Making public service markets work

Professionalising government's approach
to commissioning and market stewardship

Tom Gash, Nehal Panchamia, Sam Sims and Louisa Hotson

Foreword

This report is one of the most important that the Institute for Government has produced. It highlights many of the confusions and problems produced by the big changes in how public services are provided over the past 30 years. The private and voluntary sectors are now very large suppliers of taxpayer funded programmes – for example in health, care for all ages, employment, and probation. Meanwhile the public sector providers that remain must now often compete for the right to provide public services.

The Institute does not take an ideological position for or against competition in such services, but rather looks at the conditions for their successful delivery, and in particular, where the government needs to improve its own skills and performance in commissioning from external providers.

This report is a culmination of work which the Institute has been doing over the last couple of years about the changed landscape of public services. In common with the Institute's broader approach to research, we have worked closely with those directly involved in public services – via interviews, roundtable discussions and workshops – to learn from both successes and failures. Our focus is, as always, on how to achieve improvements in both understanding and practice. As part of our work, we have discussed early findings with the relevant departments.

The research identifies a number of positive points about where contracting-out has worked well and why, as well as going behind the headlines to explain why some well-publicised failures have occurred. A particular value of the report is in identifying: barriers to informed choice, gaming by providers to maximise their returns, and a reluctance to change methods of provision when they are not working.

The report suggests a number of ways that the government's stewardship of independent providers could be improved – all involving greater clarity about objectives and candour about performance. There are big implications for the regulation of competition and for the way departments oversee public service markets.

This is far from the end of the story but as governments, of whatever party, develop their approaches to delivering public services, they should take account of the analysis and recommendations in this rich and stimulating report.

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Acknowledgements

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Executive summary

The past 30 years have seen a dramatic shift in the way UK public services are provided. Government is now rarely the sole provider of publicly-funded services. In education, employment, health – indeed, almost every area – private, public and voluntary sector organisations compete for the right to provide our services, with users often having a say in whose services they receive. Today, roughly £1 in every £3 that government spends on public services goes to independent providers.[1]

The impact of this vast shift is, in truth, not well understood. The evidence does suggest that contracting with independent providers has worked well in simpler, more transactional services like waste management – particularly where providers also offer their services to the private sector. In more complex services, like health or education, the impact of competition is unclear, not least because government has rarely implemented changes in a way that they can be easily evaluated.

It is clear, however, that – as in directly managed services – government does not always succeed in delivering value for money. In the past months, independent enquiries and media investigations have uncovered problems in rail-franchising renegotiations, electronic monitoring of offenders and housing for asylum seekers to name just a few. Failures often have a high cost for both service users and taxpayers.

This report examines government's creation and oversight of public service markets in employment services (the Work Programme), secondary education, care for older people and probation services. It builds on previous Institute for Government research and is based on:

- 85 interviews with those commissioning, delivering and advising on service provision in these areas
- a review of existing evidence
- a series of workshops involving government officials, independent experts and private, public and voluntary sector providers of public services.

Our research identified several areas of good practice. Academy schools have often used their autonomy to develop distinctive subject specialisms and an ethos that parents and pupils value. Social care and employment service providers have attracted private investment to fund the use of new technologies. And probation trusts have teamed up with local partners to develop services that support ex-offenders to reduce offending and find sustainable employment.

However, alongside successes we find significant weaknesses in the way government departments and local commissioners approach the design and oversight of what might accurately be termed 'markets' or 'quasi-markets' in public service provision.

For public service markets to drive improvements, users and commissioners who choose on their behalf need to be engaged and informed. Funding levels need to be appropriate. New providers must be given a chance to prove their worth – and grow. Incentives should drive the desired provider behaviours and poorly-performing providers should be able to exit the market without excessive disruption for service users.

In the services we examined, however, these criteria were rarely met. We noted in particular:

- **barriers to informed choice:** in secondary education and social care for older people, we found that government efforts to support effective choice have sometimes been either limited or counter-productive.
- **gaming:** in all areas, we found providers sometimes responded in undesirable ways to the reward structures created by commissioners and regulators. Such 'gaming' behaviours included excessive

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[1] Julius, D., *Public Services Industry Review*, 2008, Retrieved 15 July 2013: http://www.bis.gov.uk/files/file46965.pdf. Note that this estimate includes services procured by government to support service delivery.

'parking' of service users with complex needs and 'creaming' of users who are easier to support, and therefore more profitable to serve.

- **barriers to exit:** in some sectors, we saw reluctance to force underperforming public, private and voluntary sector providers out of these markets in service provision – partly as a result of a lack of confidence that government can manage transitions between different service providers without causing excessive disruptions to service users.
- **funding imbalances:** providers often competed on an uneven playing field. For example, schools with overlapping catchment areas on different sides of a county boundary can receive significantly different levels of funding for each pupil they teach – a problem that the Government has now promised to address.[2]

We also observed important (and well-known) problems in co-ordinating commissioned services. Providers who offered cost-effective services for users with multiple needs were often overlooked by commissioners focused on a narrow set of departmental objectives. And commissioners of individual services appeared to be ignoring important developments in related public services. For example, a number of large providers now deliver a wide range of services (commissioned by separate government departments) in particular areas of the country. This allows these providers to achieve economies of scale and undercut competitors, making their services attractive to commissioners. But it also threatens to undermine levels of competition, leaving government vulnerable to price increases across a range of services in future.

We observed difficulties in implementing changes in government's commissioning approach. For example, the Work Programme was launched before the IT system it relied on was completed. Our research is therefore consistent with the findings of the National Audit Office and others, which suggests that the implementation of the Academies Programme and the Work Programme encountered difficulties that could have been anticipated with proper planning and testing.

Government's directly managed services often face similar problems. It is therefore vitally important to emphasise that these difficulties are not proof that direct public sector management is preferable to competitive provision. We found some evidence that gaming can be accentuated in highly-competitive environments – particularly where providers are struggling financially or under threat of exit. But our work focused largely on assessing the strengths and weaknesses of existing approaches – and the research method did not allow us to robustly evaluate where market approaches have been more (or less) effective than in-house provision.

The weaknesses we observed appear to relate to a number of underlying problems including:

- **failure to understand the nature of the services being provided:** services have inherent properties which make it easier or harder to use market mechanisms to drive service improvement.[3] We found a lack of systematic thinking about these inherent difficulties, which in turn contributed to insufficient or inappropriate corrective action on the part of government departments.
- **uncertainty about whose job it is to perform essential market oversight functions:** we repeatedly found that it was unclear who was responsible for addressing the problems we found – which may explain why they have persisted for so long. Where they had been assigned, responsibilities often rested at the wrong geographic level or in organisations that lacked the impartiality that was necessary to perform the function appropriately.
- **low capability in central and local commissioning bodies:** government is still developing its capacity to design and steward systems that rely on independent service providers. As the Institute argued in its System Stewardship report, the shift towards decentralised delivery models necessitates a much more open and iterative engagement between providers of public services (public, private and voluntary sector) and those setting policy or 'rules'. We found, however, that government has yet to think systematically about how its role and ways of working must adapt. We found that departments and agencies:
  - o tend not to adequately stress-test shifts in approach
  - o lack adequate methods of ensuring proposals are informed by business understanding
  - o did not sufficiently value the types of flexibility that could help the system adapt to unpredictable developments
  - o fail to demand sufficient transparency of either themselves or independent service providers (public, voluntary or private)

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[2] Osborne, G., Spending Round 2013 Speech to the House of Commons, 26 July 2013

[3] Gash, T., and Panchamia, N., *When to Contract: Which Service Features Affect the Ease of Government Contracting?* Institute for Government website, January 2013, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/when-contract

        o   focus excessively on reducing upfront costs, to the detriment of quality, diversity and levels of competition

Underpinning these difficulties were well-documented weaknesses in commercial skills and departmental structures and processes that were not always up to the job.[4]

Our findings have significant implications for government's public service reform agenda. Not least, they suggest that departments that have recently embarked on major new reforms should focus on ensuring that their design and oversight of existing public service markets is effective, before accelerating or embarking on new reforms. The current pace and scale of change represents a high risk strategy that may undermine confidence in the reform agenda in the longer term.

Recommendations

Government is already taking several positive steps to improve commissioning and oversight of public service markets. For example, the Cabinet Office has established a small, virtual Commissioning Academy to improve skills in this area. However, there is still insufficient recognition of the scale of the challenges across government.

We argue that government must urgently professionalise its approach to commissioning and overseeing public service markets, embracing what we call a 'market stewardship' approach. This approach focuses on ensuring long-term outcomes and value for money and involves policy makers:

- engaging closely with users, provider organisations and other interested parties across the system to understand needs, objectives and enablers of successful delivery
- setting the 'rules of the game' and allowing providers and users to respond to the incentives this creates
- constantly monitoring the ways in which the market is developing and how providers are responding to these rules, and the actions of other providers
- adjusting the rules of the game in an attempt to steer the system (much of which is, by design, beyond their immediate control) to achieve their high-level aims.

To support effective market stewardship, government departments and other commissioning organisations should:

1. Clarify roles, responsibilities and accountability arrangements
2. Be more considered, open and flexible in design
3. Focus on competition, market structure and market dynamics
4. Increase transparency.

Recommendation 1: Clarify roles, responsibilities and accountability arrangements

Given confusion about what needs to be done to ensure public service markets are operating effectively, there is an urgent need to clarify the roles that must be performed, who must perform them and how the organisations and individuals involved should be held to account for performance. To achieve this, we propose the following:

1.1 **Government departments should adopt a version of our 'market stewardship framework'** (figure 3, p. 19) which identifies the key functions that need to be performed to ensure effectiveness. For example, every department should be able to identify which organisation is responsible for ensuring users are able to make informed choices, and which organisation is responsible for clarifying how provider failure (in terms of performance or financial failure) will be managed.

Some organisations need to be impartial and all organisations need to be structured (and funded) in a way that ensures they can perform their role effectively. Therefore, for each market stewardship function, the responsible central or local government department must ask:
    o   does this organisation need to be impartial to perform this role?
    o   does this organisation have the capability to perform this role effectively – or could it develop it?

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[4] For example see Blatchford, K., and Gash, T., *Commissioning for Success: How to Avoid the Pitfalls of Open Public Services*, Institute for Government, London, August 2012, retrieved 9 June 2013, http://www.instituteforgovernment.org.uk/publications/commissioning-success

1.2 Once roles and responsibilities are clear, **all central and local government departments should produce 'accountability maps'** which detail both the organisations and individuals responsible for each aspect of market stewardship.[5] Select Committees should demand that departments produce these 'accountability maps'. This will allow them to focus much more on understanding overall system performance and the capacity of the department to ensure high-quality, cost-effective services, rather than on the failing of individual providers, which may grab the headlines but might have less bearing on performance.

1.3 Our research, like other Institute work, repeatedly showed the importance of clear and continuous leadership at ministerial and official level. We support the Cabinet Office's drive to ensure 'senior responsible owners' (SROs) are in place for all major projects. To ensure continuity of leadership and accountability, **we recommend that each public service market is overseen by a designated senior responsible owner, starting with the largest areas of spend** (worth over £100 million p.a.). SROs should be – among other things – responsible for maintaining up-to-date accountability maps. **SROs must remain in post for at least three to five years**. Given current career **incentives it is likely to be necessary to provide financial incentives or other rewards to achieve this**. We have previously recommended that government departments conduct regular skills audits to understand gaps in commissioning and market stewardship capabilities, and reiterate that this is an essential step.

1.4 There is an urgent need for **greater cross-civil-service leadership of this agenda and far greater clarity on the roles of the Cabinet Office and Her Majesty's Treasury (HMT).** The efforts of the Cabinet Office Efficiency and Reform Group (ERG) have usefully aimed to improve central support and oversight but our research suggests that central processes (with the possible exception of the Major Projects Authority and HMT review processes) are largely tangential to the way in which departments design and oversee public service markets. We reiterate the findings of previous Institute research, arguing that urgent efforts are needed to strengthen functional and corporate leadership to address:

- poor identification and management of cross-government risk (see recommendation 3.3)
- inadequate cross-departmental and comparative management information[6]
- duplication of activities across departments
- inability to redeploy appropriately skilled individuals to the areas of greatest need[7]
- the absence of a systematic way of thinking or talking about commissioning and public service markets.

Recommendation 2: Be more considered, open and flexible in design

Our research confirmed the findings of our previous research on government policymaking, which emphasises the need for greater involvement of those who deliver services in the policy design; the need to continually learn about what is working and adapt; and the need for external challenge and scrutiny.

2.1 **Policymakers and commissioners must systematically evaluate and manage the risks of contracting out public services.** Our 'service characteristics' framework (figure 1, p. 17) provides a way to identify which services are harder to contract out, why problems might arise and how to manage (and reduce) them. For example, if it is difficult to measure the value added by providers, there is a risk that government will not be able to reward providers appropriately for their contributions. This risk can sometimes be managed – for example, by measuring and rewarding user views (or choices); rewarding relative performance compared to other providers; and paying for interim outputs known to contribute to

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[5] This builds on a recommendation of Moyes, W., Wood, J., and Clemence, M., *Nothing to do with Me: Modernising ministerial accountability for decentralised public services,* 2011, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/nothing-do-me

[6] McCrae, J., Stephen, J., Guermellou, T., Mehta., R., *Improving Decision Making in Whitehall: Effective use of management information*, 2012, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/improving-decision-making-whitehall

[7] See, for example, Magee, I., Gash, T., Stephen, J., *System Upgrade? The first year of the Government's ICT strategy*, 2012, retrieved 16 July 2015,http://www.instituteforgovernment.org.uk/publications/system-upgrade

the desired outcomes. We provide examples of risks and mitigations in our *When to Contract* report. [8] Where there is doubt over contracting out decisions, we suggest that government pilots changes and retains some provision in-house to retain an understanding of costs, delivery models and performance.

2.2 **Central and local commissioners should test any major changes to provider incentive systems**, working with providers in the sector or those who have a good understanding of the provider perspective. We suggest **high-powered, commercially-minded challenge boards,** and **scenario and simulation exercises** as effective methods.[9] These processes should also include user representatives and professional groups wherever possible.

2.3 **Central and local commissioners should find ways of increasing flexibility**, for example by using **performance-related break clauses,** such as those available (but not yet invoked) in the Work Programme; establishing **clear change processes**; and creating **rolling contracting cycles.** Where possible, government should **tie levels of payment to outcomes and volumes of work actually undertaken**. These types of changes ensure that when requirements change, services can change too, without exorbitant costs.

2.4 **Policymakers should ensure they evaluate the effectiveness of services delivered by independent providers to inform future design choices.** For example, they should **use randomised control trials** to assess how effectively providers help their users compared to a small sample of individuals receiving no service. This may not always be politically attractive but it is essential for understanding the value add of independent providers and improving performance over the longer term. It also paves the way for ensuring that payments are more closely tied to providers' actual success in improving outcomes.

Recommendation 3: Focus on competition, market structure and market dynamics

Our research emphasises that commissioners and policymakers often pay too little attention to the long-term development of competitive markets of service provision. There is therefore a need to redouble efforts to ensure a sufficient range of capable suppliers and to maintain competitive tensions. Otherwise, the exit of one or two providers can leave government with a limited choice of suppliers and low bargaining power – as recently happened in the electronic monitoring re-tendering process.

3.1 **Government departments should conduct or commission regular market studies** (akin to the one currently commissioned by the Department for Education for childcare and early-years services)[10] to measure:
  - users' willingness and ability to exercise choice and the factors affecting this
  - barriers to market entry and expansion
  - perverse effects of competitive incentives
  - barriers to, and risk of, provider contraction and exit.

Such studies should pay special attention to ensuring that there are clear pathways to growth for small- and medium-sized providers. If desired, departments could usefully **invite the Office of Fair Trading or other outside experts to advise on market design**, as Her Majesty's Revenue and Customs did when considering a new system of childcare vouchers. **The Major Project's Authority should require all major projects involving public service markets to demonstrate that a market study has been carried out prior to project approval.**

3.2 **The Prime Minister, Chancellor or Minister of the Cabinet Office should consider ways of creating external, public scrutiny**, particularly when:
  - outsourcing major areas of work, for example those worth over £100 million per annum

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[8] Gash, T., and Panchamia, N., *When to Contract: Which Service Features Affect the Ease of Government Contracting?* Institute for Government website, January 2013, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/when-contract

[9] Further options are found in section one of this report and in Blatchford, K., and Gash, T., *Testing New Commissioning Models: A Guide to Help Policy Makers Learn about Publicly-funded Markets*, Institute for Government, London, 2012, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/testing-new-commissioning-models

[10] La Valle, *Childcare and Early Years Provider Survey 2011,* 2012, Department for Education Research Report RR240

- making significant changes to commissioning models worth over £100 million per annum.

There is a range of ways to achieve this. Ministers could, for example:
- create a statutory obligation to publish 'competition impact assessments' (ideally performed by an independent organisation such as the Office of Fair Trading (OfT) or Competition and Markets Authority (CMA)) prior to implementing reforms
- give the National Audit Office (NAO) 'super-complaint' powers, allowing the NAO to oblige the OfT to investigate competition or consumer issues found during the course of value for money studies.

3.3 **The Cabinet Office or the Treasury should initiate an immediate cross-sector review of levels of competition in each region of England and Wales.** This review would seek to define the maximum market share that any provider should have in a specific sector and/or region and would highlight any areas where competitive pressures are too low. This should spur government to enable new providers to enter the market and grow or, where needed, may trigger investigation by competition authorities.

3.4. There is an urgent need to **re-examine the role of independent competition regulation** in public service markets. There is currently a range of models for spotting potential anti-competitive practice in public service markets – with areas such as health having an independent economic regulator (Monitor) but others subject to limited economic regulation. It remains unclear, for example, whether and how areas such as secondary education or probation services are (or should be) subject to competition regulation. The OfT have developed valuable tools for assessing private markets but there is a strong consensus that not all of these tools can be applied to public service markets without significant adaptation.

Recommendation 4: Increase transparency

The Government has taken a number of positive steps to improve the transparency of public service markets, including by publishing information on upcoming government contracts on .Gov.UK, the government's new internet portal. Such steps must be urgently augmented.

4.1 Government contracts should oblige all public, voluntary and private sector providers of public services to publish details of:
- **the funding they receive from government**
- **their performance against contractual obligations**
- **the suppliers to whom they subcontract services, the value of these contracts and, where practical, their performance**
- **user satisfaction levels (where available).**

This transparency could also be achieved simply by clarifying (and if necessary adjusting) the rules on 'commercial confidentiality' to confirm which data, that government holds in relation to contractor fees and performance, can be subject to freedom of information requests. A more incremental approach would be to ensure that contractual arrangements made it clear that no supplier could prevent a sub-contractor from publishing similar information.

We have engaged widely to develop these recommendations but note that they should all be thoroughly (though rapidly) stress-tested prior to their implementation.

Conclusion

As markets in public services become an increasingly dominant model for public service delivery, the issues identified in this this report require urgent attention. Failure to address them will most likely lead to mistakes and falling public confidence in this approach to public service reform. Success will mean more effective services, better value for money and growing public confidence that this agenda – sensibly applied to appropriate areas – can deliver results.

Introduction

> Our aim is to open up the system, to end the one-size-fits-all model of public service, which too often meant one supplier fits all, with little diversity, irrespective of how good new suppliers – from elsewhere in the public sector, and from the voluntary and private sectors – might be.

<div align="right">Tony Blair, Prime Minister (2004)</div>

> From now on, diversity is the default in our public services. What does that mean? It means that instead of having to justify why it makes sense to introduce competition, as we are now doing with schools and in the NHS, the state will have to justify why it makes sense to run a monopoly.

<div align="right">David Cameron, Prime Minister (2011)</div>

Policy context

The past 30 years have seen a dramatic shift in the way government delivers public services. Where possible, government has sought to give citizens an active role in choosing the organisations from which they receive public services, forcing organisations to compete for the right to provide services. Where choice is deemed inappropriate, for example in rehabilitation services for prisoners, government has attempted to stimulate competition between providers by commissioning services. Voluntary sector and profit-making providers have meanwhile been encouraged to offer public services in areas where public sector provision was previously the norm.

Today, waste management, employment services, education, early-years care, – in fact, most services – are provided not by government-managed institutions, but by competing, independent organisations. In some areas, for example the school system, only voluntary sector and publicly-owned organisations can provide publicly-funded services. In others, the private sector has an increasing role, with private companies now providing almost all prisoner escorting services and 14% of prisons expenditure.[11] There is now, in effect, a 'public services industry' conservatively estimated as being worth over £80 billion (bn) per year in 2008.[12] Since then, the Academies Programme (which has effectively converted state schools into charities) and other shifts will likely have seen the size of the industry rising to nearer £100bn.

This shift has been dramatic, and at times controversial. Most members of the public are less concerned about who provides their public services than how good those services are – but a significant proportion (34% according to one recent survey) are not comfortable with people making profits from public service provision.[13] The public sector workforce, meanwhile, has often seen changes as an attempt to reduce wages – a shift many representative bodies believe to be unfair and detrimental to staff quality and service standards. And several advocates of a strong, activist state have associated the shift as an attempt to shrink the state by the back door – mistakenly associating the introduction of choice and competition (which changes the way public services are provided) with privatisation (which removes the state's direct funding role).

Others argue that the shift in direction has coincided with significant improvements in service standards, particularly in less complex services where there is also a large private market for the service in question.

In truth, the evidence on whether a more diverse and competitive landscape of public service provision has improved standards is extremely limited. Reforms have rarely been set up in a way that their impact can be

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[11] Oxford Economics, *Open Access: Delivering quality and value in our public services,* 2012, CBI, retrieved 15 July: http://www.cbi.org.uk/media/1757565/open_access_report.pdf

[12] Julius, D., *Public Services Industry Review*, Department for Business Innovation and Skills website, July 2008, retrieved 8 June 2013, http://www.bis.gov.uk/files/file46965.pdf . Around a third of government managed expenditure is spent through competitive tendering processes according to HM Treasury, Public Spending Statistics Release, Table 9 'Public sector expenditure on services by economic category, 2006-07 to 2010-11' Retrieved 15 July 2013, http://www.hm-treasury.gov.uk/pespub_natstats_feb2012.htm

[13] NCVO, Reform quantitative poll: attitudes to private sector involvement in public services, May 2011, retrieved 15 July 2013, http://www.ncvo-vol.org.uk/sites/default/files/Poll.pdf

evaluated and comparing systems before and after reforms is difficult, given inevitable differences in funding, user needs and behaviour, and policy environments over time.[14] On balance, it is likely that competition has driven up service standards in simpler, more transactional services – particularly where providers also offer their services to the private sector. There is reasonably convincing evidence that the competitive tendering of refuse collection and street cleaning in the 1980s and 1990s, for example, contributed to cost savings of around 20% to 30% and no discernible reductions in quality.[15]

In more complex services, like health or education, the impact of competition is contested, not least because government has rarely implemented changes in a way that they can be easily evaluated.

It is clear, however, that the shift to competitive public service provision has not been a panacea for public sector performance and productivity. Government has encountered a number of problems designing and overseeing contracts with independent providers of public services. It failed to anticipate high-profile failures by individual companies – for example, G4S's failure to deliver Olympic Games' security support or the financial collapse of the care homes provider Southern Cross. There will always be individual organisations that struggle from time to time.

What taxpayers and service users should be far more worried about is a series of research reports which suggest that there are entire service areas where government is consistently failing to get the best from a large number of independent suppliers. Since 2010, independent research and select committee enquiries have roundly criticised contractual arrangements for electronic monitoring of offenders, housing provision, and back-to-work support, to name just a few.[16] These problems have not, however, prompted government to systematically re-examine its overall approach to commissioning and public service markets. Different government departments and local commissioning bodies have developed their approaches in relative isolation, with little reference to the experiences of those employing similar approaches elsewhere in government.

Past research

The Institute for Government's previous work on public services confirms that government is still learning how to get the best from independent public service providers. Civil servants and political advisers express anxiety about their ability to incentivise providers appropriately – partly because many (including some who play a leading role in reforms) have limited relevant experience.[17] They are also unsure about where contracting independent providers is preferable to in-house provision, and how best to ensure that new reforms work.

Our work to date has attempted to provide support by bringing together people from public services so that they can learn from each other's successes and failures, capturing this knowledge[18] and other evidence, and developing practical guides, including:

- *When to Contract*, which identifies the factors that should influence decisions about whether to outsource public services to independent providers[19]
- *Market Testing*, which identifies ways of testing new approaches to commissioning public services before full-scale implementation.[20]

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[14] For example see Audit Commission, *Healthy Competition: How Councils Can Use Competition and Contestability to Improve Services*, Audit Commission online archive, London, November 2007, retrieved 8 June, http://archive.audit-commission.gov.uk/auditcommission/subwebs/publications/studies/studyPDF/3411.pdf

[15] Grout, P., *Private Delivery of Public Services*, Centre for Management and Public Organisation, Bristol University website, 2009, retrieved 7 June 2013, http://www.bristol.ac.uk/cmpo/publications/publicservices/ppfinal.pdf

[16] For example see Geoghegan, R., *Future of Corrections: Exploring the Use of Electronic Monitoring*, Policy Exchange website, 2012, retrieved 7 June 2013, http://www.policyexchange.org.uk/publications/category/item/future-of-corrections-exploring-the-use-of-electronic-monitoring and Policy Exchange and House of Commons Work and Pensions Committee, *Work Programme: Providers and contracting arrangements. Fourth report of Session 2010-2012*, 2011, retrieved 16 July 2013, http://www.publications.parliament.uk/pa/cm201012/cmselect/cmworpen/718/718i.pdf

[17] Blatchford, K., and Gash, T., *Commissioning for Success: How to Avoid the Pitfalls of Open Public Services*, Institute for Government, London, August 2012, retrieved 9 June 2013, http://www.instituteforgovernment.org.uk/publications/commissioning-success

[18] Gash, T., and Roos, T., *Choice and Competition in Public Services: Learning from History*, Institute for Government website, 2012, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/choice-and-competition-public-services

[19] Gash, T., and Panchamia, N., *When to Contract: Which Service Features Affect the Ease of Government Contracting?* Institute for Government website, January 2013, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/when-contract

Aims and method

This report focuses on developing a deeper understanding of the way the UK government currently uses what we call 'market mechanisms' in public services. It examines the strengths and weaknesses of current approaches and focuses particularly on understanding the underlying reasons for success and failure.

We focus on four public services that rely heavily on using competition between autonomous providers as a mechanism for driving service improvement:

- employment services with a focus on the Work Programme
- secondary education
- care for older people
- probation services.

We selected these four case studies to provide a degree of variety in terms of:

- the amount of choice that users have over providers
- the 'maturity' of different systems
- the characteristics of the different services.

We also took into account the degree of interest in our work from policymakers working in these areas. All these areas also affect some of the most vulnerable groups in society. We drew on a range of sources during the course of the research:

- a literature review of academic articles, think-tank reports, select committee findings and government policy documents and evaluations in each of these service areas (a full bibliography is provided at the end of the report)
- 85 semi-structured interviews: 40 government officials (including regulators); 29 provider body employees or representatives; 13 academics/advisers; two user or staff representatives and one councillor
- visits to provider organisations to speak to staff and users, and closely observe the way they deliver public services
- roundtable discussions and problem-solving workshops with senior officials, provider bodies and experts to develop and test our findings
- a review of relevant research conducted by the Institute for Government on the historical development of particular public service markets.[21]

Where possible, we worked closely with practitioners and government officials to get maximum insight into the workings of each of these systems and presented our early findings directly to relevant departmental policy leads. We also tested our analysis in each of the four areas with experts for review and comments before finalising the paper. The project itself was overseen by an advisory group including senior figures from across government, academia and those working in private and voluntary sector providers.[22]

Structure of this report

This report comprises two main sections. The first section contains our overall analysis of how effectively government is deploying user choice and competition between providers to drive service improvement. Here, we explain the theory and practice of using market mechanisms to drive service improvement and highlight the main challenges government faces as it increases its reliance on market mechanisms as drivers of service improvement. Based on this analysis, we also highlight some steps government can take to reduce its current difficulties and areas where solutions need to be generated urgently.

