

Meg Hillier MP
Chair, Public Accounts Committee

By email

27 March 2018

Dear Meg,

DBS modernisation programme

I am writing to provide the information requested at the PAC hearing on 19 March together with further areas of clarification. Adele Downey, CEO of the DBS, will be writing to you separately.

Further to question 73 raised by Mr Lee Rowley MP, concerning the Capita contract in particular the margins agreed as part of the original contract, and more generally on the margins agreed in contracts across the Home Office, the details are as follows:

In our experience and based on the best expert advice available across Government, for IT service contracts the operating margins are in the region of 5%-30%. If overhead levels are factored in, (such companies typically bear a range from 8%-12%), then the range of gross margin is 13%-42%. The margins are lowest for IT infrastructure services, and highest for security design, technical architecture design, and project management services.

For standardised IT operations services (infrastructure plus applications management), which make up the highest volume of services outsourced by government, margins are towards the lower end of the range.

Business process outsourcing services typically exhibit operating margins in the range 7%-15%. With lower overheads in the range 5%-10%, the range of gross margins in this business is 12%-25%.

The contract with TCS, as originally awarded, included large elements of IT infrastructure operations, applications management, some business process outsourcing and some initial applications design and systems development.

With this mix, and the range of margins above, a target gross margin of around 22% (giving TCS the opportunity to earn 10%-17% operating margin) was viewed as good value, and was certainly the best value in the procurement exercise conducted.

In reality, TCS has had to deploy significantly more high-end skills to redesign the technical architecture, following GDS insistence on using cloud hosting, and additional skills to redesign the applications architecture when the cloud hosting proved unworkable. Because of this, the earnings that TCS are actually receiving from the contract yield margins far below those it would normally expect to earn from government business of this type.

In comparison, the Capita contract which was much more heavily weighted towards business process outsourcing services, was let with a 19.6% gross margin on change services, with expected overheads of 7.6%, yielding 12% operating margin. Pure business process services attracted 15.6% gross margin.

Where the term “gross margin” has been used, it refers to revenue after having subtracted direct costs and where the term “operating margin” is used, it refers to gross margin after deducting further overheads and administrative costs.

The Home Office is committed to supporting the DBS throughout the process of commercial negotiations with TCS to agree the best possible outcome. I will write to the Committee sharing the outcome of the negotiations once they have concluded later this year.

I also want to take the opportunity to clarify the position in relation to incorrect disclosures on certificates. This relates to questions 170 to 176 and questions 196 to 201, where the answers could lead to misunderstanding about the disclosure of convictions and cautions, the disclosure of police intelligence and the separate disputes processes available.

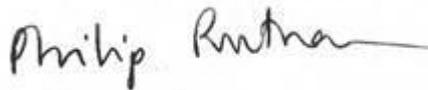
The DBS is responsible for the disclosure of recorded convictions and cautions in line with statute, including the filtering rules, as set out by Ms Downey. There is a DBS disputes procedure, which can be used to dispute applications details (name, address etc.) and convictions, cautions or barred list information.

The disclosure of police intelligence on enhanced certificates is undertaken by the police in accordance with a statutory test for relevance. It is the Chief Officer's responsibility to decide what intelligence is relevant and ought to be disclosed. The police do not decide what convictions and cautions are disclosed.

In situations where an applicant disputes the relevancy of police intelligence disclosed on a certificate, then there is a separate process for appealing the police decision through the Independent Monitor, as described in the evidence. The disclosure of convictions and cautions is not subject to that appeal route.

If further clarification is required, we would be very happy to provide it.

Yours sincerely,

A handwritten signature in black ink that reads "Philip Rutnam". The signature is written in a cursive style with a long horizontal stroke at the end.

Sir Philip Rutnam
Permanent Secretary