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Directors
Department for Education

From: John Kirkpatrick
Senior Director

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Dear Jennifer and Anne

CMA recommendations on the Technical and Further Education Bill

I am writing on behalf of the Competition and Markets Authority (CMA) regarding the Technical and Further Education Bill (the Bill) currently before Parliament.

The CMA works to promote competition for the benefit of consumers, both within and outside the UK. In the strategic steer to the CMA published in December 2015, the government said that “the CMA has a clear mandate to look at any Government rules and regulations...and advise on any implications they might have on competition...there will be a presumption that the Government will accept all of the CMA’s published recommendations unless there are strong policy reasons not to do so”¹. The attached paper contains the CMA’s recommendations in relation to the Bill.

The CMA has experience of public service markets, and how these can be made to work for consumers, across a range of sectors. Earlier this year, following on from previous work on higher education², the CMA made recommendations in respect of government legislation covering higher education and research³. The CMA also has some specific experience of further education, having undertaken merger analysis in the sector and contributed to research studies commissioned by government⁴. We have been discussing issues in the further education and qualifications markets with DfE officials, at their invitation, for some months.

Our recommendations on the Bill, which reflect the content of those discussions, relate to qualifications markets. The Bill is not prescriptive on how the Institute for Apprenticeships and Technical Education (the Institute) will procure and approve

¹ [Government’s Strategic Steer to the CMA \(2015\)](#)

² [An effective regulatory framework for higher education: a policy paper](#)

³ [CMA recommendations on Higher Education and Research Bill](#)

⁴ For example: the [BIS research paper on Further Education Market in England \(2016\)](#)

technical education qualifications in future. However, it does lay the groundwork for significant change to how these markets will work and ultimately the qualification choices available to learners.

We note that the independent panel led by Lord Sainsbury has recommended that government should move away from the current awarding organisation market model, where qualifications which deliver similar but different outcomes compete with one another, and instead adopt a licensing approach.

We have not undertaken our own assessment of these qualifications markets and are not well placed to comment on the overall conclusions of the panel. Rather, our intention in writing this letter is to highlight the opportunities and risks that we see to a licensing approach from a competition point of view, and to make recommendations as to how government should account for these as it develops detailed policy in this area.

Should government (or the Institute) go down the route of offering limited or exclusive licences for each qualification, we recognise that this could lead to benefits such as a clearer and more understandable system for learners and employers, and could allow greater focus on qualifications that are more rigorous and useful – and ultimately more valuable to learners and employers.

On the other hand, under an exclusive licensing model, the licence holder for a particular qualification may assume a quasi-monopoly position for the duration of the contract – meaning that training providers and learners would have limited scope to take their business elsewhere if service provision was not up to scratch⁵. This means that contractual arrangements (including contract specification and ongoing oversight by the Institute) must be carefully designed in order to discipline licence holders and ensure that they are incentivised to supply qualification services that meet learner and employer needs.

I have attached our advice to you as an annex to this letter. In summary, our recommendations are as follows:

- **Recommendation 1:** contractual arrangements should be designed so as to promote innovation during the life of the contract.
- **Recommendation 2:** contractual arrangements should be designed so as to enable a smooth transition from an incumbent supplier to an alternative supplier.
- **Recommendation 3:** an assessment should be made of the impact of different contracting options on the competitiveness of technical education qualification markets over the short, medium and longer term – and this should be given due weight in the final policy design.

⁵ This can be characterised as a form of ‘for the market’ competition where suppliers compete to win a contract but then do not face direct competition during the term of that contract. Depending on the model adopted, even exclusive licence holders may be quasi rather than full monopolists, as other suppliers may be able to continue to offer unapproved qualifications (that do not attract public funding).

We are grateful for the constructive way in which your colleagues have engaged and continue to engage with us, and would be very happy to provide further information or assist in any other way, including in conducting the competition impact assessment described in recommendation 3 above and in the development of secondary legislation.

John Kirkpatrick
Senior Director

CMA recommendations on the Technical and Further Education Bill

1. The Technical and Further Education Bill (the Bill) proposes to extend the remit of the Institute for Apprenticeships so that it also covers college-based technical education. The Institute for Apprenticeships and Technical Education (the Institute) will have powers to:
 - determine occupations in relation to which it may be appropriate for people to undertake apprenticeships or obtain qualifications;
 - publish standards in relation to England for such occupations as the Institute considers appropriate;
 - approve technical education qualifications; and
 - make any arrangements that it considers appropriate to secure that suitable technical education qualifications are available.
2. The Bill does not specify the approach that the Institute will take to approving and securing technical education qualifications.
3. We note that the independent panel led by Lord Sainsbury has recommended that government should move away from the current awarding organisation market model, where qualifications which deliver similar but different outcomes compete with one another, and instead adopt a licensing approach.
4. We have not undertaken our own assessment of this market and are not well placed to comment on the overall conclusions of the panel. Rather, our intention is to highlight the opportunities and risks that we see to a licensing approach from a competition point of view, and to make recommendations as to how government should take these into account in the development and implementation of policy.