The second section focuses on the four service areas we investigated. Each detailed case study provides:

- a short summary of findings

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[20] Blatchford, K., and Gash, T., *Testing New Commissioning Models: A Guide to Help Policy Makers Learn about Publicly-funded Markets*, Institute for Government, London, 2012, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/testing-new-commissioning-models

[21] See, for example, Sims, S., *The Development of Quasi-Markets in Secondary Education*, Institute for Government website, November 2012, retrieved 8 June 2013, http://www.instituteforgovernment.org.uk/publications/development-quasi-markets-secondary-education

[22] See acknowledgements section for a full list of advisory group members.

- a brief history of the sector
- an analysis of the difficulties in applying market mechanisms based on the inherent characteristics of the particular service
- an analysis of current strengths and weaknesses
- the reasons for these strengths and weaknesses
- identifies lessons for those currently working in these areas or in other public service markets.

Section 1: Overall Analysis

Cross-cutting findings and recommendations

What we need more than ever are effective commissioners who can deliver better outcomes for citizens and better value for money on ever tighter resources, who will embrace new and innovative ways of delivering public services that better reflect the needs of their user.

Francis Maude, Minister for the Cabinet Office (2013)

How do public service markets work?

Governments employ a range of approaches for improving the performance of public services. Since the 1980s, different approaches have fallen in and out of favour in the UK, including:

- more active performance management of government-managed institutions
- increased involvement of professionals in policy development and internal challenge
- workforce reform – for example, changing professional intakes, skill-sets, roles or terms and conditions
- increased user 'voice' – providing users and citizens with the chance to express how they feel services should be provided.

The idea of competition has been an important component of some of these approaches. For example, Audit Commission star ratings of local authorities sought to engender an environment where councillors and local authority officials wanted to outperform their peers in other areas. This form of competition – known as 'yardstick competition' – can be powerful.[23] Public officials often compete vigorously for prestige and career advancement. Indeed, a common complaint about government performance management is that it has sometimes been too successful in influencing behaviour, encouraging government agencies to 'hit targets, but miss the point' in terms of actually improving service quality.

Yardstick competition is, however, distinct from the type of competition we are looking at – which is based on the idea of creating 'markets' or 'quasi-markets' in public service provision. The core theory, central to economics, is that: new providers will bring new (and potentially better) approaches; the providers which perform best will grow; and those that fail will first lose custom encouraging them to 'up their game' or, if they don't improve, exit the market. Providers will gain access to private (or public) capital to innovate and improve efficiency and effectiveness – knowing they will benefit by attracting more business in the long term.

For such a system to work:

- new providers must be able to enter the market and grow
- providers must be competing actively, and in desirable ways
- providers must be able to exit the market
- those choosing services (whether service users or public officials choosing on their behalf) must be able and motivated to make informed choices
- (as in all modes of service delivery) levels of funding must be appropriate to achieve government's objectives.

Why are markets in public services different?

Even in private markets, some form of government regulation is required to ensure that these criteria are being met and the market is driving good outcomes for consumers as well as those providing services. Business practices that deliberately mislead consumers are generally prohibited, for example. And most countries have

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[23] Gash, T, Hallsworth, M, Ismail, Sharif and Paun, A (2008), *Performance art: Enabling better management in public services*. Institute for Government

competition regulators to prevent one organisation from gaining dominance and exploiting the absence of competition to raise prices at the expense of customers.

In public service markets, however, additional regulation is usually deployed. An important difference between public and privately funded markets relates to government's price-setting role. In private markets, the amount of a good consumed is determined by individuals. If consumers like (or need) a product or service, they will be willing to pay more for it, driving providers to meet this demand and then compete to lower prices. If consumers don't think a service is worth the money, they won't buy it or will buy an alternative product that satisfies similar needs.

In public markets, government usually determines prices – the amount paid for a service. Often, this is to protect fairness. For example, government could give every family £5,000 per year for every child of school age to support the costs of education, but politicians (and the public) tend to worry that some parents won't spend it on their children.

On other occasions, it is because government has policy objectives that might differ from those of individuals or families. For example, politicians might believe there are wider social benefits to ensuring that children from different socio-economic backgrounds mix.[24] Or the goods in question might be under-consumed if it was left to individuals to decide how much to pay. For example, prisoners might not choose to spend their money on activities that help them to avoid re-offending, but the public are so keen for them to do so that they are (sometimes) willing to subsidise rehabilitation services in return for lower crime rates. And individuals might not take the same steps as governments to stop the spread of epidemics.

Different services clearly have different inherent properties and our past work has shown that these properties fundamentally affect the respective roles for government and users and the degree to which funding should flow directly from individual choices.[25] Service characteristics affect the ease or difficulty of designing complete contracts and making the transition from direct public management to markets of public service provision.[26] The service characteristics that matter (shown in Figure 1) should influence where public service markets are introduced and the degrees and types of regulation used.

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[24] A straightforward cash transfer to fund education would be likely to lead to wealthier parents 'topping up' their expenditure, leading to school intakes being more closely tied to family income. The current system, meanwhile, heavily encourages parents to opt into the state funded system due to the degree of public subsidy (which can't be received by those opting out) – encouraging more varied intakes.

[25] Blatchford, K., and Gash, T., *Testing New Commissioning Models: A Guide to Help Policy Makers Learn about Publicly-funded Markets*, Institute for Government, London, 2012, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/testing-new-commissioning-models

[26] Gash, T., and Panchamia, N., *When to Contract: Which Service Features Affect the Ease of Government Contracting?* Institute for Government website, January 2013, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/when-contract

Figure 1: Service characteristics to consider when applying market mechanisms in public services

In order to assess…	…Ask	Work Programme	Academies	Social Care	Probation (Trusts)
The appropriateness and effectiveness of user choice mechanisms	Do consumers face high switching costs?	N/A	Problematic	Highly Problematic	N/A
	Are consumers often involved in distress purchasing?	N/A	Unproblematic	Highly Problematic	N/A
	Is the service a merit good?	N/A	Problematic	Problematic	N/A
The costs and risks of using market mechanisms, and the need for regulation to mitigate these risks	Is it difficult to measure the value added of providers?	Problematic	Problematic	Problematic	Highly Problematic
	Are service outcomes highly dependent on the performance of other services?	Problematic	Problematic	Problematic	Highly Problematic
	Does delivering the service require investment in highly specific assets?	Unproblematic	Problematic	Problematic	Unproblematic
	Is the service characterised by high demand uncertainty?	Problematic	Unproblematic	Unproblematic	Problematic
	Is the service characterised by high policy uncertainty?	Unproblematic	Unproblematic	Unproblematic	Highly Problematic
	Is the service essential for government's ultimate decision-making or coercive authority?	Unproblematic	Unproblematic	Unproblematic	Problematic

RAG Rating Key

- Highly Problematic
- Problematic
- Unproblematic
- N/A

Difficulties in introducing market mechanisms in a particular service do not necessarily mean that they are inappropriate – and indeed, many of the risks we identify will also make it more difficult to manage services directly. However, commissioners should understand these risks and identify mitigating actions that can help reduce those risks. For example, if service outcomes depend on the performance of other services, the commissioner could partner with a public sector partner to co-commission a bundle of services that deliver multiple outcomes. Further examples of potential mitigations are provided in the Institute's *When to Contract*[27] report and outlined in Figure 2.

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[27] Gash, T., and Panchamia, N., *When to Contract: Which Service Features Affect the Ease of Government Contracting?* Institute for Government website, January 2013, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/when-contract

Figure 2: Sample of possible mitigating actions in response to specific contracting risks

...Ask	If 'yes', consider retaining the service in-house or the following actions
Is it difficult to measure the value added of providers?	• Use individual choice as a proxy for quality • Retain a public sector comparator • Collect data to generate reliable performance and counterfactual models
Are service outcomes highly dependent on the performance of other services?	• Identify functions that facilitate coordination and keep in-house • Bundle functions together in one aggregate contract • Specify and reward desirable collaborative behaviour
Does delivering the service require investment in highly specific assets?	• Own the asset and only contract out operation • Negotiate long-term contracts • Minimise risk of policy and demand uncertainty
Is the service characterised by high demand uncertainty?	• Negotiate payment caps and minimum income guarantees • Make capital investments and only contract out service operation
Is the service characterised by high policy uncertainty?	• Achieve a broad and cross-party consensus • Design short, flexible contracts • Keep contracted functions at arm's length from political influence
Is the service essential for government's ultimate decision-making or coercive authority?	• Retain service in-house

The types of regulation and government activity required to ensure effective delivery of public services through market mechanisms are varied. During the course of this project, the Institute created a framework which captures the key functions that we believe government must either perform itself, or ensure someone else is performing, to achieve its objectives. This was developed in two ways.

- First, 'bottom-up' by identifying the functions that government and its agencies currently perform in a range of public service markets; creating logical groupings for these functions (and renaming them); and then identifying the key goals that each function supports.
- Second, 'top-down', drawing on the economic literature of regulation. This framework is shown in Figure 3 and represents just one way of thinking about government's goals and functions in relation to public service markets.

Figure 3: Market stewardship goals and functions
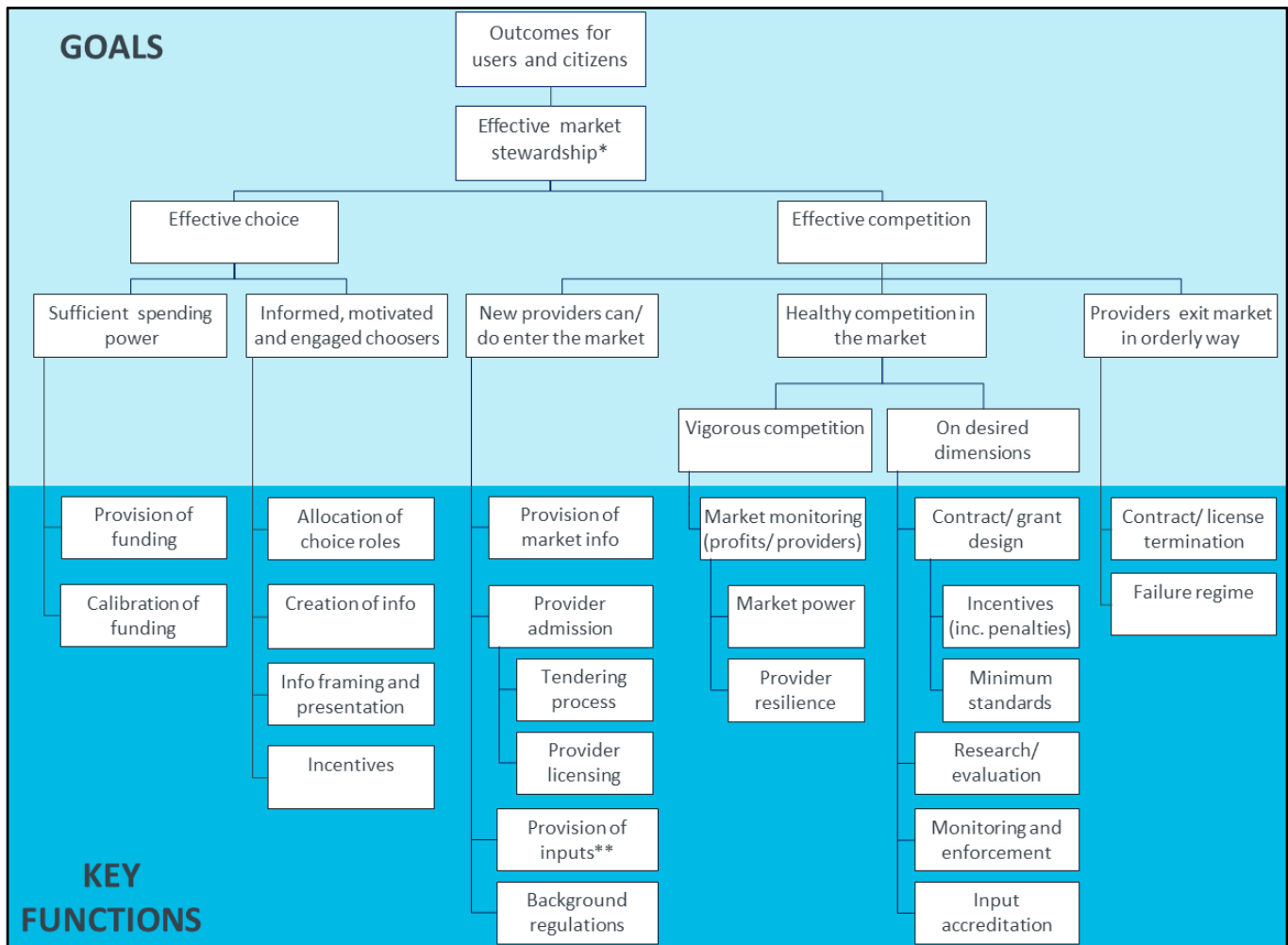
* Assessed against democratically-determined goals (e.g. quality, economy, equity)
** Inputs might include assuring access to a professionally accredited workforce; infrastructure etc

Source: Institute for Government framework based on economic literature and bottom-up analysis of key functions performed by departments where market mechanisms are deployed

We use the term 'market stewardship' to describe the government's overall role in relation to public services where market mechanisms play a central role. In these public service markets, the government does not directly control the way services are delivered. The outcomes are instead determined by the interaction of service providers, service users and the design of the market itself (e.g., the amount of 'money' each user has.)

This requires government to adopt the mind-set and approach of a system (or market) steward.[28] This involves policymakers:

- engaging closely with users, provider organisations and other interested parties across the system to understand needs, objectives and enablers of successful delivery
- setting the 'rules of the game' and allowing providers and users to respond to the incentives this creates
- constantly monitoring the ways the market is developing and how providers are responding to these rules, and the actions of other providers
- adjusting the rules of the game in an attempt to steer the system (much of which is, by design, beyond their immediate control) to achieve their high-level aims.

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[28] Hallsworth, M., *System Stewardship: the future of policy making?* Institute for Government, London, 2011, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/system-stewardship

The term is not used widely in government circles but we believe it is a useful way to think about how government should design and oversee public service markets because it emphasises:

- the need for constant vigilance and sensitivity to how the market is developing – government needs to dedicate appropriate resource and attention to understanding how the market is working, and how it responds to changes
- the need for ongoing, iterative and piecemeal adaptation – the outcomes of complex systems are inherently unpredictable which makes system-wide reforms a leap in the dark, in which the learning that has occurred through past adaptation is lost
- government's ultimate responsibility for how the market is performing, while also appreciating the lack of **direct** control that government has – in David Cameron's words, rather than formulating specific plans to achieve particular aims, policymakers instead 'create the conditions in which performance will improve'.[29]

Definitions for terms used in this report

There is no common professional language for discussing 'markets' in public service provision and a range of terminology is employed across different areas. We provide definitions for the terms we use in our work below.

Market stewardship: departments have an important role in supporting the effective delivery of public services through market mechanisms. They must perform a set of key functions (see Figure 3) and iteratively engage with providers of public services to steward the market towards producing desired outcomes. The term emphasises the long-term oversight of market mechanisms, as well as the commissioning process (see below).

Commissioning: the process of assessing the needs of people or users in an area, designing and specifying the services to meet those needs, and choosing the delivery mechanism to secure an appropriate service while making best use of total available resources.

Outsourcing: the transfer of activities or services that are currently provided in-house to external suppliers. Organisations usually do this to concentrate on what they do best and reduce overall costs. Also known as 'contracting out'.

Procurement: the specific aspect of the commissioning cycle that focuses on the process of buying goods and services to maximise efficiency and value for money from initial advertising through to final contract arrangements.

Privatisation: the process by which ownership of government enterprise is fully transferred to the private sector. The newly-created private company recovers most if not all of its revenues from the general public and private sector customers. Government's role shifts to setting up regulatory agencies and holding the regulator to account for its performance. We do not examine privatisation in this report but it is important to note the difference between 'privatisation' and 'outsourcing'.

Quasi-market: originally coined by Professor Julian Le Grand, the term 'quasi-market' describes a series of public service reforms introduced in the late 1980s. These reforms were market-like because they introduced a split between the purchasers and providers of public services, and competition between providers. Le Grand added the prefix 'quasi' however, to emphasise some important differences with conventional markets: providers are not necessarily profit-maximising firms (they may be state-owned or charitable organisations); choice may be exercised on behalf of the user; and, users 'spending power' is determined by the value of a voucher or earmarked budget, rather than their wealth.

What do the public think?

There is a wide body of polling which captures public attitudes to this shift towards markets in public services. This polling consistently shows the following.

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[29] David Cameron's speech to Civil Service Live, 8 July 2010

1. **The public care more about quality of provision than who provides their services.** A Populus survey published in July 2012 found that 75% of people agree that 'the most important thing is to have high-quality, free, public services not who is involved in running them'.
2. **The public support choice.** 2009 research from the British Social Attitudes (BSA) survey concluded 'There is widespread public support for the idea that people should be able to exercise choice when using public services'.[30] It is not known how much the public value choice in different services however – so it is less clear how much users would be willing to pay for increased choice.

The public are less comfortable with private and voluntary sector provision in some public services than in others.[31] Those services most associated with the state – such as prison and probation services – are often seen as best provided by the public sector only.[32] As ever, however, different survey questions can achieve apparently contradictory results:

1. A poll by ComRes carried out for the Confederation of British Industry (CBI) and the Association of Chief Executives of Voluntary Organisations (ACEVO), found that over 70% agreed that a variety of different providers would be more successful than just one provider at coming up with new ways of doing things, reducing costs, and ensuring good customer service.[33] Yet only 50% agreed with the statement that 'public services have more to gain than lose from making use of the expertise of private and voluntary sector organisations'.[34]
2. A majority of people in Britain (68%) believe that parents should have a 'basic right to choose' when it comes to schooling (BSA 2010). Yet only two in 10 people in Britain support a system whereby 'schools vary so that parents can choose what's best' (BSA 2007).[35]
3. Fifty per cent also believe that 'in Britain today parents have a duty to choose the best possible school for their child, even if this means schools in the local area might suffer' (BSA 2010). More than six in 10 (63%) believe parents ought to send their child to 'the nearest state school' (BSA 2010).[36]

How effective is government design and oversight of public service markets?

As noted above, our research did not involve a rigorous examination of the outcomes produced by each sector. Neither did it attempt to rate the performance of each sector – for example, through cross-national comparisons – nor attempt to answer the question of whether market mechanisms are a preferable delivery model to direct public sector management.

However, we did attempt to understand in broad terms how each sector was felt to be performing well and less well. Often, our interview respondents highlighted various dimensions of performance – for example, efficiency, quality and innovation – and discussed their sector's overall performance as being an attempt to balance between these dimensions as effectively as possible. To caricature, the Work Programme was felt to have driven cost reduction effectively but not led to dramatic service innovation focused on quality improvement. The Academies Programme was felt to be driving considerable innovation – for example, the development of distinctive subject specialisms and ethos by individual schools – but interviewees were less certain about the system's efficiency. The social care market was seen as being highly efficient in delivering care at low cost, but driving poor outcomes because of the lack of integration with public health services. And probation trust commissioning (soon to be overhauled by a major national outsourcing programme) appeared to drive considerable innovation but there was little confidence about either effectiveness or value for money.

Such simplifications are not always helpful but it is important to recognise that each sector has a radically different look and feel. This is partly because the history and objectives for each sector have varied significantly. The social

[30] National Centre for Social Research, *British Social Attitudes 25th Report,* January 2009, retrieved 8 June 2013, http://www.natcen.ac.uk/study/british-social-attitudes-25th-report/our-findings

[31] Worth, S., *Do the Public Back More Reform of Public Services? An Overview of the Latest Opinion Research*, Policy Exchange website, September 2012, retrieved 8 June 2013, http://www.policyexchange.org.uk/publications/category/item/do-the-public-back-more-reform-of-public-services

[32] NCVO, Reform quantitative poll: attitudes to private sector involvement in public services, May 2011, retrieved 15 July 2013, http://www.ncvo-vol.org.uk/sites/default/files/Poll.pdf

[33] ComRes Poll Digest, ComRes website, 2012, retrieved 16 July 2013, http://www.comres.co.uk/poll/698/cbi-provider-diversity-poll.htm

[34] Populus, Private Companies and Public Service Survey, Populus website, 2012, retrieved 16 July 2013, http://www.populus.co.uk/uploads/OmPrivate_Public.pdf

[35] Summarised in Exley, S., *Research Briefing: Public attitudes to school choice and diversity in Britain*, 2013

[36] Summarised in Exley, S., *Research Briefing: Public attitudes to school choice and diversity in Britain*, 2013

care market only came into existence, for example, after a series of central government reforms in the 1980s and early 1990s – all aimed at curbing the rapidly rising costs of care for the aging population. Likewise, the Work Programme was implemented at a time of government expenditure reduction, leading to an emphasis on cost that previous programmes for the unemployed (for example, Flexible New Deal) did not have to the same extent. The Academies Programme was originally conceived as a way of turning around failing schools, and the current programme retains a focus on quality improvement, even though most schools now converting to academy status are already effective schools. The market in probation services has been shaped by the state's relative reluctance to invest in rehabilitation services and the consequent relative importance of the voluntary sector.

These distinct histories have led to important differences in government's approach to the design and oversight of the 'market' in each service area. Most noticeable are the differences between systems designed to encourage competition based largely on price (for example, social care and employment services) and systems that provide a fixed price to providers and ask providers to compete on quality (as in the academies system).

Differences in performance also relate to the inherent characteristics of each service area. As highlighted above, services have different natural properties affecting the appropriate role for government and users, and the ease of incentivising independent providers to perform. Figure 4 shows clearly that the services we examined all have different natural properties. It shows too that there is a common thread, which is that there are a number of predictable difficulties that government will encounter when overseeing the use of market mechanisms in each sector.

Figure 4: Service characteristics in the four service areas examined

In order to assess...	...Ask	Work Programme	Academies	Social Care	Probation (Trusts)
The appropriateness and effectiveness of user choice mechanisms	Do consumers face high switching costs?	N/A	Problematic	Highly Problematic	N/A
	Are consumers often involved in distress purchasing?	N/A	Unproblematic	Highly Problematic	N/A
	Is the service a merit good?	N/A	Problematic	Problematic	N/A
The costs and risks of using market mechanisms, and the need for regulation to mitigate these risks	Is it difficult to measure the value added of providers?	Problematic	Problematic	Problematic	Highly Problematic
	Are service outcomes highly dependent on the performance of other services?	Problematic	Problematic	Problematic	Highly Problematic
	Does delivering the service require investment in highly specific assets?	Unproblematic	Problematic	Problematic	Unproblematic
	Is the service characterised by high demand uncertainty?	Highly Problematic	Unproblematic	Unproblematic	Problematic
	Is the service characterised by high policy uncertainty?	Unproblematic	Unproblematic	Unproblematic	Highly Problematic
	Is the service essential for government's ultimate decision-making or coercive authority?	Unproblematic	Unproblematic	Unproblematic	Problematic

RAG Rating Key

- Highly Problematic
- Problematic
- Unproblematic
- N/A

Source: Institute for Government analysis

Note: Assessments are, to a significant degree, subjective; please see extended case studies for explanations of our assessments

In each service area, we assessed how far government had overcome the inherent difficulties in designing and overseeing effective markets of provision. We focused on identifying performance against the criteria we outline above as being essential for markets in public services to drive positive outcomes:

- informed choice, appropriate funding
- opportunities for entry and expansion
- competition on the desired dimensions
- free but orderly exit of failing providers.

Detailed assessments of our findings are found in Section 2 of this report but here we draw out some common themes and areas of difference.

Figure 5 provides an impressionistic overview of our findings, which are described further below. It is important when looking at the chart below not to over-interpret the high proportion of amber ratings which only indicate the potential for improvement, rather than profound and urgent problems.

Figure 5: Impressionistic representation of issues in areas investigated

	Work Programme	Academies	Social Care	Probation (Trust commissioning)
Sufficient and appropriately calibrated funding	Problematic	Problematic	Highly Problematic	Problematic
Informed, motivated and engaged choosers	N/A	Problematic	Problematic	Problematic
New providers can/do enter the market	Problematic	Unproblematic	Unproblematic	Problematic
Healthy competition in the market (on desired dimension)	Problematic	Problematic	Problematic	Problematic
Providers can/do exit the market in an orderly way	Problematic	Problematic	Unproblematic	Unproblematic

RAG Rating Key

- Highly Problematic
- Problematic
- Unproblematic
- N/A

Source: Institute for Government analysis

Sufficient and appropriately calibrated funding

In theory, there is an optimal level of consumption of public services, at which neither lower nor higher consumption is economically efficient. However, the setting of overall funding levels in any public service area is in practice extremely difficult – one that lies largely outside the scope of this report and relates to public and political priorities as well as practical reasoning.

Nonetheless, we did observe that overall funding levels were of critical importance in all of the markets we studied. Tight budgets can encourage efficiency but it is clear that market mechanisms do not change the general rule that 'you get what you pay for'. In the case of social care, for example, funding levels are clearly inadequate to achieve government's stated objectives in this area. *The Care and Support White Paper*[37] has set the objective of intervening earlier to help people retain their independence and to avoid more expensive NHS treatments. However, because local authorities have had their funding reduced, they have been forced to reduce the proportion of people eligible for publicly-funded support. In 2005, half of councils provided support to people assessed as having 'moderate' needs, but by 2011 the figure had fallen to 18%.[38] This means that they are increasingly only providing care for higher levels of need, usually in the later stages of life. Michelle Mitchell, Charity Director-General at Age UK, pointed out the irony of the situation:

> Local authorities are increasingly only delivering the things they are legally obliged to… They only have enough money for people to go into care homes, for those in critical need. So while the policy objective tells you that you need to invest in intervention… what's actually happening is that local authorities are increasingly only focusing on the very, very highest in need. People are going into hospital, there isn't wrap-around support getting them out of hospital, so they either go back into hospital or into a care home.

Our interpretation of the Work Programme suggests that it too may be suffering from sub-optimal funding levels. There is disagreement in the sector on this but the balance of evidence suggests to us that it is quite likely that

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[37] Department of Health, *Caring for Our Future: Reforming Care and Support White Paper*, Gov UK website, 2012, retrieved 5 June 2013, https://www.gov.uk/government/publications/caring-for-our-future-reforming-care-and-support

[38] Care Quality Commission, *The State of Care and Adult Social Care in England 2011/12,* CQC website, 2012, retrieved 5 June 2013, http://www.cqc.org.uk/public/reports-surveys-and-reviews/reports/state-care-report-2011/12

unemployed people who could be cost-effectively supported into employment are not being helped due to funding decisions. Providers have an interest in arguing that services are not adequately funded of course, but the case is put succinctly by a director of one contractor: 'These contracts are on the edge of being financially viable. You have to aggressively cream and park.'

We also noticed that funding levels sometimes varied for arbitrary reasons that could distort competition. This is most apparent in relation to secondary education where an academy's funding varies based on geographical factors that do not affect the costs of service provision. This means schools on two sides of a county boundary who compete for pupils can receive significantly different amounts of funding per pupil. Providers are therefore not competing on a level playing field and may simply be rewarded for their different starting funding levels rather than their performance. One head teacher described such a situation to us: 'You only need to go across the border into [name of town removed], so the same areas that over a third of our kids come from… they have about 700 students (and no sixth form) we have 1,300 students and their budget is almost identical to mine.'

