial burden. While some associations are now routinely advertising everything above £50,000 on Public Contracts Scotland, this does seem to count against the principle of the Bill in removing unnecessary bureaucracy.

As well as the £5M and £4M thresholds for publication of a procurement strategy and community benefit justification, the distinction between EU and Procurement Reform Bill thresholds, there are other requirements with regard to remedies, feed back to unsuccessful tenderers and successful tenderers and on going EU treaty obligations. This makes for a complex and unwieldy piece of legislation which in itself needs to be considered with the Public Contracts (Scotland) 2012 Regulations and the EU Directives. This is particularly difficult for small organisations with a limited turnover.

Housing associations already have the cost of providing substantial audit information to the Scottish Housing Regulator\textsuperscript{11} and to OSCR on the use of tenants’ monies and the efficiency of their operations.

- We would comment on the costs for other organisations and in particular economic suppliers. The amount of information required by the Procurement Reform Bill in relation to sustainability and community benefit in order to satisfy requirements for audit will inevitably mean more work and further costs. As well as dissuading them from participating in the first place, this could prevent local contractors from winning work. This could have a negative impact on local communities and businesses as well as imposing an administrative burden disproportionate to any community or sustainable gain.

\textit{Do you consider that the estimated costs and savings set out in the FM and over the timescales for which they are projected are reasonable and accurate?}

23. As the only potential costs are attributed to Scottish Government, we cannot give any informed feedback on the reasonableness of the estimates or timescale. We would however anticipate that staffing and resource costs are light, given the substantial guidance we expect will be required for our sector. For example, we are aware as part of the Construction Procurement Review (see footnote 7) mandatory use of Procurement Capability Assessments may be required. These have already been identified as not appropriate for our sector, and work will be needed on adapting to be useful and fit for purpose. This must be applied to the writing up of

\textsuperscript{10} Presentation by Ashley Gould, Head of Procurement Highland Council to SFHA/Scottish Government Procurement Seminar 3\textsuperscript{rd} October 2013

\textsuperscript{11} Analysis of the finances of regulated social landlords 2012 Scottish Housing Regulator
guidance for all of the various Bill provisions, where there seems to be no allowance for our sector and its particular circumstances.

If relevant, are you content that your organisation can meet any financial costs it is expected to incur as a result of the Bill? If not, how do you think these costs should be met?

24. We have with Scottish Government hosted a series of seminars with members in October 2013 on procurement in our sector which has fortuitously coincided with the publication of the Bill.

25. This has enables us to take soundings from members and it is fair to say that there is extreme trepidation as to the additional administrative and due diligence burden that our sector will require to meet. With the uncertainty of welfare reform changes, pension issues and constraints on investment there are more requirements than ever to obtain best value for the expenditure of tenants’ rents. Most associations do not equate public sector procurement with proportionate and reasonable measures to achieve best value, given the scale of most of our businesses and the regulatory burdens they already bear. This is still less so in the commissioning of care and housing support.

26. Additional staff overheads, additional legal and consultancy costs and even the additional contractual issues and costs to do with collaboration and frameworks are all new costs which will be deducted from resource required to support tenants through welfare reform, fuel poverty and particular needs.

27. We do not think our sector should be mandatorily required through legislation to meet the additional costs that the Procurement Reform Bill will impose. We think that the sector should be removed from the designation of Public Contracting Authorities for all procurement below EU thresholds pending clarification at European and Scottish Government level of the status of the sector. This would remove them from the duties imposed for contracts above £50,000 and £2M, and relieve them from the significant extra cost which is quite disproportionate for the scale and size of the majority of our members.

Does the FM accurately reflect the margins of uncertainty associated with the estimates and the timescales over which such costs would be expected to arise?

28. Given that there is no acknowledgement of the additional cost to our sector in the FM, we cannot comment constructively on this question.

Wider Issues

Do you believe that the FM reasonably captures the costs associated with the Bill? If not, which other costs might be incurred and by whom?

29. We have already commented at length on the additional costs that will be incurred by our members. The problem does go back to the reasons why our sector is classified as public contracting bodies in the first place. Because this has arisen through the translation of an EU decision into Scottish Law, we do not fit the public procurement regime. Indeed given that a substantial number of our members do not currently obtain grant finance to build houses, but use their own income from tenants
to maintain and manage houses, then even meeting the test of being financed wholly or mainly by another public body in the 2012 Regulations – section 3 (b)(b) (see footnote 5) is not apparent. The Regulations also require that bodies are subject to management supervision by another contracting authority. While the Scottish Housing Regulator provides inspection and reporting on the affairs of associations, there is no “controle” – the exact word used in the case against France in 2004.

30. Scottish charities are not public contracting authorities, yet our members although charities in the main, are\(^\text{12}\). We are not public bodies for the purpose of the VAT regime (which would provide significant financial benefits to us)\(^\text{13}\) and we are not subject to Freedom of Information requests\(^\text{14}\) so we have many characteristics which set us apart from other public bodies.

31. Scale is one of the main issues however – many single local authorities have the budget and turnover of the whole of our sector, so even if we all collaborated jointly to procure goods and services, any benefits would be small and disproportionate to the work required for such an exercise for small organisations.

**Do you believe that there might be future costs associated with the Bill for example through subordinate legislation? If so, is it possible to quantify these costs?**

32. Given all that we have stated above, we strongly believe that as additional guidance and regulations are developed, this will mean additional bureaucracy and cost to our sector.

33. We have suggested that £8.5M may be a possible amount for the implementation of the current Procurement Reform Bill. This does not take account of the additional costs which future regulations may bring to bear on housing and support services and therefore we suspect this is conservative.

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\(^{12}\) [www.oscr.org.uk/media/2151/Whos%20in%20charge.pdf](http://www.oscr.org.uk/media/2151/Whos%20in%20charge.pdf)

\(^{13}\) [http://www.hmrc.gov.uk/manuals/vatgpbmanual/vatgpb2320.htm#IDACH1QG](http://www.hmrc.gov.uk/manuals/vatgpbmanual/vatgpb2320.htm#IDACH1QG)