Scotland Excel

To: **Joint Committee**

On: **29 June 2018**

Report
by
Director Scotland Excel

Proposed Contract Rebate/Supplier Levy Strategy

1. Introduction

To date, Scotland Excel have relied almost exclusively on member requisitions to cover operating costs. The funding update provided (ref agenda item), summarises the current financial position and 5 year projection for the organisation. Within this, a number of options to generate additional income are outlined, including the incorporation of volume rebates into appropriate contracts. Current projections are that this could generate a sum in the order of c.£800k by 2023/24. This paper sets out the approach that Scotland Excel will adopt to embed rebate/supplier levy additions into appropriate contracts.

2. Principle of rebates and levies

Despite the differences in approach, both methodologies can potentially derive additional income from contract expenditure.

For volume rebates, a special condition is added to a contract where a defined percentage of the contract spend is paid by the supplier to the contracting authority. Normally, this would include a spend threshold, so that suppliers who receive only a relatively small portion of the business that passes through the contract are unaffected. Also, the inclusion of a threshold further protects the contracting authority from adverse pricing to pay for the rebate. Typically, the rebate would be calculated over a period of one year, which allows spend above the threshold to be considered, and also allows suppliers to make suitable financial arrangements based on contract return

However, for a supplier levy, the process is slightly different. In this case, a defined percentage is added to supplier invoices, and as such paid by the buyer at the point of call off. Again, spend threshold values can be incorporated for the same reasons as rebates. One key advantage of levies over rebates is of course that there is less of a time lag between contract call-off and recovery of the monies earned.

One of the key challenges when either are considered, is overcoming the risk that incorporating a rebate or a levy could adversely affect pricing on the contract. However, market analysis would suggest that if the level is maintained below c.0.75%, there is less of a likelihood of an adverse price variance.

3. Contract selection and review

It is anticipated that not all contract arrangements will lend themselves to incorporating rebates or levies. In order to make this effective, the contract manager must have a clear understanding of the cost drivers that impact the delivered price of the goods or services. Over the past few years, Scotland Excel has developed and embedded a market pricing variance tool across the contract portfolio (contract indexation model). A prerequisite to make the model effective is that the cost drivers highlighted are well understood, and used as an aid in contract and supplier management. In turn, this allows the adoption of a holistic approach when considering appropriate contract areas to incorporate rebates or levies.

Identification and review of relevant contracts will be incorporated into the established contract governance model. At contract strategy development, the inclusion of rebates will be considered on the basis of the nature of the contract, the goods or service provided, the market conditions and the anticipated supply base. Agreed outcomes will then become an integral part of the contract strategy, which will be subject to the normal level of review and consultation with the User Intelligence Group (UIG), and subsequently embedded into the tender documents. At the point of contract award, the rebate inclusion will become part of the terms and conditions of contract, and as such delivery will become a contractual commitment.

4. Anticipated level of impact

Some category activity within the current contract portfolio cover market segments in which the use of rebates is commonplace, for example, within construction. Within the current contracts for electrical and plumbing materials, an annual rebate in excess of £200k has been generated and distributed to councils.

The key difference with any additional rebates generated is that it is proposed that they will be held by Scotland Excel to support current and anticipated financial constraints, and to suppress the need to increase member requisitions for future development activity. As indicated in section 1, it is anticipated that up to £800k annually could be generated within a 5 year period. This is based on a subset of the portfolio, primarily within the construction category with a combined annual forecast turnover of c.£230m, with a rebate value not exceeding 0.55%.

It must be stressed that it is not intended to include a rebate provision within social care contracts, and development of the social care contract offering is likely to be supported by rebates generated for other contract areas.

5. Conclusion/Recommendation

It is anticipated that further developing and expansion of the scope of rebate inclusion across the portfolio provides support to enable the organisation to establish a sustainable financial position.

Members are requested to endorse the approach summarised for the inclusion of a rebate or supplier levy mechanism across appropriate areas of the contract portfolio.