Informed choice

For competition to drive improvement, those choosing their (or our) public service providers need to make informed choices. In two of the areas we looked at – secondary education and social care – users are being encouraged to take a more active role as consumers. The Coalition's policy asks parents and pupils, older people and carers to demand more efficient and effective services that better suit their needs, and for providers to respond to these demands to attract and retain 'customers' and the funding that follows them.

We found several examples of government interventions that have been valuable in informing and framing user choice. Published inspection ratings of schools and care homes are an obvious example. Results of standardised tests and, more recently the 'contextual value added' ratings of schools are further examples. A number of local authorities are also actively deploying or considering providing additional support for those choosing schools that they felt were encouraging pupils towards effective schools.

Nonetheless, there remain a number of significant barriers to informed choice, as highlighted in the recent Boyle Review of choice in public services.[39] In social care, users lack both the information to make informed choices and, often, the support in navigating the choices that need to be made. A major problem here is gaining credible comparative information, as the Department of Health has recognised with its commitment to a national online directory in the *Social Care White Paper*. Another significant problem is a shortage of signposting and low awareness of options available. As the National Audit Office summarised in a recent review of the sector, 'Users had difficulty judging the quality of service in care homes until they were resident, and the lack of information on alternative providers meant they had little option but to stay with a provider, regardless of the quality of the service provided.'[40]

These barriers are exacerbated by structural barriers to choice relating to inherent service properties and government's unwillingness to fund excess market capacity. Choice of schools will always be somewhat constrained by the number of schools nearby and the fact that these schools will likely be oversubscribed, for example. We interviewed a director of a rural local authority who said: 'It's just impossible to offer choice on that scale. That's a problem with the market-focused viewpoint. That's fine if you can generate a market, but actually in many parts of rural England, you can't.'

Publicly-funded care options meanwhile, are severely limited by funding constraints. Councils often 'block buy' care services to get price discounts but this practice, while more efficient in the short run, clearly limits the number of affordable options for users. Where funding is extremely low, even those who have been provided with 'individual budgets' to choose their own care can end up with very few options. For example, those with complex care needs and those suffering dementia and mobility problems, receive higher overall funding so have more flexibility regarding the care packages they contract – though they are often less able to exercise their choice without additional support.

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[39] Boyle, D., *The Barriers to Choice Review: How are People Using Choice in Public Services?* Gov UK online, 24 January 2013, retrieved 5 June 2013, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/80070/Barriers_to_choice_review_0.pdf

[40] *NAO, Oversight of User Choice and Provider Competition in Care Markets, NAO website, November 2011, retrieved 8 June 2013,* http://www.nao.org.uk/report/oversight-of-user-choice-and-provider-competition-in-care-markets/

Figure 6: Proportion of people who 'selected the school/provider of support or social care services/GPs surgery/hospital from a number of options' (%, N=1485)
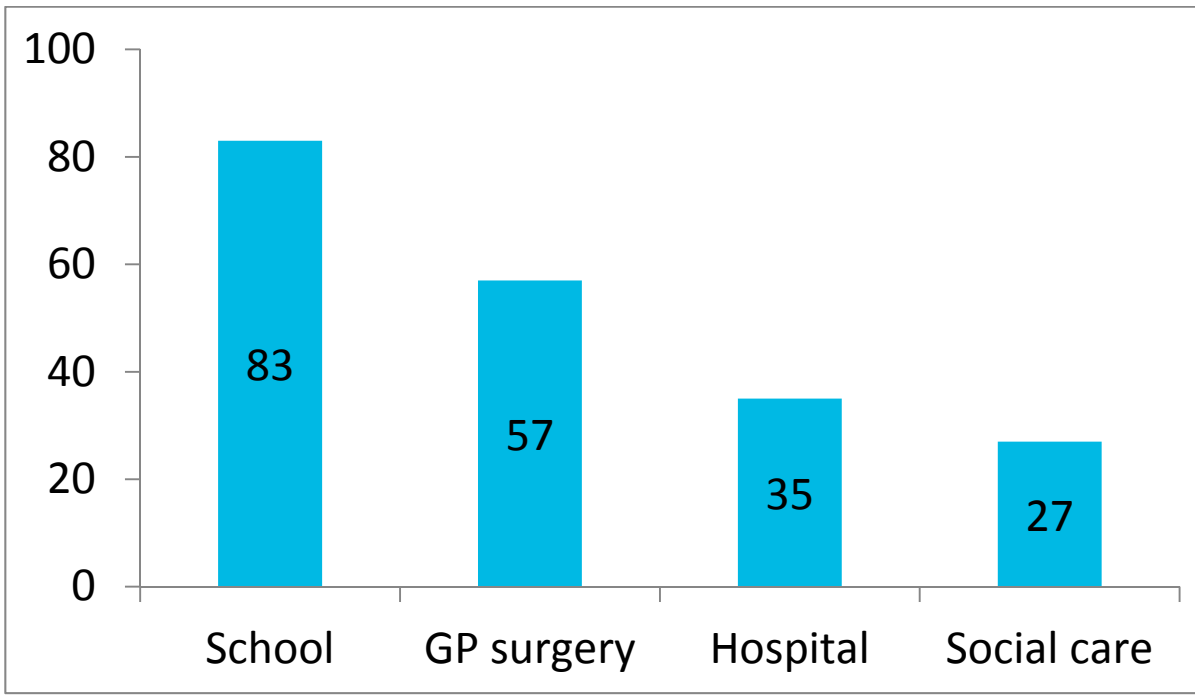
Source: Ipsos MORI poll for Boyle Barriers to Choice Review

Where public sector commissioners choose on users' behalf – in employment services and probation services but also, to a significant degree in social care – they too are not always well informed. In the commissioning of rehabilitation services, knowledge of the effectiveness of different providers in reducing re-offending (or achieving other outcomes) is extremely weak. Governors of failing schools currently select the management team they believe can transform the school's performance. But they too often lack access to robust information regarding the performance and capability of different academy chains. The Department for Education (DfE) is aware of, and planning to address, this gap but it remains significant. Elsewhere, knowledge of provider performance is less problematic. In employment services, commissioners are reasonably confident that they understand the relative performance of different providers, as are those providers who sub-contract work to specialist operators. However, there remain concerns that methods for comparing the performance of providers working with different local labour market conditions have not yet found adequate ways of separating provider quality and labour market effects.

Low barriers to entry

Competition is most likely to drive improvement if promising providers are allowed to prove they are effective and if good providers are able to expand sustainably. In the service areas we examined, there were a number of providers and experts who complained of barriers to entry but overall we did not observe severe problems in this regard except in probation services. Here, new providers were reluctant to invest in developing new rehabilitative services offerings, largely because short contracts (often of only 12 months) made flows of work uncertain and there were seen to be few growth opportunities. These barriers have subsequently been removed and several providers who have not previously worked in the sector are now bidding to provide the probation services at a regional level following Justice Secretary, Chris Grayling's commitments to outsource the vast majority of probation services.

There were some barriers to entry in other sectors. The main issues highlighted to us related to the involvement of smaller providers in the Work Programme. Many felt that bidding processes for national contracts were excessively costly, partly due to frequently changing requirements and subsequently protracted timescales. 'Bid teams', which do not even exist in the smallest providers, were often kept busy for months with detailed data requests, which both put off providers from bidding for contracts initially and then led to some providers exiting the bidding process leaving reduced levels of competition. Several providers and potential providers of Work Programme contracts were also deterred by the financing requirements that accompany 'payment by results' contracting. Smaller and less experienced providers sometimes lacked the commercial experience to attract investment – something even experienced large operators found challenging given the financial markets' initial discomfort with the programme.

Elsewhere, there were notable regulatory barriers that prevented new service offerings – for example, provision of care in mixed-age settings. These barriers were, however, usually the result of deliberate (if arguably unhelpful) attempts to prevent a particular type of service being provided. Such barriers clearly reduce market innovation (and therefore should not be imposed lightly) but they are usually taken due to safety or public acceptability concerns. The most obvious regulatory barrier we encountered was the prohibition on allowing profit-making providers to compete in the publicly-funded secondary education market. While there are already several significantly-sized chains of non-profit providers and many more small chains emerging, this decision clearly limits competition and diversity.[41]

Providers also faced moderate barriers to expansion in some sectors. Planning regulations (and straightforward space constraints) for example, clearly limit the expansion of some effective schools and care providers, although expansion is possible through federation and the creation of chains. Academies are currently prohibited from borrowing above a certain level, limiting their freedom to make capital investments.

In addition, we observed strong advantages to incumbency in employment services and secondary education (see barriers to exit below) which limit the opportunities for effective providers to grow.

Competition on desired dimensions

Competition is most likely to drive improvement where incumbent providers are competing on the desired dimensions. However, in every sector we found that providers sometimes responded in undesirable ways to the reward structures created by users, commissioners and regulators. Common 'gaming' behaviours included 'parking' service users with complex needs and 'creaming' users who are easier to support, and therefore more profitable to serve.

Such gaming was most apparent in the Work Programme where the combination of low fees and specific design choices in the 'payment by results' system of reward acted to discourage investment in helping those who were less likely to get back into work swiftly. Providers responded to incentives (and loopholes) in all sectors, however. One of our interviewees argued, for example, that a small minority of care homes are far too quick to send their residents to hospital for minor conditions, developing a mentality of 'just ring 999' to transfer costs onto NHS providers.[42]

Academies told us they knew of (or were) schools that encouraged their students to take vocational qualifications where they would boost overall exam results, even where they did not feel that these were the most valuable options for students. Many academies felt compelled too to focus disproportionate resources in helping students on the so-called C/D borderline, due to the importance that government and parents attach to schools' success in securing students with five or more A-Cs at GCSE level. Academies have also, in rare cases, been known to deliberately or accidentally skew their intakes towards easier-to-teach pupils, both by recruiting from effective 'feeder' schools and from discouraging less able pupils from attending. The 'pupil premium' is notionally intended to encourage schools to embrace and provide additional support to pupils with greater needs. However, most head teachers we spoke to highlighted that the premium is currently far from adequate to reflect the true additional costs of providing high-quality support to the most challenging students.

'Gaming' does not only take place in competitive systems, of course. Indeed, the perverse consequences of performance management regimes in public service delivery are well documented.[43] But it is noticeable that our research did suggest that gaming can be accentuated by fiercely competitive environments. As one head teacher told us, 'This is the first year I've ever got in private tuition for kids on the C/D borderline. I don't like to do it... but I have to.'

Low barriers to exit

Competition is most likely to drive improvement where those providers who aren't providing effectively are forced to contract or stop providing services. However, we saw reluctance to force underperforming providers out of these 'markets' in service provision, partly as a result of a lack of confidence that government can manage transitions between different service providers without causing excessive disruptions to service users.

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[41] As noted above, there are good theoretical reasons why profit-making providers might be excluded from public service provision, particularly where contracts are incomplete but little empirical evidence to allow us to determine the merits or demerits of this approach

[42] Interview 018

[43] See Gash, T, Hallsworth, M, Ismail, S, and Paun, A, *Performance Art: Enabling Better Management in Public Services*, Institute for Government website, December 2008, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/performance-art

In secondary education, our analysis suggests that some schools are able to perform poorly for extended periods before being taken over by alternative management, particularly where they operate in favourable catchment areas. Financially failing schools are also seen by many as being allowed to continue under the same management for too long – even though it is known that financial difficulties are very often followed by downturns in school performance as cost-cutting measures are introduced.

In commissioned services, including social care, employment and re-offending services, we heard that some commissioners are too attached to incumbent providers with whom they have relationships. Historically, the Department for Work and Pensions (DWP) has had a particularly poor record of cutting short provider contracts, even where they don't meet minimum standards. The department is promising to take more decisive action against Work Programme providers who are still struggling two years into the programme.

However, it may surprise observers of the collapse of Southern Cross Healthcare that we did not see strong evidence that orderly exit was a major problem for residential social care services. Southern Cross' collapse was not itself the disaster that it might have appeared at first glance. Ultimately, the firm was bought and, though the uncertainty worried those in Southern Cross homes and their families, service disruption for users was limited. There was no state bail-out – something which might have had the perverse effect of encouraging excessive risk-taking by other providers. The successful winding down of Southern Cross is arguably more a result of luck than judgement. The main reason that orderly exit is possible in social care services is that most businesses which fail will be bought as going concerns, simply because the care sector is expanding and because conversion to residential accommodation, though not expensive, is sufficiently costly to act as a deterrent to asset-stripping.

More problematic may be dealing with future financial failures of academies and academy chains, particularly if borrowing opportunities are extended. Currently school governors bear a minimal liability where schools go bankrupt and some experts are concerned that the costs of financial mismanagement by academies that are part of chains will be picked up by taxpayers rather than the chains overseeing the failure.

Implementation difficulties

The Department for Work and Pensions' Work Programme was implemented rapidly following the 2010 General Election. The Academies Programme was also implemented at pace under the coalition – and was essentially a new programme, albeit one building on the brand and design features of the Labour Government's programme of the same name.

The rapid pace of implementation meant that service users could quickly benefit from any programme benefits but our research confirms the findings of previous reforms that pace contributed to – or at the very least was accompanied by – considerable implementation difficulties. The NAO review of the Academies Programme found that the costs of converting schools to academy status significantly exceeded expectations.[44]

Their early review of Work Programme implementation was complimentary about the way in which DWP had consciously addressed some of the weaknesses of previous programmes but pointed out:

- a lack of testing of the programme's assumptions
- high costs for the termination of existing welfare to work contracts (over £63 million)
- IT difficulties.

They explain, 'The IT project to support the programme was not fully functional when the programme was launched. A consequence is that the department will not be able, until March 2012 at the earliest, to carry out automatic checks to confirm that people who find work have stopped claiming benefits.'[45]

We found that failure to test assumptions and reluctance to phase programme roll-out significantly limited the department's ability to anticipate reasonably predictable difficulties. Given the reliance of the Work Programme on its model for estimating performance and referrals, it should have been opened up to external scrutiny, including by providers. The disruption of moving Work Programme providers from one part of the country to another should also have been more carefully factored into the department's planning.

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[44] See NAO, *Managing the Expansion of the Academies Programme*, NAO website, November 2012, retrieved 8 June 2013, http://www.nao.org.uk/report/managing-the-expansion-of-the-academies-programme/

[45] See NAO, *Managing the Expansion of the Academies Programme*, NAO website, November 2012, retrieved 8 June 2013, http://www.nao.org.uk/report/managing-the-expansion-of-the-academies-programme/

In the Academies Programme expansion, it is clear that the consequences of reform had radically different effects in different parts of the country. In counties where schools were allowed or encouraged to implement age-range changes after converting to Academy status, there has been a dramatic (though unsustainable) increase in levels of competition. Elsewhere, specific chains have already achieved the dominant share of school provision in some areas. In other places still, there has been little discernible change in terms of choice for parents or competition. These different consequences were felt by many we interviewed to have been insufficiently appreciated, and the consequences of these differences have not been planned for.

The approach to implementation in both these programmes also meant that neither programme can be easily evaluated. For this reason, debates about the relative effectiveness of each programme take place on weak foundations, limiting the capacity for the departments to learn and improve future programmes accordingly – and also limiting our capacity to identify and hold to account those responsible for success and failure.

Were there problems cutting across the sectors examined?

In the course of our research, we heard significant concerns regarding the co-ordination of services. In the Work Programme, providers who believed they offered cost-effective services for users with multiple needs argued that they had been overlooked for work because commissioners and 'prime contractors' were excessively focused on a narrow set of departmental objectives, rather than overall outcomes and value for government. All sectors, meanwhile, complained that other publicly-funded services were occasionally obstructing their efforts. For example, employment service providers would complain that ex-offender probation appointments could clash with job interviews and further education colleges did not have the incentives to deliver skills that employers value.

These barriers to effective cross-sector working can at times be overcome, however. For example, some probation trusts have develop joined-up approaches to offender management – in one area, ex-offenders are placed on a long-term residential programme at a Care Farm, which is contracted to deliver the drug treatment orders of the court, a supervised, structured programme of farming-related activities and skills and educational training – but these types of practices were not universal. Several interviewers argued that co-ordination difficulties were exacerbated where profit-making providers were involved in service delivery. They may, for example, be tempted to withhold information that is costly to share or could financially disadvantage them. Meanwhile, public and voluntary sector organisations are unlikely to be willing to provide cost-free services for the benefit of profit-making providers and may even hijack the efforts of these providers, if they mistrust their intentions or would like to be seen as more effective than them.

Others, however, felt that the introduction of profit-motivated providers could offer a route for overcoming co-government co-ordination problems. Many of the UK's largest public service companies provide a range of government services in specific geographic areas – and some interviewees argued that they would be incentivised to find synergies across their service portfolios.

This may indeed be happening to some extent. A number of large providers who have a broad service offering in particular areas of the country do appear, for example, to be achieving economies of scale that allow them to regularly undercut competitors, for example. However, while this makes these providers attractive to commissioners, this shift also threatens to undermine levels of competition. If individual providers come to dominate specific parts of the country, government may become vulnerable to price increases across a range of services in future. This is a particular concern given that we heard evidence that many companies have explicit strategies to gain economies of scale in certain regions of the country.

What did we learn about the respective merits of public, private and voluntary sector provision?

Often, the public debate about public service markets is framed in terms of the respective merits of public, private and voluntary sector providers. Some argue that private providers are inherently more efficient due to their management practices and the incentive of a profit motivation. Others argue that the experience and ethos of public sector or voluntary sector providers make them inherently superior.

Our research did not look extensively at the respective performance of organisations from different sectors. However, our evidence did appear to show that performance varies as much (or more) within sectors as it does across sectors. Private providers of employment services who sub-contracted their work to others told us 'whether a provider is public or private makes no difference' and commissioners of social care services similarly told us that they had both good and poor private and voluntary sector provision in their areas.

Previous research has found similar results. As the Julius Review of the Public Service Industry put it after conducting a series of interviews with providers, 'All three sectors disputed the reputed advantages of the other two and, indeed, there is little empirical evidence to support such stereotypes. The variation within each sector is generally more striking than the variation across sectors.'[46]

This appears to suggest the fact of competition itself (and the way that competition is constructed) which matters more than the motivation of the organisations competing. It also suggests that attachment to any particular sector is inappropriate.

However, it is important to acknowledge that there might be good theoretical reasons why government would still want to contract with providers who are mission driven. First, mission-driven organisations may attract mission-driven individuals who may donate additional unpaid labour.[47] Second, and arguably more feasibly, mission-driven organisations may be less likely to 'game' public service contracts that are often incomplete. Mission-driven organisations may also concentrate not only on delivering narrowly-defined contractual specifications but on producing wider goods. Ironically, these benefits will always be invisible because they are not measured – and refusal to game or focus on narrow objectives may in fact lead to mission-driven organisations performing less well against certain metrics. This (seemingly insoluble) difficulty may, along with public attitudes, explain continued political attachment to ensuring voluntary sector involvement in public service delivery.

Why do levels of effectiveness vary?

Many of the problems we identified in the four sectors we examined, summarised above, will be familiar to practitioners, policymakers and academics. However, unlike much other research in this area, our focus was on developing a better understanding of the underlying reasons for the strengths and weakness we observed in terms of outcomes and market design. Again, each sector had distinct service-specific reasons for their strengths and weaknesses but there were a number of important common themes, including:

- **clarity and continuity of purpose**
- clarity regarding government's **roles and responsibilities** in relation to public service markets
- **appreciation of service and market characteristics**
- provider **capability**
- government's **market stewardship and commissioning capabilities.**

Clarity and continuity of purpose

Our interviewees argued that clarity of purpose provided clear benefits in the area of market design and oversight. This is true in all areas of government activity but we heard that there are particular reasons that clear objectives are valuable in this context. Political commitment is highly important in generating the confidence of officials, providers and investors that a market will be established or expanded – and therefore influences the degree of competition and the costs of capital. The ministerial leadership of the then Employment Minister, Chris Grayling, in relation to the Work Programme and Secretary of State for Education, Michael Gove in relation to the Academies Programme, provided clear reassurance in this regard. The social care market, meanwhile, is well established and few expect a major shift in government's attitudes towards private and voluntary sector involvement.

Nonetheless, all the programmes we examined were felt to be subject to some lack of clarity on what they were intended to achieve. Even if ministers and officials in these areas may have been clear regarding objectives, many providers were not. The Work Programme was announced as being an attempt to drive investment and innovation, for example, but had a financial envelope that suggested the focus was heavily on increased efficiency.

In the Academies Programme, meanwhile, it remains unclear whether, how, and to what extent, governments have expected choice and competition to increase standards in schools. Ministerial statements have often emphasised the inherent value of giving parents a choice, meaning that the instrumental value of using it to increase standards may at times have been of secondary importance.[48] It is also unclear to what extent

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[46] Julius, D., *Public Services Industry Review*, Department for Business Innovation and Skills website, July 2008, retrieved 8 June 2013, http://www.bis.gov.uk/files/file46965.pdf

[47] This theory is proposed by Besley and Ghatak 2005 although most evidence shows that voluntary sector employees do not in practice donate more unpaid labour than private or public sector employees – and often donate less (Grout 2009).

[48] Exley, S., *Are Quasi-Markets in Education what the British Public Wants?* Paper prepared for the SPA conference 2012, retrieved 16 July 2013, http://www.social-policy.org.uk/lincoln2012/Exley%20P6.pdf

governments have been trying to create a full quasi-market, as opposed to using competition simply to inject some degree of pressure at the margins of the system. The gradual and piecemeal way in which quasi-market reforms have been introduced over a long period suggests it may not be the former.[49] More recent reforms suggest the latter.

Circumstances, of course, change. But we found – as in other Institute for Government research – that discontinuity of leadership at either ministerial or official levels was highly disruptive.[50] This was particularly apparent in relation to the Work Programme, where both ministerial and official leadership changed in quick succession. Providers felt that the changes at official level left them unable to communicate effectively with the department for a considerable period of time while new leadership was put in place. There was noticeably no succession planning for key personnel.

Roles and responsibilities

We found repeated uncertainty about whose job it was to perform important market stewardship functions. This meant that is was not always clear who was responsible for identifying and addressing significant problems.

Ambiguities are at their most profound in the oversight of the social care market. Here, it is not even clear who is accountable for overall performance of the market. In theory, social care is a locally accountable service funded through the non-ring-fenced elements of local authority grants. In practice, however, local authorities have minimal freedom to determine overall funding levels – both due to a well-documented difficulties in raising local taxation and to the fact that social care accounts for such a significant (and increasing) proportion of total local authority expenditure. In this non-ring-fenced system, central government can argue that councils are diverting money intended for social care to other areas and not driving sufficient value from providers. Meanwhile local government can argue that overall funding levels are inadequate and quality care is unattainable.

There is also a reluctance to assign important stewardship responsibilities decisively. Recently, the Department of Health has advocated a 'sector led' approach to build buy-in across the various agents – national government, the Care Quality Commission, local authorities and providers. This has merits but our research shows that it leads to confusion unless there is a clear and shared understanding of which institution is ultimately responsible for ensuring that collaborative processes achieve results. For example, the Department of Health, the Care Quality Commission, local authorities and providers have all taken steps to improve the supply of information to service users and their families – but this appears to have contributed to confusion and duplication of efforts rather than a system that effectively supports better choices by users and commissioners.

Important stewardship roles were also not clearly assigned in relation to oversight of the academies system. It was not clear who was responsible for ensuring competition, for example. Lack of monitoring of levels of competition combined with the permissive approach to federation of schools has led to the dilution of competition noted above. It is also noticeable that no-one is currently carrying out the task of providing information on academy chain performance, although the department is considering doing so. Without this information, governing bodies – who decide who will take over the management of their school – are likely to find it difficult to understand the relative financial health, academic records, and capabilities of different sponsor chains.

In addition to roles not being assigned however, we found several examples where the organisation charged with the role was inherently inappropriate to carry out the task. It is, in our view, not sensible, for example, to task individual boards of governors with the lead responsibility for selecting the organisation that should take over their school when it fails – as they will always lack the experience, capability, and impartiality required.[51] Our research also suggests that administration of academy admission appeals and investigations of infringements of the admission code also need to lie with a different body – one that is independent of both academies themselves and the political process.

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[49] Sims, S., *The Development of Quasi-Markets in Secondary Education*, Institute for Government website, November 2012, retrieved 8 June 2013, http://www.instituteforgovernment.org.uk/publications/development-quasi-markets-secondary-education

[50] Page, J., Pearson, J., Jurgeit, B. and Kidson, M., *Transforming Whitehall Departments.* Institute for Government, 2012, retrieved 15 July 2013, http://www.instituteforgovernment.org.uk/our-work/more-effective-whitehall/transforming-whitehall

[51] Governing boards are typically not only partly responsible for school failures in the first place but also often have representative of academy chains taking a leading role (affecting impartiality) and will, one hopes, only have to perform the task of changing school management periodically.

Similar problems were found in social care, where, until recently, local authorities were responsible for identifying risks of providers going bankrupt, but in reality lacked the geographic scope to oversee the financial health of regional or national providers.

One cross-cutting difficulty was reconciling the need for political influence in agreeing the goals of market-based delivery models with the need for independent, largely rule-based decision making when it came to assessments of performance and the awarding or removal of contracts. In the case of the Work Programme, for example, there is little ambiguity about market stewardship responsibilities because DWP is essentially responsible for all aspects of market design and oversight. However, while in theory departmental officials should have a clear focus on ensuring value for money over the long term, in practice they are often inherently conflicted. For example, officials knew that ongoing transparency on Work Programme performance data and modelling assumptions was desirable, but were also nervous of the consequences of transparency in terms of individual, departmental and ministerial reputation.

Inadequate appreciation of service and market characteristics

The failure to assign important roles appropriately may relate to an over-estimation of the degree to which basic market mechanisms are sufficient to ensure effective choice, competition and performance. As noted above, each service we examined has natural properties that mean appropriate rules of engagement and significant ongoing oversight of market activity will be required to ensure public service markets deliver their intended outcomes. Excessive, unnecessary regulation can be problematic, but our research suggests that many of those leading the design and oversight of market mechanisms do not place sufficient emphasis on understanding:

- the inherent characteristics of each service
- the extent to which these would work against the desired outcomes for government in a market-like system
- the possible routes for mitigating these biases.

In secondary education, for example, there are a range of barriers to effective competition and plenty of opportunities for chains to develop local monopolies. Government will either need to prevent or overcome these problems – or else find additional mechanisms for incentivising performance beyond pupil choice. In the Work Programme, meanwhile, economies of scale will tend to drive the market towards rapid consolidation – unless active steps are taken to ensure supply chain diversity.

For all core public services, continuity of service is highly valued by users so the financial failure of providers requires careful management. Where assets are owned by independent organisations rather than government there is a risk of moral hazard, whereby failed organisations can exploit public demand for service continuity by demanding either bail-outs (where their services are provided to large numbers of people) or excessive compensation for the purchase of assets. Our research did not give the impression that sufficient contingency planning had taken place in this respect, or indeed that departments always had a clear understanding of the costs of forcing a provider to discontinue its operations.

Provider capability

Many of the strengths and weakness we observed clearly related to provider. This research confirmed the findings of our previous research that new providers take a while to develop their capacity and capability – often taking some time to become more professional and to innovate with their service model. We also found, however, that the actions of commissioners and regulators can significantly accelerate or diminish the pace of this evolution. Provider representative bodies and professional bodies can also accelerate improvements, particularly where they encourage shared learning across the provider community.

Because it can take many years for providers to develop their capabilities, it is important for the expansion of providers to be phased appropriately. This has recently been recognised by the Department for Education, which has urged one academy chain to limit further expansion until it has improved its capabilities to deal with the scale of work it is now undertaking. However, we heard (and recognised) concerns that departments were not sufficiently understanding of the time required for smaller providers to develop their capability and take on increased workloads.

