

**INQUIRY INTO NSW GOVERNMENT'S USE AND
MANAGEMENT OF CONSULTING SERVICES**

Organisation: CEPA
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NSW Legislative Council
Public Accountability and Works Committee

17 July 2023

Dear Committee Members,

Submission: Inquiry into the NSW Government's use and management of consulting services

Thank you for the opportunity to provide a submission to this inquiry.

CEPA is an economic and financial consulting business, with offices in Australia and the United Kingdom. Our clients include government, regulatory agencies, private companies, consumer groups, and investors. CEPA's advice to Australian clients relates mainly to the design of regulatory frameworks and competitive markets to support efficient service provision in the energy, water, transport and communication sectors. Although we have not previously advised the NSW Government, we would like to share some brief observations from our work with other public sector clients, in Australia and internationally.

Well-managed consulting services can deliver value

When used effectively, consultants can deliver substantial value to public-sector clients – and the community at-large – by providing:¹

- Specific expertise that would be impractical or inefficient for the client to develop or maintain in-house.
- Additional capacity to help the client deliver an unanticipated or peaky workload.
- An independent opinion on the issue at hand.

These elements are present in many of CEPA's successful client engagements. For example, we frequently advise economic regulators to assist in determining the prices that monopoly service providers can recover from their customers. In this context, the support we provide may include:

- Advice on financial or economic questions that require specialist technical knowledge. Although economic regulators are – appropriately – experts in their field, there are certain topics that may require particularly in-depth research and/or benefit from international and cross-sectoral experience which consultants can be better placed to provide. It may also be difficult for regulators to maintain internal careers paths for staff who wish to develop certain specialist skills. A firm of expert consultants can provide that career path.
- Partnering with the regulatory agency to deliver an intensive workload. For example, regulatory determinations might only arise every few years, so that it is not practical or efficient to maintain an internal team large enough to deliver the work during such peaks.
- Independent analysis and evaluation. For example, an external perspective on issues raised by stakeholders may help to test and challenge the regulator's existing positions. Similarly, an external arms-length evaluation can be a helpful tool for reviewing the past performance of the regulatory framework.

¹ Nous Group has provided a useful explanation of these three rationales for seeking consulting advice, which is available here: <https://nousgroup.com/insights/government-spending-consultants/>.



Economic regulation is a highly contested space with competing viewpoints. Economic regulators often find it valuable to seek a neutral and objective perspective.

Certain conditions are required to support effective management

In our experience successful collaborations between consultants and the public sector rely on the presence of certain factors. In particular, we wish to highlight the importance of **informed clients** that have the capacity to **clearly define the scope** of the consultancy and oversee a genuinely **competitive procurement process**, with **accountability** supported by transparent reporting. We elaborate on these four inter-related factors below. These relate to the following aspects of the Committee's terms of reference: *the transparency of work undertaken by consultants, and the accountability of consultants for this work; whether consultants are being used strategically and in a way that delivers value for money; and the impact on the capacity and future development of the NSW public service as a result of the increasing reliance on the use of consultants.*

1. Consulting services best complement informed and well-resourced clients.

To get full value from the independent specialist advice that consultants can provide, the client must have the internal capability to adequately scope, manage and review the consultant's work. Our most effective partnerships are characterised by clients with clear understanding of how the consultancy will contribute to their objectives and the ability to engage with us on the detail of the advice we provide. Accordingly, we consider that maintaining and building the capability of the public service is essential: consulting services should be seen as a complement to this expertise, not a substitute.

2. A well-defined scope is critical to effective management of consulting services.

In our experience, clients receive the most value from consulting services when the outcomes they wish to achieve are clearly identified. Among other benefits, a precisely defined scope: supports a competitive procurement process (see below); enables the client to monitor progress against its objectives; and can help to avoid cost-overruns and excessive use of contract variations/extensions.²

It can sometimes be appropriate for public-sector clients to engage with consultants to refine the scope in advance of issuing a tender. For example, our clients in other jurisdictions sometimes formally approach the market to seek feedback on draft terms of reference. CEPA has also supported clients in defining the terms of reference for other consultants. While such processes can provide useful information to the procuring entity, care should be taken to avoid the potential for 'consultant shopping' or engaging with only a limited subset of suppliers.