Innovation

5. The Institute is likely to seek to embed a variety of quality, price and innovation requirements through its bid assessment criteria and contract specification. The balance of these requirements is a matter for government and the Institute. However, we note that innovation is both important in this market and challenging to promote in a monopoly or exclusive licensing context.
6. An important innovation dimension in this market is likely to be the responsiveness of qualification content to developments in technology and industry practice. Our understanding is that the Institute will co-develop qualification standards with employers to reflect the skills, knowledge and behaviours required for a particular occupation. Employers have a vital role to play here; we consider it important that a broad range of employer needs are considered and not only those of larger incumbents.

Recommendation 1: contractual arrangements should be designed so as to promote innovation during the life of the contract. In particular, steps should be taken to ensure that the content of qualifications is updated on a timely

basis to reflect developments in technology and industry practice, where these impact the knowledge and skills that a learner will need to be successful in that industry.

7. For example, one way to promote innovation in the system would be to ensure that: (i) the Institute has a duty to maintain up-to-date standards in accordance with learner and employer needs and (ii) licence holders have a duty to update corresponding qualifications accordingly, in a timely fashion. Depending on contract duration, this may require qualifications to be updated one or more times during the life of a contract.

Step-in

8. Suppliers holding exclusive licences would not face direct competition during the life of that licence. Such suppliers may have stronger incentives to comply with contractual terms relating to price, quality and innovation if there exists a credible threat that an alternative provider could 'step-in' and supply those services on a timely basis, in the event of poor performance by the incumbent. In addition, suppliers may work harder and provide a better service when they believe that rival suppliers have a realistic chance of competing for the contract in future licensing rounds.
9. Contractual specifications that limit barriers to step-in can improve competitive tension both during a licence period and at the point of re-tendering, and therefore strengthen the positive incentives outlined above. This can also support system resilience in the case of supplier failure, for example due to financial insolvency.
10. For example, if the Institute contracts in a way that provides it with continued access to (or ownership of) intellectual property that is generated during the lifetime of an exclusive qualification licence, this could support the ability of other suppliers to provide services in respect of that qualification in future⁶.

Recommendation 2: contractual arrangements should be designed so as to enable a smooth transition from an incumbent supplier to an alternative supplier, either during the contract term (if required) or at the point of re-tendering.

Other aspects of contracting strategy

11. A variety of decisions relating to contract design could have a profound bearing on: the intensity of competition in the initial licensing round (short term effects); the extent to which winning suppliers continue to face some competitive tension during the licence period (medium term effects); and the

⁶ On the other hand, if suppliers do not retain IP in respect of the qualifications that they develop, they may face reduced incentives to invest. We expect that the Institute will want to ensure that the payment and wider contractual arrangements adopted in respect of IP ensure that suppliers are rewarded for (and retain incentives to make) efficient investments in qualifications.

intensity of competition at future licensing rounds (long term effects). These considerations are set out in the report on public sector procurement commissioned by the OFT⁷ and are discussed below:

Participation criteria

12. More bidders generally means more intense competition and is likely to lead to better quality and/or lower prices. This suggests that procurers should avoid placing excessive information requirements on bidders, and should avoid pre-qualification criteria that overemphasise past experience or firm size.
13. However, there can be good reasons to impose pre-qualification requirements or limit participation. For example, pre-qualification criteria can be a valuable means of demonstrating competence where services are complex and desirable outcomes are difficult to define contractually. In addition, procurers may seek to narrow the pool of bidders where bid evaluation is particularly difficult and costly, or where 'winners curse' is a concern⁸. Judgements on participation criteria therefore need to be made on the basis of a good understanding of the number and nature of potential bidders in FE qualifications markets and the likely basis of competition among them.