We also heard that national commissioners have opted for contractual arrangements that make it difficult for smaller providers to expand organically and incrementally. For example, some questioned whether sub-contractors in the Work Programme would find it possible to make the significant jump to become 'prime'

contractors. The absence of clear pathways to growth clearly creates risks that small providers will remain sub-scale, even where they have the potential to compete with (or even outperform) larger national players. Equally, big jumps between small and large contracts might lead to smaller providers over-extending – to the detriment of quality.

Market stewardship and commissioning capabilities

It is clear that government is still developing its capacity to design and steward systems that rely on independent service providers.

As the Institute argued in its *System Stewardship* report, the shift towards market-based delivery models necessitates a much more open and iterative engagement between providers of public services (public, private and voluntary sector) and those setting policy or 'rules'. We found, however, that:

- government generally lacked the tools it required to work collaboratively when adjusting system incentives
- tended not to adequately stress-test shifts in approach
- lacked ways of ensuring proposals were informed by business understanding
- did not sufficiently value the types of flexibility that could help the system adapt to unpredictable developments
- failed to demand sufficient transparency of either itself or independent service providers
- focused excessively on reducing upfront costs, to the detriment of quality, diversity and levels of competition.

Government departments also struggle to maintain effective relationships with independent providers. When contracts with private providers are being designed, there is often significant mutual mistrust. Providers may see commissioners as being closed to discussion and complain that legitimate questions or concerns are not dealt with; commissioners express concern that providers are simply pushing for contract designs that will advantage them commercially. As a result, commissioners often ended up designing contracts, and more broadly markets, with little input from the providers who actually deliver the services. In the private sector, firms often find they get the best results by working collaboratively with their suppliers. But in government, concerns for fairness often result in it dealing with a very large number of suppliers for extended periods, making the development of close, collaborative relationships practically difficult. This was particularly the case in the Work Programme.

There were also frequent complaints that commissioning and procurement processes were run in an unprofessional manner. Goal-posts moved too frequently, increasing the costs for both the government and providers involved. CBI research has previously shown that 84% of providers consider that bid costs were having a detrimental effect on competition, and limiting the participation of smaller firms. The most significant reasons given by providers for high bid costs were 'inadequate specification' (62%), followed by the 'absence of a standardised approach' (36%).[52]

Even once providers are selected, however, relationship management approaches often lead to dissatisfaction on all sides. When commissioners find it difficult to assess the contributions of autonomous providers, they often compensate by imposing what providers see as excessive ad-hoc requests for information, even where – as in the Work Programme – government has stated it is only interested in 'results'. Meanwhile, however, commissioners are often reluctant to take decisive steps to demand greater transparency from providers on such things as performance and supply chain management, impose financial or other penalties, and remove contracts. The reasons for this dynamic are complex but include failures to work through what will happen in the case of underperformance in advance, a lack of commercial skills and experience, and risk-aversion in the face of potential legal challenge.

Commissioning organisations don't do enough to encourage co-ordination between providers of related services, as in health and social care, and too often fail to encourage the development of innovative services that meet multiple user needs. This is unsurprising given well documented structural incentives for government organisations to focus only on their own departmental objectives. But the finding does run contrary to the expectations of proponents of outsourcing that the market will by itself help to address co-ordination problems. Our research also suggested that the most innovative approaches to commissioning tended to be the result of local public sector partners working together – with nationally commissioned services not yet demonstrating the same capacity to work collaboratively towards common ends.

[52] Confederation of British Industry, (CBI), *Buying a Brighter Future,* 2012, retrieved 16 July 2013, http://www.cbi.org.uk/media/1830922/cbi_procurement_reform_report_12_november_2012.pdf

All of these problems relate to a combination of processes, personnel, cultures, and incentives. However, we believe there are two fundamental problems: commissioning and market oversight capabilities and the underlying incentives operating within the public sector context.

Commissioning Skills

The National Audit Office (NAO) has provided a useful summary of the skills it believes are required to oversee markets in public services (figure 7). In all of the areas we examined, there were significant skills gaps. The problem of attracting high-calibre commercial skills into the public sector is often over-stated as seen by the recent success of the Cabinet Office in bringing high-profile figures into government as Crown Representatives. However, pay and status considerations can act as barriers to recruitment of the best talent on a full-time basis, which suggests there may be benefits in finding models (for example top-level advisory or steering groups) which bring these skills to bear on major programmes on at least a part-time basis.

Generally, however, we found that skills shortages were not the result of a failure to attract skills but of insufficient recognition of these skills gaps in the first place. For instance, government tends not to value the benefit of cross-functional commissioning teams led by an experienced responsible owner (SRO) or the advisory role providers can play in major shifts in market design as highly as the evidence suggests it should. Too often, departments implementing new market models would deploy non-specialist staff in roles of considerable responsibility

Figure 7: NAO summary of core skills required for oversight of public services markets

Area of oversight	Skills required
Establishing rules, policing, enforcement and redress	Commercial and consumer law and litigation skills: including knowledge of, and capability to enforce, competition and consumer law; awareness of ways to encourage compliance; and understanding of redress mechanisms.
Demand-side effectiveness	Consumer insight and information skills: including developing information systems that facilitate user choice and enable user feedback; mapping demand for new services; understanding product/service characteristics; and behavioural insights, both for users and intermediaries.
Supply-side effectiveness	Commercial, economic and analytical skills: including an understanding of actual and potential barriers to market entry, expansion and exit, particularly those faced by smaller businesses and third sector organisations; facilitating new entry of providers; shaping and sustaining markets to deliver the services users want; and understanding how to set tariffs/prices that represent value for money.
Continuity regime and financial monitoring	Financial and business analytical skills: including designing continuity regimes to limit risks to the taxpayer; an understanding of administration and insolvency law; financial analysis of provider viability; and business review.
Evaluation of market outcomes	Evaluative and economic skills: market and economic analytical skills; and evaluation of user outcomes.

NOTE

1   This is not intended to provide an exhaustive list of the skills requirements for oversight of public services markets but to give a general indication of the types and areas of expertise and skill that are likely to be required.

Source: National Audit Office

Underlying public sector incentives

We found several examples of the inherent biases of the UK's political and administrative system impacting on decisions regarding market design and oversight. This is not the place for a full analysis of these biases and the reasons underlying them but they include:

- short-term focus
- leadership churn
- a preference for visible markers of action
- a reluctance to create 'losers' in any change process.

Given that these biases are unlikely to change significantly, we can only call for them to be recognised and for stronger mitigations to be put in place to deal with them. For example, given that changes in political leadership

are likely to be frequent due to the combination of elections and the need for prime ministers to use reshuffles as a tool for ensuring party loyalty, the Civil Service will need to pay special attention to protecting continuity of leadership in the design and implementation of market-based delivery models. And because timescales for change may be accelerated, there is a need for processes of testing that operate within political time horizons.

A more radical approach is to recognise that public officials often find themselves with conflicts of interest when stewarding public service markets. Government is already taking several positive steps to improve commissioning and oversight of public service markets. For example, the Cabinet Office has established a small, virtual Commissioning Academy to improve skills in this area. However, there is still insufficient recognition of the scale of the challenges across government.

We argue that government must urgently professionalise its approach to commissioning and overseeing public service markets, embracing what we call a 'market stewardship' approach. This approach focuses on ensuring long-term outcomes and value for money and involves policy makers:

- engaging closely with users, provider organisations and other interested parties across the system to understand needs, objectives and enablers of successful delivery
- setting the 'rules of the game' and allowing providers and users to respond to the incentives this creates
- constantly monitoring how the market is developing and how providers are responding to these rules, and the actions of other providers
- adjusting the rules of the game in an attempt to steer the system (much of which is, by design, beyond their immediate control) to achieve their high-level aims.

To support effective market stewardship, government departments and other commissioning organisations should:

1. clarify roles, responsibilities and accountability arrangements
2. be more considered, open and flexible in design
3. focus on competition, market structure and market dynamics
4. increase transparency.

Recommendation 1: Clarify roles, responsibilities and accountability arrangements

Given the confusion about what needs to be done to ensure public service markets are operating effectively, there is an urgent need to clarify the roles that must be performed, who must perform them and how the organisations and individuals involved should be held to account for performance. To achieve this, we propose the following.

1.1 **Government departments should adapt and adopt a version of our 'market stewardship framework'** (figure 3, p. 19) which identifies the key functions that need to be performed to ensure effectiveness. For example, every department should be able to identify which organisation is responsible for ensuring users are able to make informed choices and which organisation is responsible for clarifying how provider failure (in terms of performance or financial failure) will be managed.

Some organisations need to be impartial and all organisations need to be structured (and funded) in a way that ensures they can perform their role effectively. Therefore, for each market stewardship function, the responsible central or local government department must ask:

  o does this organisation need to be impartial to perform this role?
  o does this organisation have the capability to perform this role effectively – or could it develop it?

1.2 Once roles and responsibilities are clear, **all central and local government departments should produce 'accountability maps'** which detail both the organisations and individuals responsible for each aspect of market stewardship.[53] Select Committees should demand that departments produce these 'accountability maps'. This will allow them to focus much more on understanding overall system performance and the capacity of the department to ensure high-quality, cost-effective services, rather than on the failing of individual providers which may grab the headlines, but can have less bearing on performance.

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[53] This builds on a recommendation of Moyes, W., Wood, J., and Clemence, M., *Nothing to do with Me: Modernising ministerial accountability for decentralised public services,* 2011, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/nothing-do-me

1.3 Our research, like other Institute work, repeatedly showed the importance of clear and continuous leadership at ministerial and official level. We support the Cabinet Office's drive to ensure senior responsible owners (SROs) are in place for all major projects. To ensure continuity of leadership and accountability, **we recommend that each public service market worth over £5-10 million p.a. is overseen by a designated senior responsible owner**. SROs should be – among other things – responsible for maintaining up-to-date accountability maps. **SROs must remain in post for at least three to five years**. Given current career **incentives it is likely to be necessary to provide financial incentives or other rewards to achieve this**. We have previously recommended that government departments conduct regular skills audits to understand gaps in commissioning and market stewardship capabilities and reiterate that this is an essential step.

1.4 There is an urgent need for **greater cross-civil service leadership of this agenda and far greater clarity on the roles of the Cabinet Office and Her Majesty's Treasury (HMT).** The efforts of the Cabinet Office Efficiency and Reform Group (ERG) have usefully aimed to improve central support and oversight but our research suggests that central processes (with the possible exception of the Major Projects Authority and HMT review processes) are largely tangential to the way in which departments design and oversee public service markets. We reiterate the findings of previous Institute research, arguing that urgent efforts are needed to strengthen functional and corporate leadership to address:

- poor identification and management of cross-government risk (see recommendation 3.3)
- inadequate cross-departmental and comparative management information[54]
- duplication of activities across departments
- inability to redeploy appropriately-skilled individuals to the areas of greatest need[55]
- the absence of a systematic way of thinking or talking about commissioning and public service markets.

Recommendation 2: Be more considered, open and flexible in design

Our research confirmed the findings of our previous research on government policymaking, which emphasises the need for greater involvement of those who deliver services in the policy design; the need to continually learn about what is working and adapt; and the need for external challenge and scrutiny.

2.1 **Policymakers and commissioners must systematically evaluate and manage the risks of contracting out public services.** Our 'service characteristics' framework (figure 1, p. 17) provides a way to identify which services are harder to contract out, why problems might arise and how to manage (and reduce) them. For example, if it is difficult to measure the value added by providers, there is a risk that government will not be able to reward providers appropriately for their contributions. This risk can sometimes be managed – by, for example, measuring and rewarding user views (or choices); rewarding relative performance compared to other providers; and paying for interim outputs known to contribute to the desired outcomes. We provide examples of risks and mitigations in our *When to Contract* report. [56] Where there is doubt over contracting-out decisions, we suggest that government pilots changes and retains some provision in-house to retain an understanding of costs, delivery models and performance.

2.2 **Central and local commissioners should test any major changes to provider incentive systems**, working with providers in the sector or those who have a good understanding of the provider perspective. We suggest **high-powered, commercially-minded challenge boards,** and **scenario and simulation**

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[54] McCrae, J., Stephen, J., Guermellou, T., Mehta., R., *Improving Decision Making in Whitehall: Effective use of management information*, 2012, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/improving-decision-making-whitehall

[55] See, for example, Magee, I., Gash, T., Stephen, J., *System Upgrade? The first year of the Government's ICT strategy*, 2012, retrieved 16 July 2015, http://www.instituteforgovernment.org.uk/publications/system-upgrade

[56] Gash, T., and Panchamia, N., *When to Contract: Which Service Features Affect the Ease of Government Contracting?* Institute for Government website, January 2013, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/when-contract

exercises as effective methods.[57] These processes should also include user representatives and professional groups wherever possible.

2.3 **Central and local commissioners should find ways of increasing flexibility**, for example by using **performance-related break-clauses,** such as those available (but not yet invoked) in the Work Programme; establishing **clear change processes**; and creating **rolling contracting cycles.** Where possible, government should **tie levels of payment to outcomes and volumes of work actually undertaken**. These types of changes ensure that when requirements change, services can change too, without exorbitant costs.

2.4 **Policymakers should ensure they evaluate the effectiveness of services delivered by independent providers to inform future design choices.** For example, they should **use randomised control trials** to assess how effectively providers help their users compared to a small sample of individuals receiving no service. This may not always be politically attractive but it is essential for understanding the value add of independent providers and improving performance over the longer term. It also paves the way for ensuring that payments are more closely tied to providers' actual success in improving outcomes.

Recommendation 3: Focus on competition, market structure and market dynamics

Our research emphasises that commissioners and policymakers often pay too little attention to the long-term development of competitive markets of service provision. There is therefore a need to redouble efforts to ensure a sufficient range of capable suppliers and to maintain competitive tensions. Otherwise, the exit of one or two providers can leave government with a limited choice of suppliers and low bargaining power – as has recently happened in the recent electronic monitoring re-tendering process.

3.2 **Government departments should conduct or commission regular market studies** (akin to the one currently commissioned by the Department for Education for childcare and early-years services)[58] to measure:

- o users' willingness and ability to exercise choice and the factors affecting this
- o barriers to market entry and expansion
- o perverse effects of competitive incentives
- o barriers to, and risk of, provider contraction and exit.

Such studies should pay special attention to ensuring that there are clear pathways to growth for small and medium sized providers. If desired, departments could usefully invite the Office of Fair Trading or other outside experts to advise on market design, as Her Majesty's Revenue and Customs did when considering a new system of childcare vouchers. The Major Project's Authority should require all major projects involving public service markets to demonstrate that a market study has been carried out prior to project approval.

3.3 The Prime Minister, Chancellor or Minister of the Cabinet Office should consider ways of creating external, public scrutiny, particularly when:

- o outsourcing areas of work worth over £100 million per annum
- o making significant changes to commissioning models worth over £100 million per annum

There is a range of ways to achieve this. Ministers could, for example:

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[57] Further options are found in Section 1 of this report and in Blatchford, K., and Gash, T., *Testing New Commissioning Models: A Guide to Help Policy Makers Learn about Publicly-funded Markets*, Institute for Government, London, 2012, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/testing-new-commissioning-models

[58] La Valle, *Childcare and Early Years Provider Survey 2011,* 2012, Department for Education Research Report RR240

- create a statutory obligation to publish 'competition impact assessments' (ideally performed by an independent organisation such as the Office of Fair Trading (OfT) or Competition and Markets Authority (CMA)) prior to implementing reforms
- give the National Audit Office (NAO) 'super-complaint' powers, allowing the NAO to oblige the OfT to investigate competition or consumer issues found during the course of value for money studies.

3.3 The Cabinet Office or the Treasury should initiate an immediate cross-sector review of levels of competition in each region of England and Wales. This review would seek to define the maximum market share that any provider should have in a specific sector and/or region and would highlight any areas where competitive pressures are too low. This should spur government to enable new providers to enter the market and grow or, where needed, may trigger investigation by competition authorities.

3.4. There is an urgent need to re-examine the role of independent competition regulation in public service markets. Private and voluntary sector providers often argue that incumbent public sector providers are not exposed to competition or are given preferential treatment in biding processes for political reasons. Meanwhile, there is clear evidence of anti-competitive practice emerging in private markets adjacent to the public sector. For example, the OfT has recently referred the private healthcare market to the Competition Commission after observing practices that appear to be undermining outcomes for users.

There are currently a range of models for spotting potential anti-competitive practice in public service markets – with areas such as health having an independent economic regulator (Monitor) but others subject to limited economic regulation. It remains unclear, for example, whether and how areas such as secondary education or probation services are (or should be) subject to competition regulation. The OfT have developed valuable tools for assessing private markets but there is a strong consensus that not all of these tools can be applied to public service markets without significant adaptation.

Recommendation 4: Increase transparency

The Government has taken a number of positive steps to improve the transparency of public service markets, including by publishing information on upcoming government contracts on .Gov.UK, the government's new internet portal. Such steps must be urgently augmented.

4.1 Government contracts should oblige all public, voluntary and private sector providers of public services to publish details of:

o the funding they receive from government
o their performance against contractual obligations
o the suppliers to whom they subcontract services, the value of these contracts and, where practical, their performance
o user satisfaction levels (where available).

This transparency could also be achieved simply by clarifying (and if necessary adjusting) the rules on 'commercial confidentiality' to confirm which data that government holds in relation to contractor fees and performance can be subject to freedom of information requests. A more incremental approach would be to ensure that contractual arrangements made it clear that no supplier could prevent a sub-contractor from publishing similar information.

It is unlikely that there will be any quick fixes that transform the outcomes produced by public service markets overnight. Testing and, unless difficulties are found, adopting these recommendations will, however, lead to significant improvements and will be an important step on the journey to professionalising government's approach to design and oversight of the market-based delivery models that are fast become the norm in UK public services.

Section 2: Case Studies

The Work Programme

Summary

In June 2011 the Coalition Government launched the Work Programme, its flagship initiative for helping the long-term unemployed into work. Although it was billed as a 'revolution in back-to-work support', it actually built on over two decades of experience in commissioning employment services. Even after 20 years of practice however, there remained room for improvement – with one of the main criticisms being that providers sometimes focused excessively on placing easy-to-help jobseekers into short, fragmented spells of employment that often saw them return to benefits relatively quickly. The Work Programme attempted to change this by:

- paying providers largely 'by results'
- specifying higher payment rates for harder-to-help groups
- adopting a 'black box' approach to contracting
- shifting market share to higher-performing providers.

It was hoped that these design features would incentivise providers to help all participants into work and keep them there for longer.

The Work Programme has now been running for two years. In some respects, it has been highly successful. The Programme hit ambitious implementation timescales of less than 12 months and significantly reduced government expenditure on outsourced employment services.

However, early outcomes remain disappointing in many ways. In November 2012, it was revealed that all 18 prime providers failed to meet the minimum performance target of getting 5.5% of claimants into sustainable employment. Although the latest figures (June 2013) show that performance has improved in the two main Jobseeker's Allowance claimant groups, it nonetheless remains far below expectations for Employment Support Allowance (ESA) claimants suggesting that some providers are 'parking' harder-to-place claimants.[59] There is also anecdotal evidence to suggest that some providers have found it difficult to establish effective operations and co-ordinate with JobCentre Plus (JCP) around referrals and information.

Although it is too early to tell whether these are transition problems or manifestations of wider, systemic weaknesses, the majority of those we interviewed for our research felt that there remains significant room for improvement in future outsourcing programmes. Most saw scope, for example, to improve the contract design. The payment mechanism and reliance on inaccurate forecasts were all criticised for discouraging investment in high-quality provision. Financing and regulatory arrangements were seen by some as creating barriers to market participation and risks of provider exit, even where there is no underperformance. The Department for Work and Pensions' (DWP) ongoing performance management of providers was sometimes seen as indecisive due to the reluctance to punish providers for underperformance. There was also strong criticism of the decision to relocate several providers to new geographical locations because these increased the risk of a performance dip as providers established new offices, relationships with JCP and supply chains.

We trace the successes and weaknesses of the Work Programme back to the experience and incentives of the organisations involved in the reforms. The Work Programme was, we believe, only implemented in the timescales it was set because of DWP's previous contracting experience and the maturity of the employment services provider market. Ministerial drive and official-level experience was crucial though in enabling the department to overcome various obstacles, including scepticism from the Treasury and caution in the investor community.

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[59] In year two of the programme, average performance was at 31.9% against a minimum performance level of 33% for JSA 18-24 claimants; 27.3% against a minimum performance level of 27.5% for JSA claimants aged 25 and over; and 5.3% against a minimum performance level of 16.5% for new ESA claimants.

However, Work Programme leadership was highly personalised at both the ministerial and official level, which increased the risk that the departure of certain individuals would disrupt the programme – as it eventually did. Strong political commitment to implementation also appears to have undermined both departmental and government risk management processes that could have identified and corrected difficulties early on. Meanwhile, established ways of working in the department made it difficult to develop effective relationships with providers and co-ordinate the Work Programme with related government services.

If future reforms are to mitigate these inherent biases in government's approach to contracting public services and address the weaknesses of the Work Programme, DWP – and others involved – will need to urgently focus on:

- increasing data and transparency to better understand the 'health' of the market
- stress-testing changes to incentive systems to develop commercially sound proposals
- building flexibility into contracting models to enable ongoing learning and adaptation.

History

Employment services have been contracted out for over two decades. In the late 1980s and early 1990s, national and local government increasingly began to commission voluntary and (to a lesser extent) private sector organisations to provide tailored employment services for jobseekers.[60] When Labour came to power in 1997, it accelerated this trend with the establishment of the various New Deals, Employment Zones and Pathways to Work. During this time, contract designs, payment schedules and monitoring regimes evolved and there was a gradual shift towards payment-by-results (PbR) contracts. There was also a shift to the 'prime provider' model in which the government would contract a few, large national providers to deliver employment services in a particular area. These providers would in turn sub-contract smaller voluntary and private sector organisations to supply specialist services for particular client groups. Therefore, by the time the Coalition came to power in 2010, there was cross-party consensus over the use of contractual mechanisms in the delivery of employment services, a steady evolution in contracting methods and a mature, diverse supplier base.[61]

However, challenges remained and these centred on the fact that contracted providers:

- were paid a high upfront service fee, regardless of actual job outcomes achieved
- had insufficient incentives to focus on harder-to-place claimants
- were given little scope to design services around individual needs
- were allowed to remain in the market, regardless of the results they delivered.[62]

The Work Programme attempted to address these weaknesses. Announced as part of the Coalition's Programme for Government in 2010, the policy was developed in opposition by the Conservatives under the guidance of Lord (David) Freud. Although it was billed as a 'revolution in back-to-work support', the Work Programme actually embodied a high degree of continuity with existing Labour policy and programmes (see Figure 10 for a timeline of key events).[63] In particular, it embedded the novel design features that were developed for the abortive Flexible New Deal phase two programme (FND2) during 2009. These include:

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[60] For example, during the early 1980s recession the Community Programme was a large-scale government initiative which provided temporary jobs for the long-term unemployed. A decade later, in 1992, a network of Training and Enterprise Councils were introduced, which were private companies that managed devolved funds for work-based training programmes and experimented with an 'output related funding' model.

[61] For an overview of the history and impact of contracting in employment services see Gash, T., and Roos, T., *Choice and Competition in Public Services: Learning from History*, pp.14-18, Institute for Government website, 2012, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/choice-and-competition-public-services

[62] For further details see Department for Work and Pensions, *The Work Programme*, DWP, Government website, 2011, retrieved 5 June 2013, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/49884/the-work-programme.pdf

[63] For a case study on the policymaking of the Work Programme in opposition see Haddon, C., *Making Policy in Opposition: the Work Programme, 2007-2010*, Institute for Government website, December 2012, retrieved 7 June 2013, http://www.instituteforgovernment.org.uk/publications/making-policy-opposition-work-programme-2007-2010. For an analysis of the previous Flexible New Deal scheme see Mulheirn, I., and Menne, V., *The Flexible New Deal: Making it Work*, Social Market Foundation website, September 2008, retrieved 8 June 2013, http://www.smf.co.uk/research/welfare-reform/flexible-new-deal-making-it-work/

- increasing the amount of 'payment by results' in the contract by shifting the balance from upfront attachment to outcome and sustainment fees – triggered only after a provider has secured a claimant a cumulative period of employment lasting six months or more
- specifying differentiated payment rates for different benefit claimant groups so that providers receive higher payments for helping those who are furthest away from the labour market into employment
- adopting a 'black box' approach to service provision to give providers greater freedom to decide on the types of interventions they deem most effective and appropriate for different groups
- shifting 'market share' from poorer-performing providers to higher-performing providers in each Contract Package Area (CPA).

The Department for Work and Pensions (DWP) expects these key design innovations to incentivise providers to:

- help participants stay in work longer
- focus on the 'hardest to help'
- join up a wide range of specialist services around individual needs
- continually improve performance (see Figure 9 for details).[64]

The Programme is estimated to cost between £3 and £5bn over five years. It will be funded both from the fixed Departmental Expenditure Limit (DEL)[65] and the Annually Managed Expenditure (AME) from which benefit payments are made.[66] This financing mechanism is known as the DEL-AME switch which allows DWP to draw on additional funding from the Treasury as claimants move into work and stop claiming unemployment benefits.[67]

The then Minister for Employment, Chris Grayling, demanded that the Work Programme was launched within a year of taking office, in June 2011. Given that previous programmes had taken around four years to introduce, this represented a significant acceleration in pace.

The key dates for the procurement process were as follows:

- 1 December 2010: invitation to tender (ITT) issued
- 14 February 2011: bid submission deadline
- 1 April 2011: contracts awarded
- 1 June 2011: launch of the Work Programme.

Inherent difficulties

It has always been challenging to contract employment services due to features 'inherent' in the service.[68] These are not necessarily insurmountable barriers to effective outsourced provision, but do raise some significant risks and create trade-offs that need to be carefully managed.

1) It is **hard to measure the value added by providers** primarily because it is difficult to establish whether a job outcome was the result of an individual provider's effort, the motivation of the individual claimant, the wider economy or the performance of related services. This increases the risk of paying a provider too much and, potentially, for a job outcome generated by the actions of other services[69] or, alternatively, too little due to the poor quality of related services or a stagnating local economy. For example, efforts to return a disabled jobseeker into sustainable employment may be undermined by the combination of low-quality health provision and unfavourable local economic conditions. Pricing outcomes is therefore very challenging.

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[64] Department for Work and Pensions (2013), *Work Programme Evaluation: Procurement, Supply Chains and Implementation of the Commissioning Model,* p. 9, DWP website, 2012, retrieved 5 June 2013, http://research.dwp.gov.uk/asd/asd5/report_abstracts/rr_abstracts/rra_832.asp

[65] This is a three-year departmental spending limit set at Spending Review by HM Treasury.

[66] This is more volatile, demand-led expenditure and therefore not subject to multi-year limits in the same way as DEL. AME includes social security benefits, local authority self-financed expenditure, debt interest, and payments to EU institutions.

[67] NAO, *The Introduction of the Work Programme*, p, 17, NAO website, January 2012, retrieved 8 June 2013, http://www.nao.org.uk/report/the-introduction-of-the-work-programme/

[68] Gash, T., and Panchamia, N., *When to Contract: Which Service Features Affect the Ease of Government Contracting?* Institute for Government website, January 2013, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/when-contract

[69] This is known as the 'deadweight' or non-intervention level.

2) Employment services are characterised by a **degree of demand uncertainty** as changing local economic conditions could result in more or fewer jobseekers at any particular point in time.[70] This means that forecasts regarding the number of jobseekers referred to employment service programmes are at best indicative. This is exemplified by the fact that the DWP had to re-forecast referral numbers on three separate occasions during the Flexible New Deal phase one programme (FND1) which ran from October 2009 – June 2011.[71] The key risk for government is that providers may be reluctant to accommodate an unexpected, short-term increase in demand, especially if this involves commitment to large irreversible capital investments. The key risk for providers is that unexpectedly low demand translates into uncertain revenue streams impeding their ability to plan, finance and deliver high-quality services.