3. Effective competition drives value for money and accountability.

As economists, we consider that genuinely competitive procurement processes are key to ensuring that consulting services provide maximal value. Further, effective competition can avoid the public sector becoming over-reliant on a small number of consultancies. Competitive pressure (and the prospect of being readily replaced or work being done by the client in-house) creates strong incentives for service providers to deliver quality advice and maintain high standards of integrity.

One way that the NSW Government currently aims to drive competition is through the use of panels such as the Performance and Management Services scheme (PMS scheme), which includes a capped rate card that consultants must sign up to benefit from less stringent procurement arrangements.³ While day rates can provide

² The NSW Audit Office has found that agencies were unlikely to meet targeted reductions in consulting expenditure. Specific concerns were noted in relation to the use of contract variations and gaps in monitoring the quality of outputs. Audit Office of New South Wales (2023), *NSW government agencies' use of consultants*, 2 March 2023, pp.21-22, pp.27-29.

³ For transparency, CEPA – along with several other consultants – has not agreed to the capped rates required under the PMS scheme's standard commercial framework. This is because, for the reasons stated in this paragraph, we consider that a focus on day rates is misplaced, rather than a consideration of the overall value delivered. The majority of services that we offer can be provided on a fixed price basis.



useful points of reference, they are not a substitute for a thorough value for money assessment.⁴ We suggest that competition can be most effectively harnessed during the procurement process for specific pieces of work, where the scope can be precisely defined. This supports competition (by enabling an objective comparison of each consultant's offering), enhances value for money (by encouraging consultants to put forward solutions that optimise quality and price) and allows for fixed price contracting that mitigates future cost overruns (by appropriately passing risk to the consultant).

Realising these benefits relies on tenders being released to a wide range of possible service providers and assessed by appropriately qualified staff. Although CEPA does not have visibility of how the NSW Government uses limited tendering / direct procurement, we observe that the international jurisdictions CEPA operates in appear to make far more frequent use of open approaches to the market, compared to Australia. This includes in relation to supplier panels, where frequently tenders are released to the entire panel, rather than a select few providers. Although this involves more effort and resourcing during the procurement process, this may be offset by higher quality and/or lower cost services.

Fostering competition also requires that procurement processes support participation by smaller service providers. Boutique consulting firms are often well-placed to offer specialist services that complement the expertise of the public service. In addition, smaller firms are better able to avoid and/or manage conflicts of interest.⁵ While CEPA fully supports action to improve accountability and integrity in the provision of consulting services, we encourage the Committee to ensure that this does not impose hurdles on small suppliers that are detrimental to competition.

4. Transparency promotes accountability.

Finally, we consider that transparency around the outputs of consulting engagements promotes accountability for both the consultant and the procuring agency. This allows for valuable scrutiny of the quality and accuracy of the advice, and the need for the work to have been undertaken by a consultant in the first place. Save for cases where there are genuine confidentiality concerns, we support consultancy reports being made publicly available.

Transparency is also important given the uncertainties inherent in the expert advice consultants provide. For example, economic analysis often involves making many assumptions around inputs and behaviours. Publishing such analysis incentivises the consultant to ensure they have adequately explained their advice and encourages the procuring agency to take account of any material limitations in their decision-making.

Next steps

The NSW Government has established a detailed Procurement Policy Framework. The Committee may wish to explore whether the success factors we have identified above are adequately reflected in this guidance.

CEPA agrees to the publication of this submission in full. We would be pleased to provide further details in writing, if of value to the Committee. Please direct any communications to info@cepa.net.au.

Yours sincerely,

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⁴ Indeed, the NSW Audit Office (2023, p. 23) found that spending on consultants is increasingly concentrated in a small number of firms. For example, in 2021-22 just eight firms accounted for 50% of total spend, down from 11 firms in 2017-18. Further, around 27% of total spending in the 2017-18 to 2021-22 period sat with just four firms, KPMG, Ernst & Young, PwC and Deloitte. This suggests that current procurement approaches, including less stringent arrangements for firms that accept capped rates, may not have been effective in driving competition.

⁵ For example, in his evidence today to the (Commonwealth) Senate Finance and Public Administration References Committee (reported in the Australian Financial Review, 17 July 2023), Professor Allan Fels observed that combining audit and consulting services within one business create unmanageable conflicts of interest. We consider that similar conflicts are less likely to arise for smaller firms, given the narrower scope of the advice they provide and their ability to effectively monitor potential conflicts across fewer engagements.