Contract packaging

14. The Institute is likely to wish to secure a variety of qualifications services (including content development, provision of supporting materials and training to colleges and other providers, and end point assessments) and must decide how to package or aggregate these services into contracts. As discussed below, the relationship between contract aggregation and the competitiveness of the tendering exercise is complex.
15. Initial contract award (short term effects)
 - a. The relationship between contract size and the competitiveness of the initial tendering process is ambiguous. More aggregated contracts are likely to limit participation by smaller firms (for example, if tailoring and graphic design qualifications were bundled into a single contract, an organisation specialising in tailoring may be dissuaded from bidding). On the other hand, more aggregated contracts guarantee greater scale for the winner, which may encourage more firms to bid if they believe that they can deliver the contract, either on their own or with the help of partners or sub-contractors.
 - b. A key consideration in contract aggregation is the extent to which economies of scale and scope exist between services. One option would be to create small contract packages and 'let the market decide'

⁷ [Assessing the impact of public sector procurement on competition](#)

⁸ Under some conditions, a fear of the 'winners curse' can mean that an increase in the number of bidders can lead to more cautious bids. This is more likely where cost uncertainty is considerable.

the market structure. This rationale would be that suppliers may be better placed than government or the Institute to identify which combinations of services could be jointly supplied in a more cost efficient manner.

- c. However, we recognise that it may be challenging to accommodate combinatorial bids within the bid assessment process. In addition, absent some constraint on maximum market share, suppliers could seek to dominate the market, in order to weaken competition further down the line. This is more likely if entry barriers and/or first mover advantage is significant.
- d. Greater contract aggregation may reduce the scope for tacit collusion. Letting fewer but larger contracts more infrequently removes the scope for frequent interaction between the same bidders. It introduces a certain volatility in demand and increases the cost of losing compared to smaller, more frequent tenders.
- e. Greater contract aggregation may reduce tendering and bid assessment costs.

16. During the contract (medium term effects)

- a. If a variety of suppliers hold licences, then there would be greater scope for the Institute to use yardstick competition⁹ in order to judge supplier performance on metrics such as customer satisfaction.
- b. As mentioned above, licence holders will face a greater degree of competitive tension if there exists a credible threat that an alternative provider could step-in and supply those services on a timely basis. This threat may be stronger if the initial tendering exercise delivered a market structure comprising a range of different licence holders.
- c. On the other hand, a market structure comprising a larger number of contracts would tend to increase ongoing contract management costs.

17. Contract re-tendering (longer term effects)

- a. There may be a stronger pool of bidders able to exert pressure on an incumbent, if a wider range of suppliers already hold licences for similar qualifications (for example, other qualifications within route).
- b. However, if entry barriers are low, then competitive tension can also come from new entrants. For example, suppliers of academic qualifications, international suppliers of technical qualifications or suppliers of technical qualifications that are outside of the licensing process (i.e. unregulated qualifications or qualifications at different skills levels) may all represent potential entrants. Government or the Institute may want to assess the likelihood that new entrants could impose a competitive constraint as part of its work to determine how contacts should be packaged.
- c. Subcontracting is sometimes regarded as a way of mitigating the potential negative impact of contract aggregation on competition in the

⁹ This is the process of benchmarking the performance of a monopoly with reference to the performance of other monopoly suppliers.

longer-term. However, measures to facilitate subcontracting (or an explicit requirement to sub-contract) may have undesirable competition effects because they could reduce participation and facilitate collusion. For example, such arrangements may provide incentives for bidders to form consortia, which will limit the number of bids received. Where the main contractor engages in significant subcontracting, that may indicate that there are no strong economies of scale or scope for one contractor to undertake the contract.

18. Decisions on contract packaging may involve trade-offs between these short medium and long term effects. A thorough assessment of where they are most likely to arise and have greatest impact on the government's objectives and on the interests of learners and employers will help make those trade-offs explicit and allow the government to make well founded choices.

Contract duration

19. As a general principle, our view is that contract duration should be no longer than needed to provide a return on efficient investment.
20. Longer duration contracts can support investment and encourage more bids - intensifying competition at the initial tendering round. However, longer contracts also mean that there are longer periods between where the licence holder will face relatively weak competitive tension between tendering rounds. In addition, longer contracts may make future tendering rounds less competitive because, for example, incumbents may be able to build larger informational advantages over rival bidders.

Recommendation 3: an assessment should be made of the impact of different contracting options (including those relating to participation criteria, contract packaging, and contract duration) on the competitiveness of technical education qualification markets over the short, medium and longer term – and this should be given due weight in the final policy design. As part of this, government (or the Institute) may find it useful to: undertake market testing in order to better understand the cost structure associated with delivering qualification services (including the profile of fixed and variable costs and the extent of economies of scale and scope) and; assess the potential scale and evolution of entry barriers in the market over time.

21. Our Competition Impact Assessment Guidance¹⁰ provides a structure for how to conduct such an assessment and advice on how to do so. The CMA stands ready to assist departments in conducting competition impact assessments if required.

¹⁰ [Competition impact assessment: guidelines for policymakers](#)