3) **Job outcomes are not solely controlled by employment service providers**, but depend on the performance of other services. Initially, the local JobCentre Plus (JCP) provides claimants with employment advice, but after a certain period refers them to a prime provider who in turn may refer them to one of several organisations depending on their needs (for example, a skills and training provider). Where multiple organisations contribute to achieving a particular outcome it is generally harder to ensure that their activities are effectively co-ordinated, particularly if these organisations have different ownership (i.e. public and private sector) or misaligned policy incentives. This could result in organisations competing for the same group referrals, withholding information and obstructing each other's performance making it difficult for providers to control the outcomes they deliver.

During the 2000s, the Department had made some progress towards mitigating these inherent contracting risks. First, and most importantly, DWP understood the need to estimate policy-on and policy-off performance, likely costs of provision and likely numbers of referrals to the programme. This enabled DWP to estimate the value added by employment service providers and demand. Second, DWP made the strategic decision to retain a public sector service for short-term unemployed (Jobcentre Plus) to facilitate a quicker response to fluctuations in demand. This meant that some of those who lost their jobs in the 2008 recession were placed in alternative employment relatively quickly with less need to refer them onto contracted providers.[72]

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[70] The number of people out of work for more than a year has risen from around 400,000 in 2007 to reach 855,000 in the three months ending in January 2012. For analysis see: Cooke, G., 'We need a firm limit on the time we are prepared to tolerate anyone being unemployed', *Left Foot Forward website*, 17 April 2012, retrieved 16 July 2013, http://www.leftfootforward.org/2012/04/long-term-unemployment-scandal/

[71] Interview with prime contractor organisation

[72] Gash, T., and Roos, T., *Choice and Competition in Public Services: Learning from History*, p. 16, Institute for Government website, 2012, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/choice-and-competition-public-services

Figure 8: Characteristics of employment services

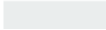| In order to assess...	...Ask	RAG Rating	Details
The appropriateness and effectiveness of user choice mechanisms	Do consumers face high switching costs?		
	Are consumers often involved in distress purchasing?		
	Is the service a merit good?		
The costs and risks of using market mechanisms, and the need for regulation to mitigate these risks	Is it difficult to measure the value added by providers?	Problematic	Although it is easy to measure job outcomes (i.e. someone is either in or out of a job), it is difficult to establish whether this was the result of a provider's effort, the motivation of the individual claimant or the performance of related services.
	Are service outcomes highly dependent on the performance of other services?	Problematic	Job outcomes can generally be delivered by a provider, but to some extent depend on the cooperation of JobCentre Plus and related services such as skills and health.
	Does delivering the service require investment in highly specific assets?	Unproblematic	Although providers need to establish offices and recruit staff when they first establish an operation, the physical and human assets are not highly specific to the service.
	Is the service characterised by high demand uncertainty?	Highly Problematic	Demand is likely to fluctuate as changing local economic conditions could result in more or less jobseekers at any particular point in time.
	Is the service characterised by high policy uncertainty?	Unproblematic	There has been cross-party consensus on the use of market mechanisms in the delivery of employment services for the last two decades and there is a low risk of major changes to the service specification.
	Is the service essential for government's ultimate decision-making or coercive authority?	Unproblematic	No.
The ease and cost of transition from a fully government owned and delivered service to one based on market mechanisms	Is there an existing supply of (high quality) providers?	Unproblematic	Employment services have been contracted out to varying degrees for nearly two decades, which has led to the development of a mature supplier base and industry-wide bodies.
	Is there an existing workforce (either in the public or private sectors) with adequate skills and capabilities to deliver high-quality services?	Unproblematic	As above.
	Does the government have the organisational capability to design and monitor the use of market mechanisms?	Problematic	DWP has developed experience in commissioning large-scale employment programmes and has experimented with various contracting methods, but it does not yet have a fully established capability in evaluating programmes.
	Does the government have enough information about cost and quality to measure provider performance?	Problematic	DWP can rely on historic data to inform pricing levels and performance metrics, but this is not available for all claimant groups.

RAG Rating Key

Highly Problematic	
Problematic	
Unproblematic	
N/A	

Figure 9: Design of the Work Programme

The Work Programme

Length of contracts
Five years

Prime Provider Model
There are eighteen contract package areas (CPA) and within these two or three prime providers. The prime contracting model involves a "top-tier" contractor employing their own subcontractors in a "supply chain" to deliver employment services. These prime providers may subcontract all service delivery to other organisations or combine elements of their own service delivery with subcontracted provision. They are subject to departmental oversight but are responsible for managing and monitoring the performance and quality of their subcontractors as well as their own performance.

Referrals to the programme
Jobseeker's Allowance (JSA) claimants over the age of 25 are referred after 12 months. Younger JSA claimants and those facing significant disadvantage can be referred earlier and Employment and Support Allowance (ESA) claimants can be referred at any time.

Payment Schedule
The attachment fee is an upfront payment to assist prime providers with the initial costs of setting up their provision and providing initial support to clients. This fee will be phased out over the first three years of the five year contracts. The job outcome fee is paid once a provider has secured a cumulative period of employment for the client (six months for most claimant groups). The sustainment fee is paid every four weeks after this for keeping a client in employment. An incentive payment is paid for every job outcome that exceeds the non-intervention plus 30% target from year four.

Differentiated Payment Rates
The job outcome fee ranges from £3,800 for the least challenging group to as much as £13,700 for the most challenging group.

Black Box
A term for minimum service prescription, which gives providers flexibility to decide which interventions to offer to best help participants into sustainable employment. It is hoped that this approach will encourage providers to form partnerships with other organisations such as local authorities, health service providers and colleges to design services around individual needs.

Contract Evaluation Process
The Department assessed the bids both in terms of quality and price. The quality element included supply chain management, service delivery, resources, stakeholder engagement and implementation. This formed the basis for the minimum service standard against which prime contractors would be measured during live running. The price element focused on the amount of discount offered by bidders on the maximum price for the job outcome fee. One point was available for every percentage point discount offered up to 20%, and thereafter one point for every two percentage points of discount offered.

Market Share Shifting
Each year, from the end of the second year, 'market share' of each participant group will be shifted by five percentage points from low performing to high performing providers in each CPA. The benchmark for a shift of market share will be a 3% or greater difference in performance between prime contractors within the specific customer groups in each contract package areas.

Contract Monitoring Arrangements
DWP has established various arrangements to monitor and manage contracts. First, Account Managers engage with providers at the senior board level to drive performance and value for money. Second, Performance Managers engage with providers at the operational delivery level to hold regular performance reviews, provide advice and collate management information. Third, Compliance Monitoring Officers (CMOs) undertake compliance visits to ensure that providers meet minimum standards of service both in terms of delivery and across their supply chain. Fourth, Third Party Provision Managers are responsible for ensuring that local contracted and non-contracted provision meets the needs of all customers. Fifth, Provider Assurance Teams test the effectiveness of providers' internal control system and collect information on governance, financial procedures (and counter fraud), arrangements with subcontractors and data security.

Merlin Standard
The DWP Merlin Standard is a set of principles outlining how relationships between members of the supply chain should function in the provision of welfare to work services.

Figure 10: Timeline of key events[73]

December 2006	John Hutton, Secretary of State for Work and Pensions, commissions David Freud to undertake a review of welfare-to-work programmes
March 2007	Freud produces *Reducing Dependency, Increasing Opportunity: Options for the Future of Welfare to Work* as an independent report for DWP. Recommends a large-scale increase in payment by results
28 June 2007	Government reshuffle: Peter Hain becomes Secretary of State for Work and Pensions
2 July 2007	Shadow Cabinet reshuffle: Chris Grayling becomes Shadow Secretary of State for Work and Pensions
31 July 2007	Peter Hain announces Labour will not take up all of the Freud proposals on expanding the contractual system for welfare-to-work providers
8 January 2008	Grayling and Cameron announce Conservative welfare policy including: increased conditionality; more rigorous assessments; expanded 'payment by results' for the private and voluntary sector
24 January 2008	Government reshuffle: James Purnell becomes Secretary of State for Work and Pensions
February 2008	Freud is rehired by James Purnell as an adviser on welfare policy
February 2008	DWP Commissioning Strategy is published outlining its commitment to a prime provider model, longer and larger contracts and greater use of 'payment by results'
March 2008	Flexible New Deal phase 1 PQQ released to replace previous New Deals and Employment Zone provision for Jobseekers Allowance (JSA) claimants in half the country – based on an eventual payment split of 20% service fee, 50% short job outcome and 30% sustained job outcome
July 2008	Government welfare green paper leaked – adoption of thrust of Freud's recommendations for increasing the role of private sector, but on limited basis
19 January 2009	Shadow Cabinet reshuffle: Grayling becomes Shadow Home Secretary; Theresa May becomes Shadow Work and Pensions Secretary
February 2009	Freud joins the Conservative Party as shadow spokesman
June 2009	Flexible New Deal phase 2 PQQ released (covering the other half of the country)
September 2009	Conservative Party publication *Get Britain Working*, incorporates Freud's proposals
October 2009	Launch of the Flexible New Deal phase 1. Service payments increased to 40% of contract value, due to weaker economy.
November 2009	Pilot 'Personalised Employment Programme' PQQ released – intended to combine support for Jobseekers Allowance and Employment Support Allowance claimants in a single, flexible programme – using an 'accelerator' model to increase outcome payments as providers are more successful
May 2010	Coalition Government comes to power. Iain Duncan Smith appointed Secretary of State for Work and Pensions; Chris Grayling appointed Minister for Employment and David Freud appointed Minister for Welfare Reform
June 2010	Personalised Employment Programme and Flexible New Deal phase 2 competitions are cancelled
June 2010	Competition for Employment Related Support Services (ERSS)

[73] Haddon, C., *Making Policy in Opposition: the Work Programme, 2007-2010*, p. 40, Institute for Government website, December 2012, retrieved 7 June 2013, http://www.instituteforgovernment.org.uk/publications/making-policy-opposition-work-programme-2007-2010

	framework opens
27 September 2010	Closing date for ERSS framework competition
October 2010	Grayling announces cancellation of the Flexible New Deal phase 1 contracts
19 November 2010	First version of Full Business Case completed
30 November 2010	Successful ERSS framework bidders notified
1 December 2010	Invitation to Tender for the Work Programme issued
3 December 2010	Payment structure, performance expectation and sanctions for failing are finalised
14 February 2011	Tenders from bidders for the Work Programme due
31 March 2011	Transition: Pathways Phase 1 contracts cease Transition: Referrals to Flexible New Deal provision end
April 2011	Upgrade of IT system starts
1 April 2011	Prime Contracts for Work Programme awarded
11 April 2011	DWP approves the business case for the Work Programme
27 April 2011	Phase 2 of Pathways to Work contracts cease
1 June 2011	Contract signing completed and the Work Programme goes live. Transfer of Flexible New Deal participants to Work Programme begins
March 2012	Upgraded IT system in place
November 2012	First performance figures released

Market strengths and weaknesses

The Work Programme has now been in operation for two years and been successful in:

- **reducing the costs of outsourced employment service provision.** DWP estimated that the Work Programme would cost £3bn to £5bn over five years, which would make it far more economical than previous welfare-to-work programmes. The Social Market Foundation (SMF) has calculated that, if minimum performance levels are achieved, Work Programme providers receive around £1,200 for each referral compared to £1,600 under the Flexible New Deal phase one programme (FND1).[74] The funding level drops to a maximum of around £900 per referral from year four onwards. Therefore, in terms of simply reducing the amount of government expenditure on contracted employment service provision, the Work Programme has been a success.

- **meeting fast-paced implementation timescales.** DWP fast-tracked the procurement of the Work Programme by establishing a two-stage procurement process in which providers would first bid to join DWP's Employment Related Support Services framework (ERSS) and then compete to deliver the Work Programme within three months of the tender. The launch of a large-scale programme within only 12 months clearly represents a significant administrative feat.

- **facilitating a degree of cross-departmental collaboration with the Ministry of Justice (MoJ).** In March 2012, the Work Programme was extended to a new claimant group – former offenders. On day one of release, prisoners are immediately referred to a Work Programme provider who is responsible for providing specialist support to get them into work as quickly as possible and thereby reduce the likelihood of re-offending.

However, it is difficult to evaluate whether the programme is actually cost-effective. The first full set of performance figures released in November 2012 were unclear about whether performance was better or worse than 'doing

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[74] Mulheirn, I., *Will the Work Programme Work? Examining the Future Viability of the Programme*, p. 6, Social Market Foundation website, August 2011, retrieved 8 June 2013, http://www.smf.co.uk/assets/files/publications/WP%20analysis.pdf

nothing' or that of previous programmes – particularly due to inconclusive debates around the accuracy of the deadweight calculation, the time period the results related to, and the performance measures used.[75]

It is clear, however, that early outcomes do not yet meet expectations. When it commissioned the Work Programme, DWP expected providers to meet, or even exceed, the key performance target of achieving employment for six months or more for 5.5% of the claimants referred to them. This would mean helping 70,000 jobseekers into sustained employment during the first 14 months of operation (June 2011 to July 2012).[76] Actual performance fell well below this. **In November 2012, it was revealed that all 18 prime providers failed to hit the target, average performance was at 3.6% and only 31,000 job outcomes were achieved.** Although performance has clearly improved in the second year of operation, with providers coming close to achieving minimum performance targets for the two main groups of Jobseeker's Allowance claimants, all have missed the target for Employment Support Allowance claimants.[77]

In addition to delivering a disappointing number of job outcomes, there is anecdotal evidence to suggest that the Work Programme suffers similar problems to previous programmes including:

1) **'Creaming' and 'parking'.** Despite the differential payment regime, we frequently heard that easy-to-help claimants have more regular and intensive contact with advisers, while those with multiple barriers who could be helped cost-effectively into work are often parked with little or no likelihood of referral to specialist support.[78] Generally, providers seem keen to cut costs, where possible, for example by making greater use of 'group sessions' and telephone rather than face-to-face contact.[79]

2) **Lack, or narrow forms, of innovation.** Although the intention of the 'black box' approach was to encourage providers to innovate by, for example, joining up a wide range of specialist services around individual needs, the programme remains a relatively narrow job-focused programme. On one hand, providers seem reluctant to invest in costly, specialist support services that could address individual barriers to work (e.g. skills, counselling and drug addiction treatment). On the other, providers are willing, but unable to access relevant funding pots (e.g. the skills budget) or co-ordinate with parallel employment support initiatives at the local level. This limits their ability to offer a holistic package of services to individuals.[80]

3) **Barriers to entry and expansion**. Although the Work Programme was expected to provide a 'massive boost to the Big Society',[81] it has proven difficult for some voluntary and community sector (VCS) organisations to enter the programme. Some of those who could enter as specialist sub-contractors have come under severe financial strain.[82] As a result, some high-capability VCS organisations are voluntarily choosing to leave the market (such as St Mungo's, a homelessness charity).[83] If this trend continues, there is a risk that the Work Programme could lose the diverse and responsive supply chains that the hardest-to-help jobseekers with multiple barriers to work rely on.

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[75] House of Commons Committee of Public Accounts. (2013). *Department for Work and Pensions: Work Programme Outcome Statistics. Thirty-third Report of Session 2012-2013.* House of Commons, p.10

[76] Centre for Economic and Social Inclusion, *Work Programme Performance Statistics: Inclusion Analysis,* 27 November 2012, retrieved 5 June 2013, http://stats.cesi.org.uk/website_documents/initial_WP_Performance_InclusionComment.pdf

[77] For official analysis see https://www.gov.uk/government/organisations/department-for-work-pensions/series/work-programme-statistics--2

[78] Department for Work and Pensions, *Work Programme Evaluation: Findings from the First Phase of Qualitative Research on Programme Delivery,* pp.107-112, DWP website, 2012, retrieved 5 June 2013, http://research.dwp.gov.uk/asd/asd5/report_abstracts/rr_abstracts/rra_821.asp; House of Commons Committee of Public Accounts 2013, *Department for Work and Pensions: Work Programme Outcome Statistics, Thirty-Third Report of Session 2012-2013,* House of Commons, London, 2013. House of Commons, oral evidence.

[79] Interview with expert advisers.

[80] Interview with civil servant and sub-contractor organisations. Also see Department for Work and Pensions, *Work Programme Evaluation: Findings from the First Phase of Qualitative Research on Programme Delivery,* pp.107-112, DWP website, 2012, retrieved 5 June 2013, p. 117 http://research.dwp.gov.uk/asd/asd5/report_abstracts/rr_abstracts/rra_821.asp

[81] Department for Work and Pensions, 'Massive boost for the Big Society as almost 300 voluntary sector organisations named as part of the Work Programme." DWP Press Release, 2011, retrieved 10 July 2013, https://www.gov.uk/government/news/massive-boost-for-the-big-society-as-almost-300-voluntary-sector-organisations-named-as-part-of-the-work-programme

[82] Damm, C., (2012), *The Third Sector Delivering Employment Services: an Evidence Review*, p. 19, Third Sector Research Centre, January 2012, retrieved 5 June 2013, http://www.tsrc.ac.uk/LinkClick.aspx?fileticket=aoUqP0rW6m8%3D&tabid=873

[83] Interview with a prime contractor organisation, sub-contractor organisation and provider representative body. Also see Ainsworth, D., 'St Mungo's leaves Work Programme after failing to receive any referrals', *Third Sector Online*, 2012, retrieved 16 July 2013, http://www.thirdsector.co.uk/news/1131555/

There have also been early problems in implementation with some providers experiencing:

4) **Unnecessarily high transition costs,** particularly when moving into areas where they didn't have an existing geographical footprint. Providers we spoke to mentioned difficulties around securing staff and premises in areas where they had not delivered before, negotiating supply chain agreements and managing the TUPE process in the short time available (April-June 2011).[84] At the same time, the IT system designed to support the Programme only became available 10 months after the launch, in March 2012.[85] This meant that DWP was unable to generate automated management information on job and sustainment outcomes, which increased the risk of fraud and error and potentially made it harder to robustly monitor provider performance during the first year of operation.[86]

5) **Poor co-ordination with JobCentre Plus (JCP).** There is reluctance among some JCP district managers and front-line staff to co-operate with contracted providers over referrals and information.[87] For example, one provider told us that the district JCP in one of its CPAs routinely blocked referrals which meant that it received 20% fewer referrals than expected in that area.[88] This is not to say that poor or inadequate communication was the norm: there were also examples of well-functioning relationships, some of which stemmed from co-location[89] or secondment of staff,[90] but these were not universal.

Whether these early problems represent a short-term performance dip or wider systemic weaknesses is debatable. Some argue that the latest statistical release demonstrates that performance will continue improving as the programme matures.[91] Others argue that performance against minimum targets is only likely to worsen as providers have promised to deliver even more for less from year three onwards. On average, selected providers offered performance levels of 38% higher than DWP's baseline targets and discounts of around 6% on DWP's payment offer for a job outcome. The attachment fee will also be phased out completely by year four. This may increase the risk of widespread creaming and parking and even the voluntary exit of high capability providers.[92] In addition, plans to introduce Universal Credit[93] could lead to major changes to the definitions of claimant groups and associated payments, which may be costly and potentially disruptive for performance.[94]

It is difficult, however, to make definitive judgements about the future viability of the programme, given that the extent of these problems is unknown. What is clear is that there have been significant transitional difficulties during the first two years of operation.

Explaining the strengths and weaknesses

Design and implementation choices

The majority of our interviewees emphasised that there were a number of market-design and implementation decisions that contributed to the initial performance dip observed.

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[84] Interview with a provider representative body; Department for Work and Pensions (2013), *Work Programme Evaluation: Procurement, Supply Chains and Implementation of the Commissioning Model,* p. 15, DWP website, 2012, retrieved 5 June 2013, http://research.dwp.gov.uk/asd/asd5/report_abstracts/rr_abstracts/rra_832.asp

[85] Department for Work and Pensions, *The Introduction of the Work Programme – Public Accounts Committee*, 15 May 2012, retrieved 5 June 2013, http://www.publications.parliament.uk/pa/cm201012/cmselect/cmpubacc/1814/181404.htm

[86] NAO, *The Introduction of the Work Programme*, p. 8, NAO website, January 2012, retrieved 8 June 2013, http://www.nao.org.uk/report/the-introduction-of-the-work-programme/

[87] Department for Work and Pensions, *Work Programme Evaluation: Findings from the First Phase of Qualitative Research on Programme Delivery,* p. 4, DWP website, 2012, retrieved 5 June 2013, http://research.dwp.gov.uk/asd/asd5/report_abstracts/rr_abstracts/rra_821.asp

[88] Interview with prime contractor organisation

[89] Interview with prime contractor organisation

[90] Interview with prime contractor organisation

[91] For the official analysis of the June 2013 performance figures see Department for Work and Pensions, Work Programme statistical summary June 2013, Gov.UK website, retrieved 16 July 2013, https://www.gov.uk/government/publications/work-programme-statistical-summary-june-2013

[92] NAO, *The Introduction of the Work Programme*, p. 11, NAO website, January 2012, retrieved 8 June 2013, http://www.nao.org.uk/report/the-introduction-of-the-work-programme/

[93] Universal Credit will bring together all working-age benefits and tax credits into one payment range.

[94] Department for Work and Pensions, *The Introduction of the Work Programme – Public Accounts Committee*, 15 May 2012, retrieved 5 June 2013, http://www.publications.parliament.uk/pa/cm201012/cmselect/cmpubacc/1814/181404.htm

- **Pricing levels** stretch the financial viability of the contracts.
- Excessive reliance on accurate **referral forecasts** leaves little margin for error.
- **Financing and regulatory arrangements** raise barriers to market participation.
- An inconsistent **contract management regime** does little to improve performance.
- Strict adherence to **competition principles** leads to high transition costs.

Each of these were the product of some difficult choices and trade-offs. We provide a short summary below.

Pricing levels stretch the financial viability of the contracts

> If providers cannot make money by doing the thing you expect them to do, then they will make money by doing the things that you don't want them to do.
>
> Expert adviser

> These contracts are on the edge of being financially viable. You have to aggressively cream and park.
>
> Director at a prime contractor organisation

The prices set out in the Work Programme contracts have been criticised by the House of Commons Work and Pension Committee for presenting 'a significant financial and operational challenge for prime contractors'.[95] The Centre for Economic and Social Inclusion (Inclusion) concludes that, depending on their costs, primes would need to exceed the performance levels just to break even.[96] Meanwhile, the SMF has calculated that, if the minimum performance levels are achieved, Work Programme providers would be operating with at least 25% less funding than their predecessors under FND1, even though there are fewer jobs around.[97]

Although one can debate these figures, our interviewees suggested that the contracts have not achieved the correct balance between risk and reward to incentivise providers to target different types of support to different groups. This is partly because providers get paid for the 'deadweight' – that is, for achieving job outcomes for those who would have got work without the help of the programme (the 'easy-to-help'). We were told that the differential payment regime is 'a blunt instrument' that has done little to incentivise providers to move beyond this and focus on the hardest-to-help.[98] Providers argue that the nine payment categories are too broad and do not reflect the number of barriers an individual faces or the length of time they have been out of work.[99] Further, the payment differences between groups are apparently not large enough to cover the real costs of provision for some groups, making investment in those with multiple needs more difficult. 'We weren't using the full range of interventions because we just couldn't afford it.'[100] There are concerns that the roll-out of Universal Credit could make matters worse.

These pricing levels were the result of three processes: development of optimistic performance expectations; heavy price reductions offered by bidders; and the selection of bids on the basis of price. The problem being that there was nothing in place to mitigate the risks that flowed from these processes along the way.

In coming to the non-intervention level (set at 5%)[101] DWP largely relied on the performance of the New Deals at the height of the boom in the 2000s and on Office for Budget Responsibility (OBR) projections for growth, which predicted that the economy would grow by 2.1% in 2011 and 2.6% in 2012. Instead, the economy has stalled and

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[95] House of Commons Work and Pensions Committee 2011, *Work Programme: Providers and Contracting Arrangements, Fourth Report of Session 2010-2012*, p. 34, House of Commons, London, 2012.

[96] Simmonds, D., *Work Programme Results: Perform or Bust?* Centre for Economic and Social Inclusion website, 2011, retrieved 8 June 2013, http://www.cesi.org.uk/sites/default/files/response_downloads/perform_or_bust.pdf

[97] Mulheirn, I., *Will the Work Programme Work? Examining the Future Viability of the Programme*, p. 6, Social Market Foundation website, August 2011, retrieved 8 June 2013, http://www.smf.co.uk/assets/files/publications/WP%20analysis.pdf

[98] Interview with provider representative body and prime contractor organisation.

[99] Interview with sub-contractor organisation and prime contractor organisations.

[100] Interview with prime contractor organisations; also see Department for Work and Pensions (2013), *Work Programme Evaluation: Procurement, Supply Chains and Implementation of the Commissioning Model,* p.4, DWP website, 2012, retrieved 5 June 2013, http://research.dwp.gov.uk/asd/asd5/report_abstracts/rr_abstracts/rra_832.asp

[101] Defined as the number of job outcomes that would be achieved without the programme's intervention.

there has been negative growth.[102] Despite this, the non-intervention level was not fully adjusted to account for changed economic conditions and, for some claimant groups, remains untested. In addition, it was uniform for all parts of the country and fixed for the duration of the contract – overlooking the likelihood of changes in the wider economy and labour market.[103] This baseline informed the ambitious performance expectations DWP set[104] and what it would pay for each outcome.

DWP could have strengthened the quality of its assumptions by sharing and testing them with potential providers before the actual procurement process. However, officials explained to us that they had to make a difficult trade-off between engaging with a large pool of providers (which was likely to be time-consuming, difficult and potentially illegal under EU procurement law) or none.[105] In the end, DWP chose the latter course of action and thus decided not to publish the data and analysis on which the minimum performance level was based. Given the political timescales it was set, there was little time or capacity for external challenge.[106]

This meant that providers had to build financial models on the basis of inaccurate assumptions. Many even offered higher performance levels for a reduced price (which will take effect from year three), but did not ask for a risk premium to offset all the uncertainties around the programme – for example the changing economy or introduction of Universal Credit.[107] Although these bids were seen as achievable at the time, providers now admit that this behaviour stretched the financial viability of the contracts further.[108]

Instead of spotting this risk during the evaluation process, we were told that the DWP procurement team ended up awarding contracts more or less on the basis of the price reductions offered. On one hand, this was due to the fact that it was very difficult to tell the bids apart in terms of quality. Indeed, some providers described this element of the process as a 'tick-box' exercise in which it was relatively easy to convey an innovative delivery model.[109] On the other hand, it reflected the department's desire to minimise spend given its reduced budget and other major commitments (namely, Universal Credit).

In summary, inaccurate assumptions, price discounting and selecting bids on the basis of price, led to the development of pricing levels that were potentially unable to cover the real costs of provision for different claimant groups.

Excessive reliance on accurate referral forecasts leaves little margin for error

> If you don't get the referrals, then that is the killer.

Director at a prime contractor organisation

> During the first few months, the workload was overwhelming and put us under a lot of pressure.

Director at a prime contractor organisation

DWP's Invitation to Tender estimated that 605,000 people would go through the Work Programme in 2011-12 and 565,000 in 2012-13.[110] Given the ambitious pricing levels, providers told us that they depended on receiving a certain flow of referrals across the different payment groups to ensure their financial viability. As a result, their financial and delivery models were tightly based on DWP forecasts and even a slight variation in the flows could cause them financial difficulties. This excessive reliance on accurate referral estimates is highly problematic given that demand forecasting is at best indicative in employment services.

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[102] Interview with expert advisers and prime contractor organisations.

[103] NAO, *The Introduction of the Work Programme*, p. 6, NAO website, January 2012, retrieved 8 June 2013, http://www.nao.org.uk/report/the-introduction-of-the-work-programme/

[104] Defined as non-intervention performance plus 10 per cent for three claimant groups.

[105] Interview with civil servant

[106] Interview with prime contractor organisation, provider representative bodies and expert advisers

[107] Interview with expert adviser

[108] Interview with prime contractor organisation

[109] Interview with sub-contractor and prime contractor organisation

[110] House of Commons Work and Pensions Committee 2011, *Work Programme: Providers and Contracting Arrangements, Fourth Report of Session 2010-2012*, p. 45, House of Commons, London, 2012.

Indeed, the number of referrals to the programme has been either well below or well above predicted flows with sharp peaks and troughs during certain periods.[111] On one hand, referrals in the first three Jobseeker's Allowance (JSA) payment groups were far higher than expected due to rising unemployment caused by the recession (approximately 15% higher than the predicted rate).[112] Providers told us that the large caseloads required greater upfront investment than anticipated, which the attachment fee could not cover alone. This allegedly limited their ability to provide high-quality, personalised services, led them to make greater use of lower-cost interventions (e.g. group sessions) and prioritise more job-ready claimants.[113] On the other, referrals in the higher payment groups, such as those in receipt of Employment and Support Allowance (ESA),[114] were far lower than expected (approximately 37% lower than the predicted rate).[115] Providers told us that lower 'higher-rate' payments often meant that they did not have the working capital to finance the needs of particular groups, for example by paying for interpreters or transport in rural areas.[116] It also meant that they could not refer as many harder-to-help claimants to sub-contractors who had been included in the supply chain because they had specific expertise working with these groups.[117]

The key problem is not necessarily DWP's inability to accurately forecast demand – this was always likely to be difficult – but, as with the minimum performance expectations, the lack of transparency around how estimates were derived. This, in combination with the ambitious pricing levels, led providers to excessively (and detrimentally) rely on estimated referral volumes across the different payment groups. In the end, the differing referral profile limited their ability to offer high levels of personalised support. Although greater JSA referrals brought increased revenue from attachment fees, it also created pressure on services. At the same time, lower than expected 'higher value' ESA referrals led to working capital problems and increased the desire to cut avoidable costs, where possible.[118]

Financing and regulatory arrangements raise barriers to market participation

> In this kind of environment, there is pretty much nowhere to turn for a sub-contractor.

> Director at a sub-contractor organisation

> Only those with 'deep pockets' will be able to survive [in the market].

> Director at a prime contractor organisation

The Work Programme's financing and regulatory arrangements have been criticised for raising barriers to market participation and creating the risk of provider exit even where there is no underperformance.

On one hand, some large providers who could have become successful prime contractors chose not to compete for the Work Programme due to early rumours that it would be based on 100% 'payment by results'.[119] On the other, a number of potentially high-capability voluntary and smaller private sector organisations were unable to compete as prime providers due to the size of the contracts, £20 million turnover requirement and the level of risk associated with the Programme.[120] Although these financing requirements raised barriers to entry, the key trade-

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[111] Rees, J., Taylor, R., Damm, C., Does Sector Matter? Understanding the Experiences of Providers in the Work Programme, p. 16, TSRC website, Feb 2013, retrieved 8 June 2013, http://www.tsrc.ac.uk/LinkClick.aspx?fileticket=oJrkSIkyQyg=

[112] Simmonds, D., (2012), *The Work Programme and the Voluntary Sector*, Centre for Economic and Social Inclusion website, 2012, retrieved 16 July 2013, http://www.cesi.org.uk/keypolicy/work-programme-and-voluntary-sector

[113] Interview with expert adviser and prime contractor organisation.; also see Department for Work and Pensions, *Work Programme Evaluation: Procurement, supply chains and implementation of the commissioning model,* p.4

[114] Employment and Support Allowance is the main benefit for people who are unemployed and have a limited capability for work because of their health. It replaced incapacity benefits for new applicants in 2008.

[115] Simmonds, D., (2012), *The Work Programme and the Voluntary Sector*, Centre for Economic and Social Inclusion website, 2012, retrieved 8 June 2013, http://www.cesi.org.uk/keypolicy/work-programme-and-voluntary-sector

[116] Department for Work and Pensions, (2013), *Work Programme Evaluation: Procurement, supply chains and implementation of the commissioning model,* p.47

[117] Interview with prime contractor organisation

[118] Department for Work and Pensions, (2013), *Work Programme Evaluation: Procurement, supply chains and implementation of the commissioning model,* p.46

[119] Interview with prime contractor organisation

[120] For analysis see Damm, C., (2012), *The Third Sector Delivering Employment Services: an Evidence Review*, Third Sector Research Centre, January 2012, retrieved 5 June 2013, http://www.tsrc.ac.uk/LinkClick.aspx?fileticket=aoUqP0rW6m8%3D&tabid=873

off for DWP was to ensure that successful providers were large enough to shoulder the risk in the contracts and achieve economies of scale.

In the end, the VCS and smaller private sector organisations that were able to enter the programme did so as specialist sub-contractors. However, many have come under financial strain due to the ambitious pricing levels and inaccurate referral flows discussed above. The pricing levels have led some (but not all) prime providers to pass outcome risk down the chain to these sub-contractors, the majority of whom cannot survive on the timing of the payments. To make matters worse, lower numbers of ESA referrals has meant that many of these sub-contractors have received few, if any, referrals, and therefore very little income from the Work Programme.[121]

DWP's decision to opt for a hands-off 'black box' approach to supply chain management (which was welcomed by all prime providers) limits its ability to directly intervene and correct these problems. It therefore decided to establish a light-touch regulatory regime in the form of the Merlin Standard, but this is widely seen to be ineffective. First, it cannot intervene in commercial decisions and thus has no influence on the terms of the relationship between prime contractors and sub-contractors. Second, it advises sub-contractors to first raise complaints directly with their prime and resolve any disputes through dialogue. But our interviewees told us that the 'gagging clauses' many sub-contractors are subject to effectively constrain their ability to raise complaints.[122] As a result, we heard that no dispute has been brought to the Merlin mediation service.

This limited right to recourse has reportedly made it difficult for some small voluntary and private sector organisations to protect their financial viability. Indeed, a recent study conducted by the National Council for Voluntary Organisations (NCVO) found that 73% of the voluntary organisations it surveyed believed their contracts were at risk of failure before the end of the contract.[123] As a result, some explain that they are left with no option but to voluntarily exit the market, which raises concerns that those left competing in the market are not necessarily the best performing. It seems that DWP is not currently monitoring this activity which is vital to understanding the 'health' of the market and the barriers to expansion that some effective sub-contractors face.

Inconsistent contract management regime does little to improve performance

> It is 'black box' with 300 pages of guidance.
>
> Director at a prime contractor organisation

Minimum performance levels are a key lever by which DWP can hold providers to account, punish poor performers by imposing penalties and manage the exit of under-performers (by terminating their contract altogether). However, the contract specified that the department would not apply any 'hard' penalties such as market share shifting or withdrawal of contracts for the first two years of operation (till June 2013). Therefore, in light of the performance achieved to November 2012, DWP placed all 18 providers on 'performance improvement plans' to identify why performance was below expectations and how it could be improved. In addition, DWP sent formal letters to the providers responsible for seven of the contracts where it believed performance was not acceptable, requesting details of the actions they would take to improve performance.[124]

Both providers and officials told us that the department has historically always been reluctant to impose 'hard' penalties and has yet to terminate a contract of an under-performing provider. Whether this is true or not, perceptions matter for the credibility of the threat. As one interviewee put it, DWP 'has just taught the market all the wrong lessons' which means that there is no real pressure on providers to improve.[125] If this is not addressed in year three of the programme, there is a risk that the programme may end up being dominated by coasting or under-performing providers.

This observably 'loose' approach to contract management actually masks the numerous reporting procedures DWP have established to monitor activity and performance (see Figure 9). While some providers felt that these reporting lines functioned smoothly, others complained that they had become overly onerous and a form of

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[121] Simmonds, D., (2012), *The Work Programme and the Voluntary Sector*, Centre for Economic and Social Inclusion website, 2012, retrieved 8 June 2013, http://www.cesi.org.uk/keypolicy/work-programme-and-voluntary-sector

[122] Interview with sub-contractor organisation

[123] National Council for Voluntary Organisations, *The Work Programme: Perceptions and Experiences of the Voluntary Sector,* p.10

[124] House of Commons Committee of Public Accounts, *Department for Work and Pensions: Work Programme Outcome Statistics. Thirty-third Report of Session 2012-2013.* House of Commons, p.9

[125] Interview with prime contractor organisation

'constant encroachment' that impede rather than facilitate performance.[126] At times, this was simply due to the ad-hoc and random nature of the requests stemming from new political priorities elsewhere in government. For example, one provider told us that Nick Clegg placed a renewed emphasis on the wage incentive scheme, which led its performance manager to urgently demand information on what the provider and its sub-contractors were doing to promote the scheme.[127]

The larger problem, however, seems to stem from a fundamental difference in understanding between prime providers and performance managers about how much flexibility they are allowed in their delivery models. On one hand, providers view the 'black box' model as a 'form of contractual protection' where they have the freedom to constantly flex delivery during live running to respond to 'what works'.[128] On the other, performance managers generally view the 'black box' as having only applied during the procurement, meaning that once contracts are awarded providers must deliver in accordance with their bids.[129] As a result, providers have had to submit contract variations and get approval for things they thought were within their discretion. Contradictory messages from different DWP officials (in particular, between account managers who reportedly encourage providers to flex delivery and performance managers who discourage it) have left providers confused about the elements of delivery they have flexibility to change.[130]

Many felt that these reporting procedures were not only demanding (and inconsistent) at times, but serve no obvious purpose and therefore add little to DWP's ability to effectively monitor contracts. For example, DWP is not currently seen to be proactively collecting information on supply chain data (which could help it to identify where problems lie) nor user satisfaction levels across contract package areas (which could serve as a valuable proxy for quality).[131] This raises questions about how DWP intends to spur rapid adoption of best practice across the market.

In summary, both officials and providers felt that DWP's approach to contract management tends against decisive action (which could better stimulate performance), while placing heavy (and inconsistent) demands on providers that, on balance, do not focus on the things that could actually improve performance.

Strict adherence to competition principles leads to high transition costs

> The aim is to get the biggest footprint you can for the structure you already have there.

Director at prime contractor organisation

> All the work we had done in [that area] was lost.

Director at prime contractor organisation

DWP officials followed EU procurement rules which they believed made it unlawful to assess providers on past experience or performance so as not to disadvantage new entrants to the market. As a result, contracts were often awarded to providers in areas where they had no previous track record, with many moving in between regions. For instance, nine out of 10 primes that already had contracts with the Department for pre-existing schemes won at least one contract in a geographical area where they had not previously delivered services and five out of 10 primes lost contracts in areas where they had existing operations.[132] As one interviewee put it, this sometimes meant 'that the best performing FND organisation lost the contract in that area and won the one next door'.[133]

This seemingly marginal contract evaluation decision actually had huge practical implications. Providers told us that those who won a contract in an area where they had an existing geographical presence were able to move

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[126] Interview with prime contractor organisation

[127] Interview with prime contractor organisation

[128] Interview with prime contractor organisation

[129] Department for Work and Pensions, *Work Programme Evaluation: Procurement, supply chains and implementation of the commissioning model,* 2013, p.3

[130] Department for Work and Pensions, *Work Programme Evaluation: Procurement, supply chains and implementation of the commissioning model,* 2013, p.43

[131] Interview with prime contractor organisation, sub-contractor organisation, JobCentre plus official and provider representative body

[132] National Audit Office, *The Introduction of the Work Programme,* 2012, p.29

[133] Interview with prime contractor organisation

quickly, while those who didn't 'were on the back foot'.[134] These providers experienced unnecessarily high transition costs primarily because it takes time to move staff, set up a new office, develop local market intelligence and establish supply chains.[135]

Providers also felt that the re-allocation of contracts had a knock-on effect on their relationship with Job Centre Plus (JCP). In previous schemes, they told us that potential coordination problems had generally been overcome by the co-location of staff which facilitated regular interactions, information sharing and a 'warm handover process'.[136] The movement of providers to different areas had the effect of ending these collaborative relationships.

DWP decided not to reinstate co-location between JCP and providers to ensure a level playing field between the two to three primes operating in each CPA. But in practice this has introduced a greater geographical distance between the local JCP and Work Programme provider, which at times has led to delays in the communication of critical information and increased the potential for misunderstanding.[137] Indeed, one JCP district manager explained to us that 'no-one actually knows what's in the black box which leads to suspicion on the part of JCP advisers as they don't know what they are referring to'.[138] This makes it difficult for them to filter information down to claimants and prepare them for the Work Programme, which is vital for early and successful engagement. For example, we heard of one case where a referred claimant mistakenly thought that he was attending an interview for an actual job. This meant that the provider had to spend the first few appointments explaining the purpose of the Work Programme delaying the time between referral and attachment to the programme and thus initial performance.[139]

The decision to prioritise the principles of competition at the expense of practical implementation considerations seems to have unintentionally led to higher transition costs, which explains the initial performance dip observed.

Underlying causes

The problems stemming from the design and implementation choices identified above will be familiar to many of those involved in the sector. These are not necessarily unique to the Work Programme, having often surfaced in previous programmes. The key question is why these have not been solved through a gradual learning process, but instead persisted. We argue that these can be traced back to the underlying skills, incentives and ways of working of the various actors involved in the system. We highlight in particular:

- highly-personalised leadership
- side-lining of departmental and government risk-management processes
- bias towards a transactional approach to contracting
- low incentives for cross-departmental and agency collaboration.

Highly-personalised leadership

There was consensus among our interviewees that Chris Grayling came to the department with 'a lot of drive, energy and conviction' combined with a very specific idea about what he wanted to achieve: the Work Programme would be based on a 'payment by results', prime provider and 'black box' model. These key decisions were non-negotiable.[140] Grayling not only took a highly hands-on approach in the design of the programme, but set demanding timescales of less than a year for implementation.

This political leadership was crucial for setting the strategic vision of a major project. It essentially 'forced DWP officials out of the silos'.[141] Grayling convened a tight coalition of senior officials from across the department, sometimes as often as two to three times a week. One official told us that DWP could not have delivered on the

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[134] Interview with prime contractor organisations

[135] Interview with prime contractor organisation and provider representative body

[136] Interview with prime contractor organisation

[137] Interview with provider representative body and JobCentre plus official

[138] Interview with JobCentre plus official

[139] Interview with prime contractor organisation

[140] Interview with expert adviser and provider representative body

[141] Interview with civil servant

timescales or pace without this strong political commitment which successfully brought together different departmental interests to achieve a common goal.[142]

This political leadership was complemented by a cadre of high-skilled senior officials who had developed strong capabilities in designing and commissioning large-scale employment service programmes. These capabilities were nurtured by well-functioning internal relationships. In 2007, the decision to co-locate policy, delivery and commercial teams ensured that, during the inception of the Work Programme, policy flowed right through to the market design.[143] Yet, there was constructive challenge, when possible. For example, officials, on the advice of providers and investors, were eventually successful in convincing Grayling that 100% outcome-based contracts would be commercially unattractive.[144]

However, we were told that this leadership was highly personalised at both the ministerial and official level. This meant that the departure of key individuals could severely disrupt the smooth running of the programme. Indeed, after the cabinet reshuffle in September 2012, Mark Hoban replaced Chris Grayling as the Minister for Employment. This coincided with a high degree of churn at the official level which left providers confused as to who exactly was in charge. One interviewee explained, 'We oscillate between very senior officials and then someone will suddenly become quite influential, and then they disappear.'[145]

To outside observers, there was a general perception that no one person was in charge. Providers felt that the commercial and diplomatic skills of the officials who designed the programme, but had subsequently left, were not widely shared across the department. Particular concerns centred on the extent to which the department had invested in smooth transition planning to ensure that the officials who took over were fully prepared for the new roles. As a result, some providers told us that their relationship with the department somewhat deteriorated during this time.[146]

The absence of clear steers from the senior leadership potentially contributed to the inconsistent contract management regime observed at the operational level. Providers complain that they have had multiple contacts with different DWP personnel (e.g. one provider is on its ninth local performance manager since the Work Programme started).[147] This has often resulted in duplication of (and sometimes contradictory) communication which does little to aid performance.[148]

Side-lining of departmental and government risk-management processes

The department's performance and commercial assumptions were subject to intense scrutiny from the Treasury, KPMG and the Major Projects Review Group. Officials told us that these processes were often highly time-consuming and burdensome.[149] Yet, none of these cross-government assurance processes were seen to mitigate the risks associated with the Work Programme, particularly the ambitious performance expectations as well as challenging timescales.

Arguably, the need for external challenge was even greater in the Work Programme primarily because one department, DWP, was responsible for all aspects of market design and implementation. This meant that there was a high risk that the drive to implement quickly would lead to the side-lining of the risk-management processes the department had assiduously developed over the preceding years.

Indeed, this is what happened in practice. First, the department had historically piloted all previous schemes before implementing them. But, in the case of the Work Programme, the department could not pilot it and meet the challenging timescales.[150] Second, officials advocated a price discovery process to allow for adjustments in price if the initial assumptions were shown to be too high or low. However, a phased approach was directly contrary to Grayling's desire for 'big bang' change. In the end, the Department had to devise the business case for the Work

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[142] Interview with civil servant

[143] Interview with civil servants

[144] Interview with civil servants and expert advisers

[145] Interview with provider representative body

[146] Interview with provider representative bodies and expert advisers

[147] Interview with prime contractor organisation

[148] Interview with provider representative bodies

[149] Interview with civil servant

[150] Interview with civil servant

Programme after the main decisions had been made and before robust data on cost was available.[151] Third, DWP had historically always aimed for a standard six-month period between award of contract and live running. However, this had to be reduced to around two months to meet political timescales and presented a major challenge for those providers who were awarded contracts in areas where they did not yet have an existing geographic presence.

Lack of institutional mechanisms for challenge

It is unsurprising that politicians will sometimes prioritise short-term delivery over long-term programme outcomes. This partly stems from the political cycle that creates a career incentive structure that rewards 'big bang' change. As a result, there are often weak short-term incentives for politicians to properly consider all options and manage the risks that could undermine value for money in the long-term.

The key problem is that there are currently no institutional mechanisms to help civil servants ensure that the specific objectives of the minister are met, while delivering value for money in the long term. As we argued in our *Policy Making in the Real World* report, 'Good policies will emerge from achieving the right blend of the political (mobilising support and managing opposition, presenting a vision, ability to set within a wider set of strategic objectives) and the technocratic (evidence of what works, robust policy design, good implementation plans).'[152]

But ministers have to recognise and value the role civil servants can play in providing such challenge. If they do not, and in the absence of institutional support, civil servants will often revert to the easy option of giving ministers what they want. One DWP official explained, 'In principle we could have had a discussion [with the minister], but to be honest there was really no point in trying to have a discussion.'[153] This meant that, although the Department had developed a strong commissioning capability and understood 'what worked', the learning was not fully capitalised on during the Work Programme.[154]

Bias towards a transactional approach to contracting

Both providers and commissioners told us that there was a degree of mutual mistrust during the design and tendering process. Providers complained that legitimate concerns were often met with silence and sometimes even threats of forced withdrawal from the competition,[155] while commissioners felt that providers were simply pushing for more favourable commercial terms that could undermine value for money for the taxpayer.[156] As a result, commissioners kept providers at arm's length during the process of establishing performance and financial assumptions. This made it very difficult for providers to scrutinise the assumptions and provide constructive challenge. As one provider put it, 'I think procurement was very complicated, and the financial model very complex, and the complexity of that remains.'[157]

In practice, this lack of dialogue meant that commissioners ended up designing a contract with little understanding of how providers were likely to respond to commercial incentives and providers ended up building financial models with little understanding of how assumptions were derived. This seems to have encouraged the submission of unrealistic bids potentially unable to cover the costs of provision for different claimant groups.[158]

This 'transactional' approach to contracting has flowed into contract management and monitoring during live running. Although the department aims for a hands-off approach to match the language of the Work Programme, many of our interviewees told us that the department nonetheless imposes a number of ad-hoc information demands on providers.[159] One interviewee explained to us that this is counter-productive as DWP actually ends up getting the worst of both worlds: 'quite hands-on control really, but not really thought through because it's more like we're pretending not to. As a result, you get lots of monitoring about some things in a structured way, and not so much about other things'.[160]

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[151] National Audit Office, *The Introduction of the Work Programme,* 2012, p.8

[152] Hallsworth, M., Parker, S., and Rutter, J., *Policy making in the real world,* 2011, Institute for Government, p.89.

[153] Interview with civil servant

[154] Interview with civil servant and prime contractor organisations

[155] Interview with prime contractor organisations and provider representative body

[156] Interview with civil servant

[157] Interview with prime contractor organisation

[158] Interview with sub-contractor, prime contractor organisations and provider representative body

[159] Interview with expert adviser and prime contractor organisations

[160] Interview with expert adviser

Indeed, the department has yet to demand transparency from providers around the information that could actually drive performance such as supply-chain management and user-satisfaction levels. This problem has surfaced elsewhere in government – for example, our research on arm's-length bodies (ALBs) found that the lack of common performance-monitoring frameworks has made it difficult for departmental sponsors to achieve the appropriate balance between freedom and control.[161]

Procurement and contract management capabilities

This 'transactional' approach to contracting seems to stem from the skills set and ways of working nurtured in the procurement and contract management profession. There was a general perception among our interviewees that procurement professionals are highly skilled in buying services at the lowest cost possible and remaining in strict accordance with EU procurement rules.[162] This seems to primarily stem from the fact that procurement professionals are rewarded for delivering upfront cost reductions rather than long-term programme outcomes.

This means that there are weak incentives for professionals to familiarise themselves with the tools and techniques that could be used to stress-test changes to provider incentive systems and ensure better outcomes in the long term.[163] In addition, concerns for fairness often mean that they have to deal with a very large number of suppliers for extended periods, making the development of close, collaborative relationships practically difficult.

Likewise, we heard that contract managers are trained to manage large-scale contracts in a 'check-list environment', which means that they are highly skilled in day-to-day management of contracts, but sometimes not as experienced in managing relationships. One official explained to us that the 'black box' approach to contracting is culturally very new and therefore it will naturally take some time for professionals to adjust their ways of working.[164] Therefore, the issue is not necessarily a lack of skills, but the types of skills and the ways of working these professionals have developed.

Provider capabilities

There seems to be a general consensus among providers that DWP's bias towards a transactional approach to contracting does little to nurture the healthy, collaborative partnerships needed to drive long-term outcomes. Yet these partnerships do not solely depend on government, but on provider capabilities as well.

By the time the Work Programme was announced, there was a mature supplier community that had been delivering employment services for nearly two decades. A wide range of industry bodies[165] had also developed during this time to facilitate the sharing of knowledge as well as increasing the voice and unity of the 'provider interest'.[166] It is therefore puzzling that providers did not identify the risks inherent in the department's assumptions, but instead worsen them by offering heavily discounted bids.

This could be because commercial and bid managers are generally incentivised by bonuses, which promotes a tendency to prioritise short-term contract wins regardless of their long-term viability. This is particularly understandable given that the termination of all previous programmes made the Work Programme the 'only game in town'. As a result, many providers were desperate to win contracts and saw a 'loss leader' strategy as the only way to ensure this.[167] This must-play mentality skewed incentives towards offering heavy price discounts which potentially stretched the financial viability of the contracts.

But this raises a fundamental question around the extent to which providers are capable of (as well as willing) to engage in robust risk management and mitigation. Indeed, some providers told us that their bids for the Work Programme were merely tweaked and re-submitted versions of their previous FND2 bids,[168] even though the level of risk had changed significantly. This highlights the need for providers to improve their ability to identify risks and provide constructive challenge to commissioners before accepting major contracts.

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[161] Gash, T., Rutter, J., Magee, I., and Smith, N., *Read Before Burning: How to Increase the Effectiveness and Accountability of Quangos*, Institute for Government website, July 2010, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/read-burning

[162] Interview with civil servant and prime contractor organisation

[163] Interview with expert adviser

[164] Interview with civil servant

[165] For example, the Employment Related Services Association (ERSA)

[166] Interview with provider representative body

[167] Interview with expert adviser and provider representative body

[168] Interview with prime contractor organisation

Low incentives for cross-departmental and agency collaboration

The difficulties providers have experienced in joining up with their district JCP and other sectors (especially skills) fundamentally stems from a misalignment of incentives that is largely beyond their control. On one hand we heard that some JCP managers and front-line advisers regard the Work Programme as 'unwelcome competition' which threatens their entire raison d'etre – that is, to help clients find work and move off benefits.[169] The more clients they refer to the Work Programme, the less their role is needed. As a result, JCP managers are actually motivated to prevent clients from having to enter the Work Programme at all. One district manager characterised the relationship as one of 'earth grabbing' and 'defending territory'.[170] On the other hand, further education colleges and training providers are driven by a different set of incentives altogether – payment by qualification rather than job outcome. This means that they are primarily motivated to deliver as many qualifications as possible regardless of employment outcomes.[171]

Insufficient focus on change management

The Department could have addressed some of these difficulties through a well-managed change process focused on aligning incentives across institutional boundaries and improving co-ordination. Previous Institute research has highlighted the critical need to continually communicate policy objectives and build a broad coalition for change to make implementation of large-scale reform both easier and less controversial.[172] However, we heard that the Department provided insufficient, and sometimes even incorrect, information to JCP district leaders and their teams, which made many reluctant to implement policy objectives.[173] This potentially stems from the fact that the department no longer has large policy teams closely monitoring JCP performance and expenditure, and oversight has moved to the finance team. This has reportedly shifted the emphasis solely onto financial targets and, beyond this, JCP 'does what it likes'. [174]

The lack of direct oversight over providers from other sectors meant that DWP had to secure the buy-in of other central government departments and agencies for their reforms, particularly the Skills Funding Agency (SFA) which funds adult further education and skills training in England. Although there are a few multi-disciplinary teams, reduced budgets have encouraged retreat into departmental silos, rather than collaboration.[175] As a result, providers told us that it has generally been difficult to access SFA funding, which limits their ability to join up a range of training services around individual needs.[176] Those who have been able to access SFA funding felt they had done so 'in spite of the system'.[177] While those with diverse portfolios (e.g. employment, skills and offender-facing services) were able to do so far more easily than those who only focus on employment.[178] However, these were exceptions rather than the norm. This highlights the need for the department to actively facilitate joined-up service provision, for example through pooled budgets, rather than simply leaving providers to muddle through the system itself.

Areas of focus

In this section, we outline the areas of focus that merit immediate investigation to improve the Department's ability to deliver public services through market mechanisms.

- **Vision and objectives**: Chris Grayling, then Minister for Employment, played a central role in defining the vision for the Work Programme and driving fast-paced implementation. This type of political commitment is highly important in generating the confidence of officials, providers and investors that a 'market' will be established (or expanded). However, it was unclear whether the objective of the Work Programme was simply to reduce the cost of outsourced provision or drive innovation in delivery, particularly in services for those with complex needs. If it was the latter, the overall funding for the programme is widely seen to be

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[169] Interview with sub-contractor organisations and JobCentre plus official

[170] Interview with JobCentre plus official

[171] See Panchamia, N., *Choice and Competition in Further Education,* 2012, Institute for Government.

[172] Gash, T., and Roos, T., *Choice and Competition in public services: learning from history.* 2012*,* Institute for Government

[173] Interview with expert adviser

[174] Interview with expert adviser and provider representative body

[175] Interview with sub-contractor organisation

[176] Interview with prime contractor organisations

[177] Interview with prime contractor organisation

[178] Interview with sub-contractor organisation

inadequate. This lack of clarity has also led to an inconsistent contract management approach whereby individual contract managers place excessive (and sometimes inconsistent) bureaucratic burdens on providers that serve no obvious purpose. This highlights the importance of identifying from the outset what it is that politicians and civil servants hope to achieve from using market mechanisms – savings or innovation – and set pricing and performance measures accordingly.

- **Data and transparency:** The Department's aim to publish performance figures in a timely, clear and transparent manner can be a powerful lever by which it can scrutinise and hold providers to account. But delays in releasing the first set of performance figures and the reluctance to withdraw contracts can significantly reduce the pressure on providers to improve. We welcome the Department's plan to publish performance figures on a quarterly basis from now on, but argue that transparency can and should be augmented further. In particular, we recommend that the department oblige prime contractors to publish details of the funding they receive from government, the suppliers to whom they sub-contract services, the value of these contracts and their performance. This latter step may appear to push against 'black box' principles, but we argue that departmental knowledge of the sub-contractor landscape is vital to understand the health of the provider market, identify in advance the risk of undue consolidation and spot potential future primes. Transparency around supply chains would also spur competition between primes for effective sub-contractors enabling these sub-contractors to expand more rapidly. Providers were far from opposed to publishing this additional data and several experts suggested to us that rules on 'commercial confidentiality' need not prove an insurmountable obstacle to publication.

- **Provider relationships and co-production:** There can be a natural tendency to keep providers at arms-length during the tendering process, given the sheer number of providers involved and the need to maintain credible competitive tension. This approach can, however, make it more difficult to capture provider insights and understand how they will respond to contractual incentives. We therefore urge the department to redesign the commissioning process in ways that combine collaboration with procedural fairness. One way of doing this could be to stress-test changes to incentive systems with a commercially-minded challenge board that understands the provider perspective, but is not vested in the contracting process. Another option would be to run scenario and simulation exercises with a small number of provider representatives to design top-level contract specifications.[179]

- **Flexibility:** The rapid implementation of the Work Programme meant that programme benefits could be quickly realised, but this understandably left little time to phase roll-out or fully test programme assumptions. This clearly limited the department's ability to identify and correct any difficulties early on, particularly in relation to pricing and referral assumptions. Given that there is not always time to engage in a lengthy testing process and that some things are simply difficult to predict in advance, we recommend building greater flexibility into contracting models to allow for ongoing learning and adaptation. One route to this would be to contract on a rolling cycle, as happens in rail franchising, where commissioning models are gradually adapted over time so that failures tend to be confined to individual projects, rather than systematic. It may also be feasible to tie fees received to how effectively providers help jobseekers into employment, compared to a small randomly selected sample of individuals who receive no service.

- **Cross-sector co-ordination:** If outcomes are dependent on the performance of other services, the assumption is that the payment structure alone will incentivise providers to do the 'joining up'. Our research found, however, that providers from all sectors experienced some difficulties in co-ordinating with related services (i.e. JobCentre Plus, skills and health) due to structural incentives for government organisations to primarily focus on their own set of objectives, rather than broader outcomes and value for government. Although we recognise that these are often difficult to overcome, it is important for the department to actively facilitate more effective cross-sector partnerships. Potential options include introducing cross-sector commissioning teams, profit-sharing agreements and co-location of providers.

- **Market stewardship:** Finally, we urge the department to re-examine its approach to commissioning, adopting what we call a 'market stewardship' approach. Our Market Stewardship framework (figure 3, p. 19) identifies the main functions that need to be performed to effectively oversee and steward public service markets. In this respect, we believe that it is necessary to have single points of accountability for contracted services – for example, a senior responsible officer (SRO) who is responsible for the value for

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[179] Further options are outlined in section one of this report and in Blatchford, K., and Gash, T., *Testing New Commissioning Models: A Guide to Help Policy Makers Learn about Publicly-funded Markets*, Institute for Government, London, 2012, retrieved 16 July 2013, http://www.instituteforgovernment.org.uk/publications/testing-new-commissioning-models

money of each public service market and incentivised to remain in post for at least three to five years to ensure stability of oversight throughout the duration of the contract.

Secondary Education

Summary

Since 2010, the landscape of secondary education in England and Wales has changed considerably. Building on the reforms of previous Labour and Conservative governments, the majority of secondary schools have now converted to 'academy' status, which has given them significant additional autonomy over their curricula, finances, and management. Academies are now funded largely based on how many pupils they can attract, meaning that schools are being encouraged to actively compete to attract pupils. They are also being encouraged to join with other academies in federations or chains to share resources and knowledge, and to purchase support services cost-effectively. Academies operate with minimal government interference, although they must submit to regular inspections and their exam results are published. However, when school performance falls below the government's floor standard, governing boards must hold open competitions to find new management ('sponsors').

Operating this new, market-like system in secondary education is not straightforward. Education is a complex service and it is difficult to measure and inform users about the value added that schools actually deliver, partly because results are so often driven by the quality of school intake. Unwillingness or inability to travel great distances to reach schools also limits choices available to pupils – and therefore the degree to which competition will affect different schools. Barriers to school expansion can also limit incentives for effective providers to grow.

In a well-functioning market, good schools (or sponsors) should be able (and eager) to expand and poor schools (or sponsors) should either improve, or shrink and close. However we found evidence of some schools persistently offering poor-quality education without consequences and, conversely, good schools closing down due to the effects of distorted competition. Very few good schools opt to expand onsite and, while expansion through federation and sponsorship is now increasingly common, there is little publicly-available evidence on the relationship between sponsor quality and sponsor expansion.

In addition to structural limitations on choice, we found further barriers. For example, choice is significantly constrained in both rural and urban areas by admissions criteria and school transport policies, which often only provide free travel to the nearest school. There are also a number of supply-side factors distorting competition. Schools with similar intakes receive significantly different amounts of funding per pupil, which means they are competing on an uneven playing field. There is also evidence that some schools, particularly those which are in danger of falling below the floor target, are engaging in behaviour that increases their measured performance but does little to improve education for pupils. This 'gaming' comes in four main forms: cream skimming; parking; crowding towards the target and choosing easier-to-pass qualifications.

Our analysis suggests that the Department for Education (DfE) has not yet fully identified and appropriately assigned the full range of functions that need to be performed to effectively steward the new market in secondary education. In particular, it is not clear who is responsible for ensuring that there is effective choice and competition in any locality or what levers exist to influence choice or competition. Governors are formerly responsible for selecting new sponsors when a school falls below the floor standard, though in reality DfE often plays a big role. However, individual governing bodies have limited incentives to consider how their choice of sponsor will affect competition in an area or to stimulate new market entrants – and the infrequency with which they perform the commissioning role suggests that they are in practice unlikely to perform it very effectively. Although the DfE now systematically collects information on sponsor performance, this information is not publicly available to either local authorities or school governing bodies.

Despite the fact that this is clearly a market mechanism it is unclear to what extent the DfE sees it as such. This has had knock on effects on performance because, to our knowledge, little has been done to try and analyse the way in which the market will develop or to put in place measures to develop and sustain competition. The pace of change has hindered the Department's ability to test reforms in order to understand how they will play out in different local markets, for example through dialogue with local authorities and providers or through simulation and scenario exercises.

Some (but not all) of these problems have been identified by the DfE and others operating in the system, such as the inspectorate, Ofsted. DfE is currently consulting, for example, on proposals to develop new performance metrics and floor standards to reduce gaming and deal with coasting schools. The Department is also not simply

relying on competition to drive improvement, and has placed significant emphasis on curriculum reform and encouraging partnerships of school support. However, this analysis suggests that further change is required before DfE can ensure that the market it has created is likely to deliver the best possible outcomes for taxpayers and students.

History

Parents were first given the right to choose a publicly-funded school by the Education Act of 1980. Open enrolment allowed parents across the country to choose which school their child attended as long as that particular school was not oversubscribed, in which case the local authority would allocate them to a school. In 1988 Kenneth Baker's Education Reform Act gave state schools the chance to hold a parental vote to opt out of local authority control. One in six secondary schools chose to do so representing a significant increase in school autonomy (and therefore variety) in the school system. Funding arrangements were adjusted to link a larger proportion of school funding to the number of pupils attending a school, placing schools in direct competition with each other for resources. The legislation standardised course content and examinations through the introduction of the national curriculum, making schools results more comparable.

Ken Clarke took over the Department for Education (DfE) in 1990 and promised to build on Baker's work to increase choice and diversity. School inspection was centralised in 1992 and the results of Office for Standards in Education (Ofsted) inspections were made public, increasing parent's ability to judge school quality. League tables were introduced with the explicit intention of helping parents to systematically compare schools.

In 1997, the incoming Labour government based their reform programme on the mantra of 'standards not structures' and reduced the emphasis on choice as a driver of educational standards. Early reforms to the admissions code were implemented to stop schools selecting pupils based on attainment. They introduced the Academies Programme. Academies are independently managed state-funded schools that have more operational autonomy than other types of schools. In 2002, the first academy schools opened replacing failed predecessor schools.

In 2005 the white paper, *Higher Standards, Better Schools for All: More Choice for Parents and Pupils* marked the return of choice as a key strand of school reform. Tony Blair openly described the reforms as being aimed at establishing what 'would in one sense be a market'.[180] Free school transport was extended to cover the three nearest schools for poorer pupils (rather than just the nearest) and choice advisers were created to help poorer parents decide which school to apply to. Local authorities were, for the first time, put under a statutory obligation to promote diversity and choice among schools. They were also obliged to hold an open contest between potential providers for any entirely new school which they wished to open. This, along with the increased use of academy sponsors to take over failing schools, added an element of commissioner choice to the pre-existing system of user choice.

The Coalition Government has dramatically increased the rate of academy conversion. Free schools (a variant on the academy model, allowing parents or teacher groups to start up entirely new autonomous schools) and studio schools (focusing on practical, project-based learning) have also been introduced, further increasing diversity of supply. Changes to school finance have increased the extent to which funding follows pupils and academies, and voluntary-aided schools have been given the freedom to vary the number of pupils they admit – allowing popular schools to increase in size if they want to. The Coalition Government is also in the process of introducing a set of new attainment and progress measures in school league tables, explicitly designed to help parents choose the school in which their child will do best.

In summary, we now have a system in which parents make a constrained choice of school for their child, governing bodies can choose sponsors (though often with heavy involvement from the Department for Education) to replace failing schools, and open competitions must be held by local authorities to decide who will run any entirely new school. Choice and competition in secondary education therefore operates through two different mechanisms – user choice (by parents) and commissioner choice. For a more detailed account of choice and co-operation in schools see *The Development of Quasi-Markets in Secondary Education*.[181]

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[180] Blair, T, 'In full: Blair's education speech' BBC online, 24 October 2005, retrieved 5 June 2013, http://news.bbc.co.uk/1/hi/uk_politics/4372216.stm

[181] Sims, S., *The Development of Quasi-Markets in Secondary Education*, Institute for Government website, November 2012, retrieved 8 June 2013, http://www.instituteforgovernment.org.uk/publications/development-quasi-markets-secondary-education

Inherent difficulties

There are several characteristics of secondary education that create particular challenges for delivering it through mechanisms of choice and competition. These do not appear to be insurmountable barriers, but a well-functioning system of choice and competition will be designed to mitigate and overcome them.

Perhaps the most important characteristic of secondary schooling is the difficulty of measuring the causal impact of schools on pupil attainment. This difficulty has several causes. Schools attempt to produce a range of outcomes for students extending far beyond formal qualifications, for example, character development, social skills and civic responsibility. Even if we do agree to restrict the measurement of performance to exam results there are difficulties in aggregating the overall 'value' of different qualifications. It is also hard to control differences in, for example, student intake in a way which allows us to isolate the causal impact of a particular school. It may be possible to control this statistically but so far the most sophisticated attempts in the UK have generated only very imprecise estimates, suffer from omitted variables and missing data, and are hard to interpret.[182]

Another important characteristic of secondary education is the economies of scale involved in its provision. Providing a broad curriculum requires a certain number of students to achieve economical class sizes – it is very expensive to offer a subject if only 10 or 15 people want to study it. Non-maintained schools face significant financial and managerial economies of scale. Federations of schools can 'purchase' teacher training internally by getting, for example, a strong history department in one school to train teachers in a weaker history department in another school, helping to keep costs down. Given these economies of scale, and a limit on students' willingness to travel, as population density declines so do the number of schools they can choose from within a given distance.

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[182] Gorard, S. (2010) Serious doubts about school effectiveness, British Educational Research Journal 36(5); Allen, R., and Burgess, S., 'Can school league tables help parents choose schools?' *Fiscal Studies*, Vol. 32, No. 2, pp. 245-261, 2011; Leckie, G., and Goldstein, H., 'Understanding Uncertainty in School League Tables', *Fiscal Studies*, Vol. 32: 207–224, 2011; Dearden, L., Miranda, A., and Rabe-Hesketh, S., 'Measuring School Value Added with Administrative Data: The problem of missing variables', *Fiscal Studies*, 32: 263–278, 2011

Figure 11: Characteristics of secondary education

In order to assess...	...Ask	RAG Rating	Details
The appropriateness and effectiveness of user choice mechanisms	Do consumers face high switching costs?	Problematic	Switching schools is possible but costly in terms of disruption to education and social groups.
	Are consumers often involved in distress purchasing?	Unproblematic	Generally well planned.
	Is the service a merit good?	Problematic	Generally considered a merit good, but legal requirement to consume up to age 16 make this less important. Socialisation of children in schools is considered by some to have strong merit good components.
The costs and risks of using market mechanisms, and the need for regulation to mitigate these risks	Is it difficult to measure the value added of providers?	Problematic	It is hard to accurately and precisely measure the causal effect of a school. Contextual Value Added (CVA) is flawed because it's imprecise and has problematic missing variables. In general, there are trade-offs between accuracy and functionality.
	Are service outcomes highly dependent on the performance of other services?	Problematic	Exam results can generally be delivered just by a school, although child health and housing quality can effect educational achievement.
	Does delivering the service require investment in highly specific assets?	Problematic	School buildings are specific assets – but the separation of asset ownership and management in the Academies Programme diminishes some of the risks in relation to this.
	Is the service characterised by high demand uncertainty?	Unproblematic	Predictable, based on demographic information, although there is only a four-year lead-time for primary.
	Is the service characterised by high policy uncertainty?	Unproblematic	Government is very unlikely to reduce demand for, or entitlement to, education.
	Is the service essential for government's ultimate decision making or coercive authority?	Unproblematic	No.
The ease and cost of transition from a fully government-owned and delivered service to one based on market mechanisms	Is there an existing supply of (high-quality) providers?	Problematic	There is an existing supply of high-quality schools. There are fewer school chain managers, meaning that the 'middle tier' of schools oversight is less well developed.
	Is there an existing workforce (either in the public or private sectors) with adequate skills and capabilities to deliver high-quality services?	Unproblematic	There is a generally capable and qualified teaching profession.
	Does the government have the organisational capability to design and monitor the use of market mechanisms?	Problematic	The DfE has limited experience in market design and oversight and is performing many of its oversight roles for the first time as responsibilities have shifted away from local authorities. Local authorities have variable capability.
	Does the government have enough information about cost and quality to measure provider performance?	Problematic	There is a significant amount of high-quality information on school attainment through exam results and inspections. Determining the value added and capability of individual schools and chains remains difficult, however.

RAG Rating Key

Highly Problematic	(magenta)
Problematic	(tan/brown)
Unproblematic	(teal)

Market strengths and weaknesses

We assess how well the government has organised the quasi-market for schools to overcome these challenges. We focus particularly on the degree to which government is supporting several prerequisites to an effective market:

- informed user and commissioner choice
- appropriate funding
- entry and expansion of promising providers
- competition on performance
- orderly contraction or exit of underperformers.

However, we note that there are important additional steps that can be taken to drive up school standards, for example changes in curricula or increased collaboration among professionals.

Our findings are based on a review of existing research and interviews with departmental officials, head teachers, local authority officers and councillors. We were able to develop detailed case studies of the local school quasi-markets in Hackney and Leicestershire but also interviewed senior officers from the DfE and three other local authorities.

We identified a number of ways in which the quasi-market in secondary education is functioning well, but focus our analysis on areas where our research suggested there is potential for improvement, namely:

- lack of competition in some areas
- coasting schools and slow exit
- lack of expansion by high-quality providers
- uneven funding
- gaming
- exit of high-quality providers.

We review the evidence for, and nature of, each of these problems below, before analysing the reasons they exist and have yet to be addressed, and suggesting some areas routes to improvement.

Lack of competition in some areas

> It's just impossible to offer choice on that scale. That's a problem with the market-focused viewpoint. That's fine if you can generate a market, but actually in many parts of rural England, you can't.

<div align="right">

Director from a rural local authority

</div>

A well-known criticism of school choice is that many children do not live close enough to two or more schools to enable choice. In the absence of genuine choice, schools face a guaranteed demand for their services and, because parents cannot choose to send their children elsewhere, do not have any market-based incentives to improve the quality of their provision.

During our research, the rural local authorities repeatedly voiced concerns about the degree of choice available in their areas. Indeed, Burgess et al (2006) found that in London and other urban areas almost all pupils are within reach of a range of schools. However, in rural areas, fewer than 60% would have to travel more than 5km and fewer than 40% would have to travel for more than 8km to reach three schools.

Figure 12: Distance to nearest three schools[183]

% of pupils with…	…three schools within 2km of home	…three schools within 5km of home	…three schools within 8km of home	Median distance actually travelled km
London	77.55%	99.93%	100%	1.65
Other urban	37.28%	91.22%	96.91%	1.53
Rural	9.71%	42.03%	63.81%	2.350

This data gives us valuable evidence about the number schools within a distance that pupils might be willing to travel. Unfortunately, as most oversubscribed schools admit pupils based on geographic proximity, some schools, despite being nearby, may not actually be a realistic option for parents. If the schools are popular then they are likely to fill their intake with pupils living very nearby. 'Catchment areas' are not normally defined by a line on a map, but by the application of a set of rules applied to all applicants, usually including criteria based on proximity.

Harris and Johnston (2007) analyse the geographic boundaries of primary school catchment areas in Birmingham to understand how many schools have catchment areas which overlap with those of other schools, and are therefore subject to competition.[184] They find that 13% of schools in their sample have catchment areas that do not overlap with any other school and that, when they do overlap, they only 'share' a mean of 15% of their pupils with the other school's catchment area. On more stringent assumptions about what constitutes a competitor school (greater than 23% 'share'), the median primary school has no competitors at all and the average number of competitors is less than one. This needs to be interpreted with some caution as the analysis relies on several assumptions and is based on primary rather than secondary schools. Nevertheless it is remarkable that even in a relatively dense urban area like Birmingham, many children appear to face a limited choice of school.

The availability of school transport also plays a big part in determining the level of choice pupils have. Local authorities are obliged to provide free transport for all pupils who attend their nearest school and live more than three miles away from that school. The Education and Inspections Act 2006 extended this right for pupils on free school meals to include all those attending one of their three nearest schools (within six miles.) The House of Commons Transport Committee raised concerns that even this additional level of provision 'does not allow for a choice of schools in rural areas'.[185] Local authorities are permitted to provide additional services if they wish but many of them are making cuts in this area. The Campaign for Better Transport recently used freedom of information requests to collect data from 81 local education authorities outside London and the six big metropolitan areas. These revealed that 72% of these authorities were reviewing or cutting one or more areas of school transport. This suggests that the range of options is probably being reduced.[186]

Lastly, school mergers can have a big effect on the availability of choice. The School Governance (Constitution) (England) Regulations 2007 gave schools the freedom to join together in a federation. This involves merging their governing bodies into a single entity and, if they wish, also creating a single head teacher for the federation. Schools are allowed to do this as long as both the governing bodies agree to do so. Federation can often be a powerful tool for school improvement – they have been transformative in Hackney – but the lack of formal checks on how this effects the competitive environment means they can also lead to significant reductions in the level of competition. One local authority director explained to us:

> We have got some of our secondary schools forming cartels to control certain areas. In [one town] I have two secondary schools who have written to me this week to say they are forming an alliance… So in effect they will be creating a monopoly in [that town.] They are coasting schools. They look as if they are OK because they have nice middle class intakes, but actually the value-added is minimal.[187]

[183] Burgess, S., Briggs, A., McConnell, B., and Slater, H., *School Choice in England: Background Facts*, Centre for Market and Public Organisation (CMPO), Working Paper No. 06/159, Bristol University website, September 2006, retrieved 5 June 2013, http://www.bristol.ac.uk/cmpo/publications/papers/2006/wp159.pdf

[184] Harris, R., and Johnston, R., *Primary Schools, Markets and Choice: Studying Polarisation and the Core Catchment Areas of Schools*, 2007, retrieved 7 June 2013, http://link.springer.com/article/10.1007%2Fs12061-008-9002-8

[185] House of Commons Transport Committee, School Travel, Second report of Session 2008-2009, p9

[186] BBC News, 'School transport: many councils "making cuts"', BBC online, 2 December 2011, retrieved 5 June 2013, http://www.bbc.co.uk/news/education-15991254

[187] Institute for Government Interview SCH007

In areas that can support two schools the danger of federation is that this creates a 'cosy' environment in which the pressure for improvement is significantly diluted.

Coasting schools and slow exit

In a well-functioning system of school choice poorly performing schools should not be able to survive unless they improve their performance. Many of our interviewees, however, complained that 'coasting' schools (schools that sustain a poor level of performance, especially when taking into account the quality of their intake) and schools that were 'gently drifting down' (going through a very slow decline) continued to survive. Indeed, a 2011 RSA report found that 50% of schools rated 'satisfactory' by Ofsted (poorly performing, but not outright failing) in the first inspection remained 'satisfactory' at the following inspection. Interestingly, even when schools do leave the satisfactory category nearly five times as many (42%) do so by slipping into the inadequate category rather than by becoming good (8%).[188]

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[188] Francis, B., (2011), *(Un)Satisfactory? Enhancing Life Chances by Improving Satisfactory Schools*, RSA, December 2011, retrieved 6 June 2013, http://www.thersa.org/action-research-centre/learning,-cognition-and-creativity/education/social-justice/satisfactory-schools

Figure 13: Trajectories in Ofsted inspection results[189]

Did the school improve, remain or decline in inspection outcomes between previous and latest inspections?
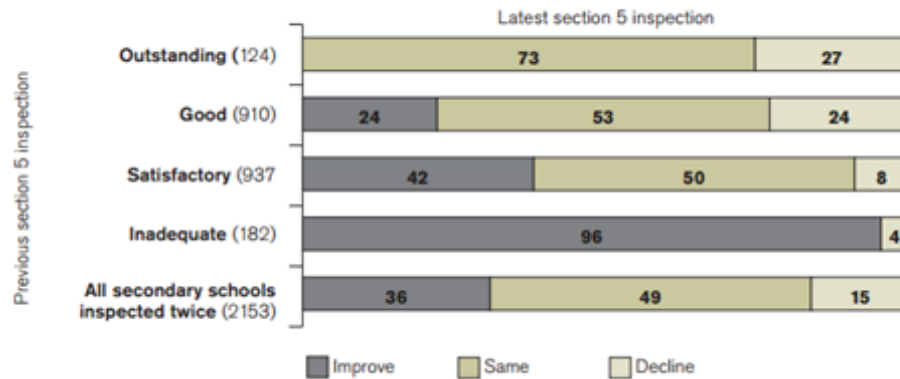
Ofsted points out that 10% of the schools which have been rated as oustanding twice in a row actually have an intake that comes within the top fifth of the most affluent intakes nationally.[190] Michael Wilshaw, the Chief Inspector of Schools, has been particularly outspoken about the need to no longer 'tolerate what is mediocre'.[191]

The local authority officials we spoke to regularly voiced concerns about the effect of coasting schools on achievement of local pupils. We also heard complaints about the slow exit of mismanaged schools. We heard an alarming example of a local authority that has been forced to transfer additional funds on multiple occasions to prop up a school suffering from chronic financial mismanagement.[192] The local authority could see that the school was a failed institution in need of restructuring, but felt obliged to support the school to fulfil its responsibility to provide enough places for children in the area. The officer we interviewed actually expressed relief when the school failed an Ofsted inspection so that they could get on with the necessary process of restructuring and stop committing additional funds to a failed institution.

Lack of expansion of high-quality providers

> I feel it's very much a market in theory and principle but there are severe limitations mainly around capital and funding for new schools and school expansion which are preventing it acting like a real market.

Local authority director

There are two ways that schools can expand: by increasing the size of a school on an individual site, or by expanding onto another site (either by opening a new school or taking over an existing one.) The analysis that follows relates to on-site expansion. We deal with multi-site expansion in a separate section at the end.

Allen and Burgess (2012) review the evidence on the relationship between exam results changes and school expansions between 2002 and 2012 and find that successful schools 'are more likely to have increased capacity over this period but only marginally more so than other schools'.

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[189] Francis, B., (2011), *(Un)Satisfactory? Enhancing Life Chances by Improving Satisfactory Schools*, RSA, December 2011, retrieved 6 June 2013, http://www.thersa.org/action-research-centre/learning,-cognition-and-creativity/education/social-justice/satisfactory-schools

[190] Wilshaw, M., 'HMCI statement to No 10 summit', *Ofsted website*, 2012, retrieved 16 July 2013, http://www.ofsted.gov.uk/news/ofsted-announces-scrapping-of-%E2%80%98satisfactory%E2%80%99-judgement-move-designed-help-improve-education-for-mill?news=18389

[191] Wilshaw, M., 'HMCI statement to No 10 summit', *Ofsted website*, 2012, retrieved 16 July 2013, http://www.ofsted.gov.uk/news/ofsted-announces-scrapping-of-%E2%80%98satisfactory%E2%80%99-judgement-move-designed-help-improve-education-for-mill?news=18389

[192] Institute for Government Interview SCH008

Figure 14: Relationship between school performance relative to other local schools, and school-size changes[193]
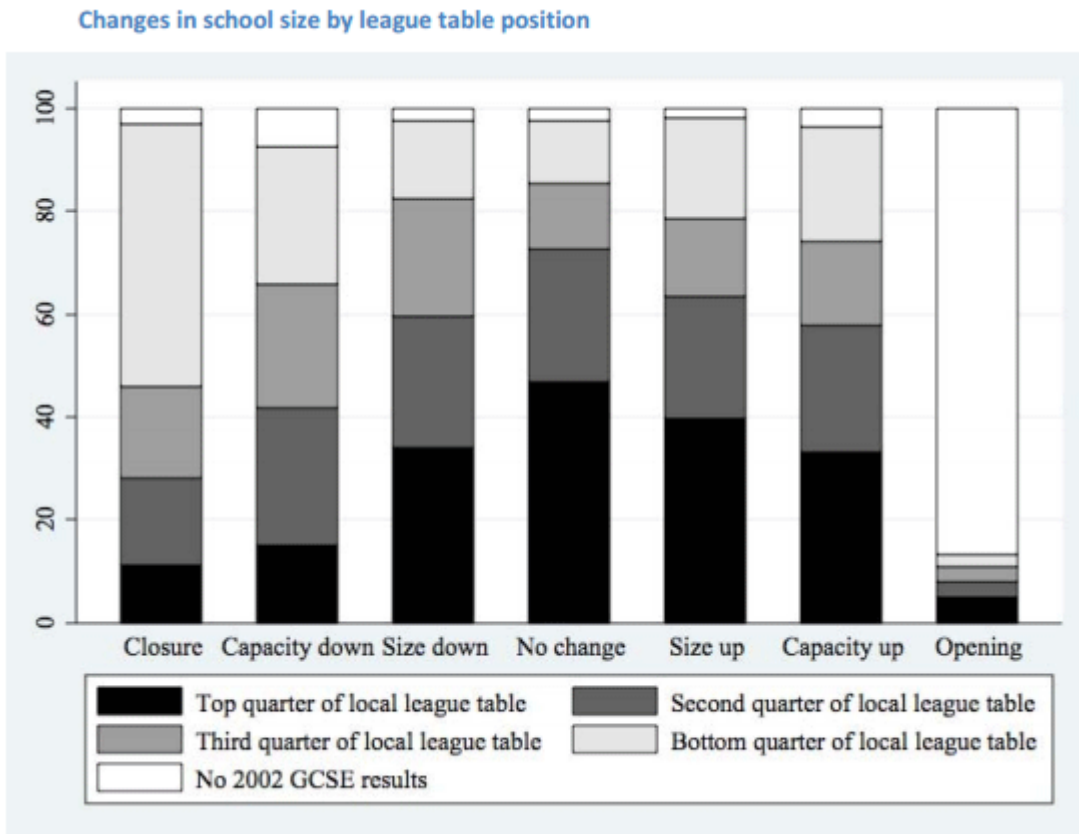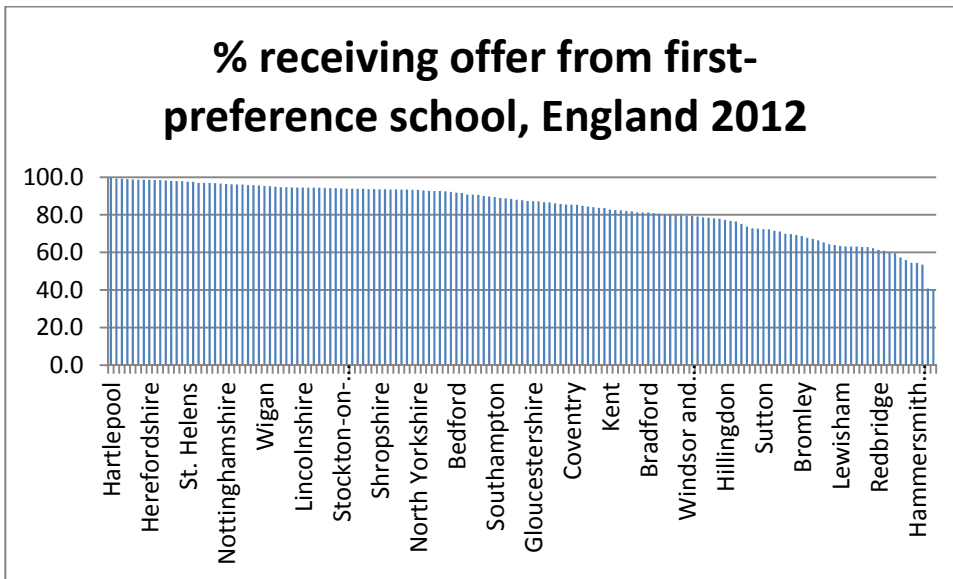

The authors also use regression analysis to determine the causes of schools growth and conclude, 'Overall there is very weak evidence that either relative or absolute exam performance is associated with capacity increases.'

The lack of expansion of good schools explains the low rates of first preference admissions in some local authorities. In a well-functioning quasi-market, however, oversubscribed schools would expand to take on these pupils. Across England 85.3% of pupils received an offer from their first preference school in 2012, but this masks wide variation across local authorities, just over 40% of which have first preference rates below 70%. These are largely urban boroughs, which raises the possibility that the high first-preference rates in rural areas may be the result of a lack of options rather than a more flexible supply side.

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[193] Allen, R., and Burgess, S., *How Can We Encourage Good Schools to Expand?* Centre for Understanding Behaviour Change, 2012.

Figure 15: Proportion of pupils receiving offer from first preference school, UK local authorities[194]

% receiving offer from first-preference school, England 2012

(Bar chart showing percentage of pupils receiving an offer from their first-preference school across English local authorities in descending order, from Hartlepool at nearly 100% down to Hammersmith at around 50%. Y-axis ranges from 0.0 to 100.0 in increments of 20.0. X-axis labels include: Hartlepool, Herefordshire, St. Helens, Nottinghamshire, Wigan, Lincolnshire, Stockton-on-..., Shropshire, North Yorkshire, Bedford, Southampton, Gloucestershire, Coventry, Kent, Bradford, Windsor and..., Hillingdon, Sutton, Bromley, Lewisham, Redbridge, Hammersmith...)

There are five key reasons why schools may be unwilling or unable to expand.

- **Physical space constraints**: This is a serious issue in inner London where high land prices combined with high population density mean that there is very little spare land on which to extend existing schools or open new ones. In Hackney, free schools are failing to find even very basic premises in which to open.

- **Capital constraints**: The Labour government spent a significant amount of money on school capital. The Successful and Popular Schools Initiative was introduced in 2005 to fund the expansion of oversubscribed schools, though the local authority remained in control of the maximum number of pupils any school was allowed to admit. In 2007 the Standards and Development Fund was introduced with the expressed intention of expanding choice for parents through the expansion of popular schools. Due to a number of factors – including fiscal pressures and an increase in the number of primary places required – the capital funding available for the expansion of popular secondary schools has now been sharply reduced. One of the local authorities we looked at has a policy of only funding capital expansion to satisfy excess demand located inside a schools catchment area.

- **Concerns about post-expansion school performance**: Allen and Burgess also analyse the characteristics of pupils in the area surrounding popular schools to assess how expanding their intake (admitting pupils living further from the school) would affect the composition of their intake. They find that in around half of these schools the pupils living in the area that would fall within the expanded school catchment have a lower prior attainment than the closest 50% of their pupils.[195] Given that league tables often foreground raw attainment scores, and these are influenced to a significant extent by prior attainment, this may act as a serious disincentive for these schools to expand.

- **Head teachers' aims**: There was consensus among those we interviewed that the vast majority of heads simply do not think in terms of expansion. One director from a local authority told us, 'I've got head teachers who would love to grow their school, but by far and away the majority are not in that mould… I've also got head teachers who say they are not interested in getting bigger. Their ambition is to run what they have got, well. There is an assumption I suspect in the whole programme that head teachers will want to get bigger and bigger and their salary will go up. I don't find that attitude in many heads...' This reluctance

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[194] Institute for Government analysis of DfE data

[195] P22

to expand may be because heads of larger schools do not have materially larger salaries than those in smaller schools.[196]

- **Impact on budgets**: The current funding arrangements are highly complex and schools may be reluctant to expand because they are unsure exactly how this will affect their financial situation. Funding arrangements are in the process of being reformed and we look at this in more detail in section [4.3.4].

Multi-site expansion

The graph below suggests that 'multi-site' school expansion – where a school or academy chain takes over another school – has been much more prevalent than schools expanding on site. This was a major component of the academies policy and has clearly added a significant amount of extra supply-side flexibility.

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[196] Allen, R., and Burgess, S., *How Can We Encourage Good Schools to Expand?* Centre for Understanding Behaviour Change, 2012.

Figure 16: Growth of academy chains[197]

Growth of the nine largest sponsored academy chains over time
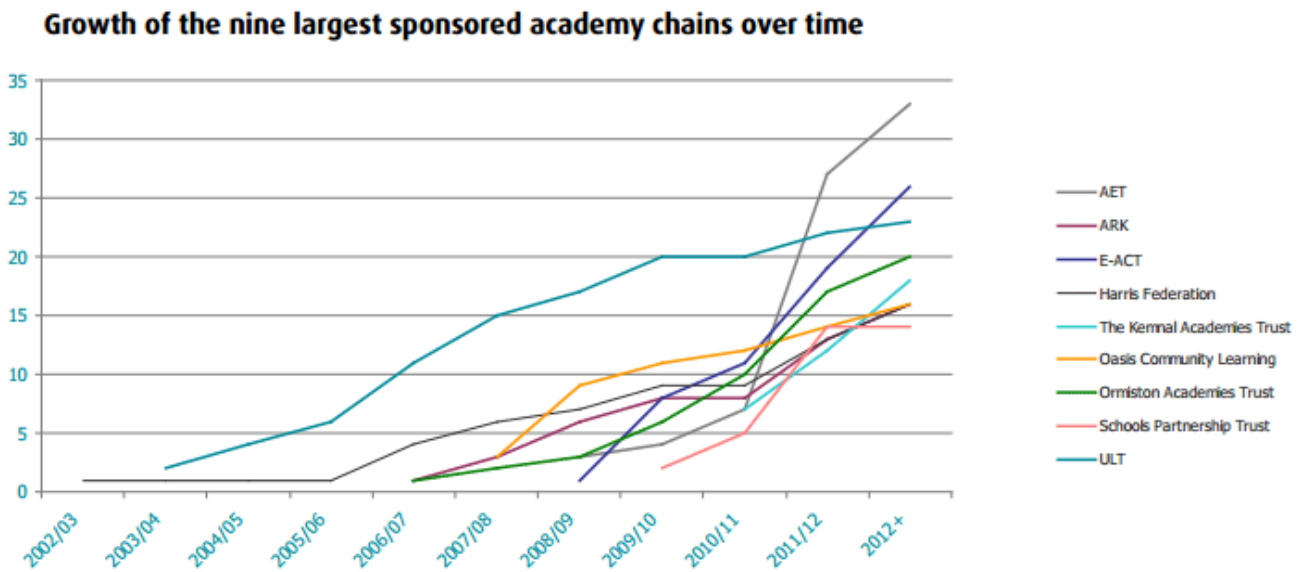
Unfortunately data on the performance of whole-academy chains is hard to come by so it is hard to assess whether or not it is the best chains which are expanding, and whether or not they outperform the predecessor school. Some have raised concerns about the performance of certain (large) academy chains based on the Ofsted ratings of the schools they run.[198] Several of our interviewees also raised doubts about particular instances in which they believed a sponsor with an inferior academic record had been appointed to take over a failing school. This might because there is currently no rigorous data set available to help governing bodies make these decisions, although the DfE does provide some advice.

Uneven funding

In a well-functioning system of school choice, schools should receive a level of funding that is proportionate to the cost of providing education, largely based on the number of pupils. If schools receive a disproportionately large amount of funding then they could remain less effective at increasing pupil attainment, while still staying ahead of other schools in the rankings and attracting more pupils. This would be an inefficient allocation of pupils across schools. If schools receive a disproportionately small amount of funding then they could struggle to compete and attract students even if they were in fact better than their competitors. In the absence of a level 'funding' playing field the quasi-market will be distorted.

Academies are funded by the Education Funding Agency based on the amount they would have received had they remained under the control of the local authority in which they are located. Local-authority-maintained schools are/were in turn funded by local authorities in line with local spending priorities and funding criteria based on a list of up to 37 allowable variables. This varied significantly across different local authorities meaning that neighbouring schools/academies sitting either side of a local authority border, but with overlapping catchment areas, can have significantly different levels of per pupil funding. One head teacher described such a situation to us 'You only need to go across the border into [name of town removed], so the same areas that over a third of our kids come from… they have about 700 students (and no sixth form) we have 1,300 students and their budget is almost identical to mine.' Many of the variables are unrelated to the number of pupils attending the school.

We would expect spending to vary by the number of Free School Meal (FSM) pupils due to the pupil premium but other than that a level playing field would require schools to receive a similar amount of funding. The Abbreviated

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[197] Hill, R., Dunford, J., Parish, N., Rea, S., and Sandals, L., *The Growth of Academy Chains: Implications for Leaders and Leadership*, National College for School Leadership, the Governor website, 2012, retrieved 7 June 2013, http://www.thegovernor.org.uk/freedownloads/acadamies/the-growth-of-academy-chains.pdf

[198] Hurst, G, and Knowles, T, 'Academies growing too fast, say experts', *The Times*, 7 January 2013, retrieved 8 June 2013, http://www.thetimes.co.uk/tto/education/article3649591.ece

Account Returns contain data on revenue spending per pupil for non-federated[199] academies and the proportion of pupils who qualify for free school meals. We have removed London schools (on the grounds that London schools receive additional funds to account for higher costs) and there are not enough data-points within London to provide useful visual comparison. We have also removed KS3-KS4 only schools because there are not enough data points. Figure 17 therefore shows KS3-KS5 non-federated academies outside London.

The graph shows wide variations in per-pupil spend among schools with similar proportions of FSM pupils, all along the distribution. The important point here is the vertical spread for schools with similar proportions of FSM pupils. Schools with around 30% of FSM pupils, for example, are evenly spread between spending just over £6,000 per pupil right up to just over £10,000 per pupil. Some of this is likely to be explained by variations in the number of children with Special Education Needs (SEN), but since they make up less than 2% of all secondary academy pupils it seems unlikely that they could fully account for the spread that is observed right along the distribution.[200] This suggests, though does not prove, that school funding does not follow pupils or reflect the cost of provision. In their consultation on reforming the funding system the DfE have themselves admitted that this system allows 'different schools in an area with similar types of pupils [to] receive significantly different levels of funding'.[201] This is largely a result of historical factors and the build of different funding arrangements and initiatives in different local authorities.

Figure 17: Per-pupil spending against proportion of FSM pupils[202]
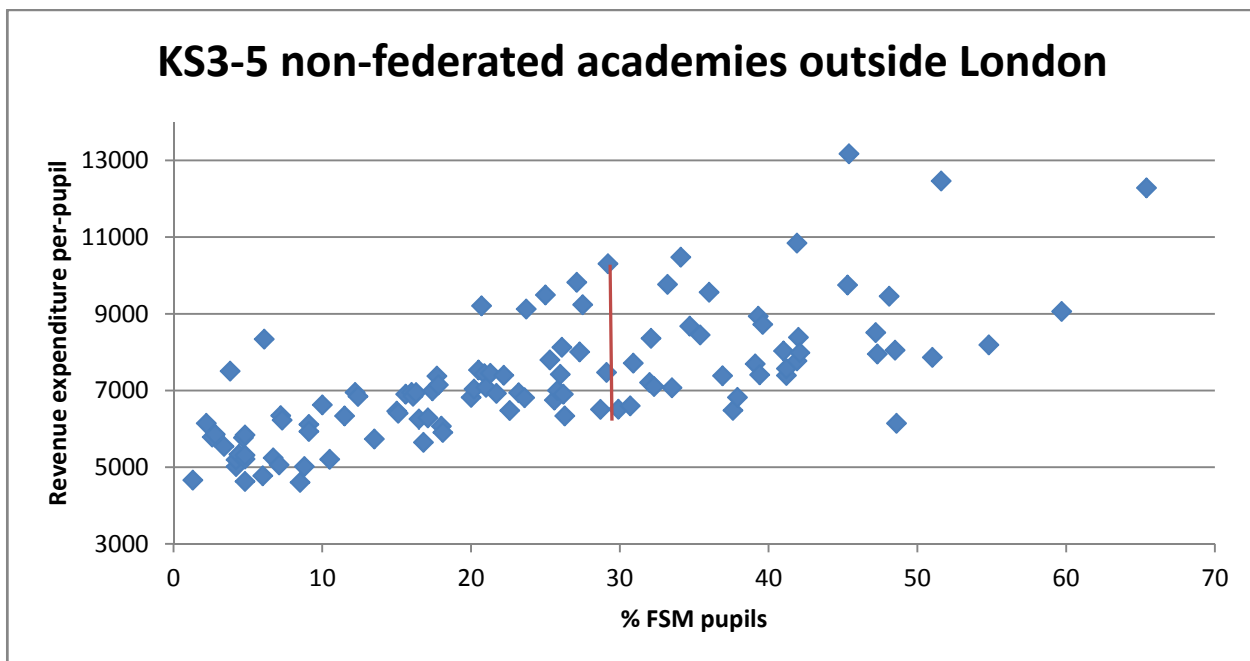
The DfE is preparing to simplify school funding by cutting down the number of criteria on which local authorities can base their funding from 37 to just 12. The aim is to increase the proportion of funding that follows pupils and make it 'more responsive to pupil numbers and parental demand'.[203] For now however, the Department seems to have backed away from a uniform national funding formula, meaning that the funding that academies receive will ultimately continue to be based on the (highly-variable) funding decisions made by their (former) local authorities.

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[199] Federated academies only return data for the federation as whole, which is less useful for present purposes.

[200] Department for Education, *Special Educational Needs in England, Statistical First Release,* Table 1D, 2012, retrieved 16 July 2013, http://www.education.gov.uk/rsgateway/DB/SFR/s001075/sfr14-2012.pdf

[201] Department for Education, *School Funding Reform: Next Steps Towards a Fairer System,* Government website, 2012, retrieved 5 June 2013, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/179138/school_funding_reform_-_next_steps_towards_a_fairer_system.pdf

[202] Institute for Government analysis of DfE Abbreviated Accounts Return data 2011

[203] Department for Education, *School Funding Reform: Next Steps Towards a Fairer System,* Government website, 2012, retrieved 5 June 2013, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/179138/school_funding_reform_-_next_steps_towards_a_fairer_system.pdf

Gaming

> Schools that turn themselves around often do it… [by] exploiting tactics to improve exam results in the short term which are not about the experience that every child gets in every lesson.

Head teacher

Gaming occurs when a provider takes actions that improve performance indicators but do not contribute to the achievement of the goal which the performance indicator is attempting to measure. The provider is knowingly taking action that 'hits the target but misses the point'. In the context of secondary education this comes in four main forms.

Cream-skimming

Cream-skimming occurs when a service provider chooses the easiest-to-provide-for users to boost their performance indicators. Admissions interviews, which could be used to covertly cream-skim pupils were banned in 1998. The recent report of the Academies Commission[204] however, raised concerns that covert cream-skimming practices persist by other methods, including social events for prospective applicants or supplementary information forms including lengthy open questions on which judgements of parental intelligence could potentially be made. There is also anecdotal evidence of schools, using tactics such as very expensive school uniforms or emphasising the expense of costly compulsory school trips to potential applicants.[205]

Parking

Parking occurs when a service provider chooses not to provide a service to a particular user. In schools this can take the form of excluding low-performing pupils from the school. Although the number of permanent exclusions has fallen steadily from 9,590 in 2001/02 to 5,080 in 2010/2011,[206] there are widespread concerns that 'informal' exclusions are on the rise. Informal exclusions include cases in which either pupils are asked to 'jump before they are pushed' to avoid having a formal exclusion on their record, or in which the exclusion is simply not recorded by the school. Although there is a lot of anecdotal evidence for the existence of such practices, up until recently there has been frustratingly little in the way of hard evidence. A recent report from the Children's Commissioner has addressed this by asking a representative sample of 1,000 teachers if they had observed such behaviour. The relevant results are summarised in Figure 18 below.

Figure 18: Proportion of teachers surveyed who have seen the above practices in their school[207]

Has your school ever done any of the following?	Primary	Secondary	All classroom teachers	School leaders
Encouraged some pupils to move to a different school, without recording such a move as a permanent exclusion	6.1%	38.9%	22%	15.8%
Encouraged parents of some children to educate them at home, without recording such a move as a permanent exclusion	0.6%	6%	3.4%	1.8%
Recorded pupils as 'authorised absent' or 'educated elsewhere' when the school has encouraged them not to come into school	1.9%	10.9%	6.3%	2.1%
Sent pupils home for any period without recording it as a fixed term-exclusion	6.7%	8.1%	7.3%	6.7%

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[204] Academies Commission (2013), Unleashing Greatness, RSA Ch4

[205] Children's Commissioner (2013) Always Someone Else's Problem: report on illegal exclusions, available at: http://www.childrenscommissioner.gov.uk/content/publications/content_654

[206] Table 1 http://www.education.gov.uk/rsgateway/DB/SFR/s001016/sfr17-2011.pdf

[207] Adapted from Table 1 of Children's Commissioner (2013) Always Someone Else's Problem: report on illegal exclusions, available at: http://www.childrenscommissioner.gov.uk/content/publications/content_654

To put these numbers in context the report emphasises that this is equivalent to an average of:

- 10 schools in every local-authority area having sent children home for disciplinary reasons without recording it as an exclusion
- just over three schools in every local authority having recorded pupils as authorised absent or educated elsewhere when the school has in fact encouraged them not to come into school
- one school in every local authority has encouraged parents to take their children out of school and educate them at home without recording it as an exclusion.

As well as parking by taking pupils out of the school, schools can park on entry. Because local authorities cannot order an academy to admit a pupil that has been permanently excluded from another school (whereas they can for a non-academy school) there is potential for academies to improve performance metrics by refusing to admit hard-to-teach pupils.[208]

Crowding towards the target

> One of the key stage 4 gaming behaviours is one-to-one tuition around the C/D borderline. You find me a school in a challenging situation that isn't doing that.

Head teacher

Because the number of children who get 5 grades between A* and C remains the most common metric for school performance there are strong incentives for schools to dedicate disproportionate resources to pushing students over the C/D borderline. This is known as crowding towards the target. Wilson et al (2006) interviewed 21 head teachers and 10 of the interviewees openly discussed the way in which they were targeting resources at this borderline.[209] Burgess et al (2005) add quantitative evidence to this, finding that low-ability pupils suffer as a result of this, particularly in schools with lots of pupils near the C/D borderline and particularly in schools that had a competitor school nearby.[210] If schools engage in this practice to a differing amount then the performance measures, and the choices based on them, will be distorted.

Equivalent qualifications

There are also widespread criticisms that some schools have switched to non-GCSE qualifications which are counted as equivalent to the GCSEs, as an easier route to achieving the supposed equivalent of five A*-C grades. It is hard to find any definitive evidence on this. Jin, Muriel and Sibieta (2011) present evidence showing both that the worst-performing schools adopted vocational qualifications most comprehensively and that the schools which most aggressively adopted vocational qualifications saw the biggest increases in performance as measured by 5A*-C.[211] This does not prove that these qualifications are easier than the traditional GCSE 'equivalents' or that gaming has occurred, but is certainly suggestive. The DfE is planning to reform and restrict the list of equivalent qualifications to reduce this potential loop hole.[212]

Exit of high-quality providers

In Leicestershire the vast majority of secondary schools have recently become academies. The county has historically operated with a system of middle and upper schools (covering 11-13 and 14-17 age ranges, respectively) and 83% of their schools are currently rated good or outstanding by Ofsted. Upon academisation, some of the schools decided to make use of their new freedoms to change their age range to the standard 11-16 or 11-18 range. Where middle schools have taken this route, upper schools have been forced to do likewise because they are losing their feeder middle schools. The result of this is that the proportion of surplus school places has dramatically increased, from 10% of secondary age pupils in 2009 to 25% in 2013 (see figure 19.) This has created a significant injection of competitive pressure as the number of excess places has increased sharply

[208] Academies Commission (2013), Unleashing Greatness, RSA Ch4

[209] Wilson, D., Croxson, S., Atkinson, A., 2006 '"What gets measured gets done": Headteachers' responses to the English secondary school performance management system. *Policy Studies*, vol. 27, no 2, 2006

[210] Burgess, S, Propper, C, Slater, H and Wilson, D, *Who Wins and Who Loses from School Accountability? The Distribution of Educational Gains in English Secondary Schools*, CMPO Working Paper No. 05/128, Bristol University website, 2005, retrieved 5 June 2013, http://www.bristol.ac.uk/cmpo/publications/papers/2005/abstract128.html

[211] Jin, W., Muriel, A. and Sibieta, L. (2011) 'Subject and course choices in england: insights from behavioural economics', Centre for Understanding Behaviour Change, Research Paper, Department for Education, London.

[212] DfE (2103) Secondary School Accountability Consultation

and schools are under pressure to attract candidates. One of the head teachers that we interviewed in Leicestershire referred to this as the 'bleeding edge' of competitive pressure.

Figure 19: Surplus school places in Leicestershire data[213]
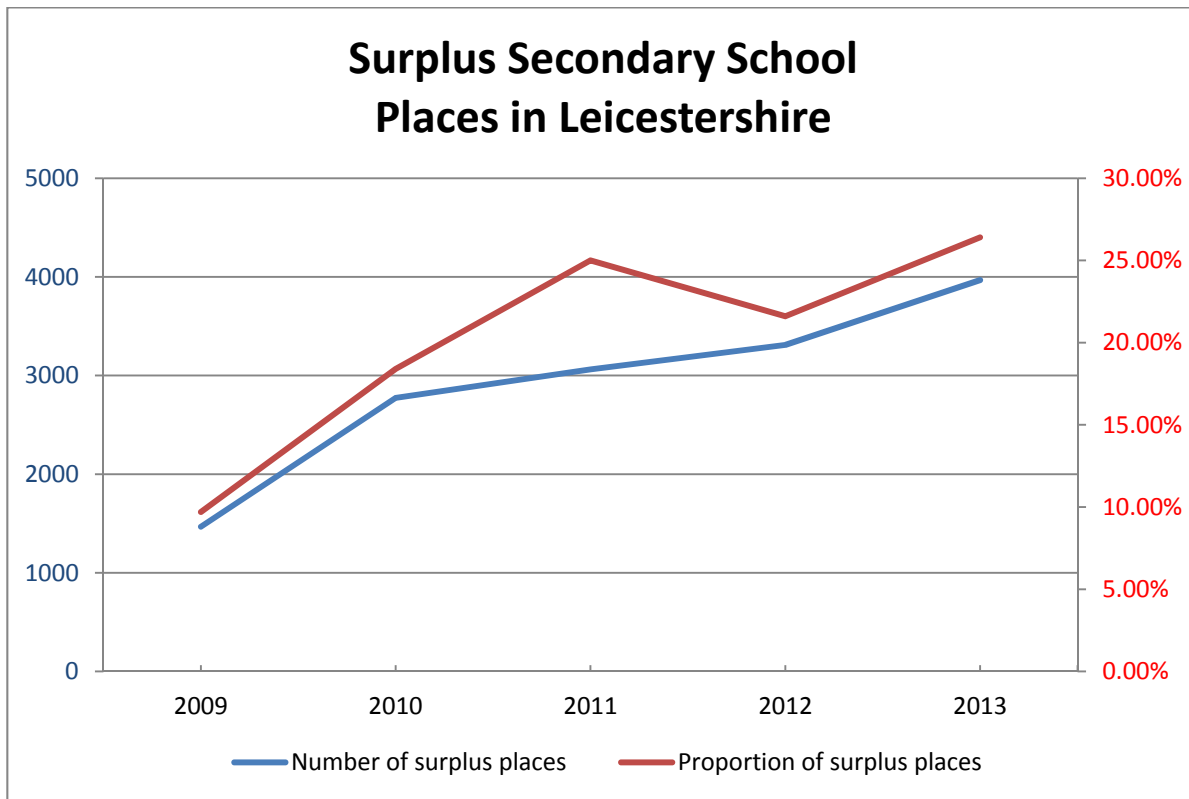
Unfortunately, there are several reasons why this development might lead to the closure of better performing, rather than worse performing, schools. The upper schools are in a difficult position because they cannot rely on pupils staying on after age 14 in the same way that middle schools can (due to loyalty or status quo bias.) They also do not have the established links with primary schools that have for a long time acted as feeder schools for the middle schools. In time, if some schools contract below sustainable capacity, this could lead to the closure of (ex-upper) schools which may be superior to the local (ex-middle). If these schools have sixth forms attached then this may also create large areas with no (high-quality) 16-18 provision. Leicestershire County Council is working with the schools to address this situation in the interest of local pupils.

Although this phenomenon is particular to the middle/upper school system in Leicestershire (only four or five other authorities operate similar systems), it is a fascinating case study of the way that competition on an uneven playing field can lead to a decline in average quality. It is also of general interest in relation to government's ability to think through how policies will play out in a market system, once the different provider organisations begin reacting strategically to them.

Explaining the strengths and weaknesses

Many of the problems we have identified will be familiar to those involved in education policy. We traced the causes of each of these five problems back to either the inherent characteristics of the service or to underlying institutional features relating to the way in which the quasi-market for secondary education is organised. Once we had repeated this process for all of the market weaknesses we were left with a rich explanatory map. In many cases, the underlying institutional factors helped explain why these weaknesses have persisted and which institutional changes need to be made to help government better steward the market.

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[213] Institute for Government analysis of data supplied by Leicestershire County Council

Lack of competition in some areas

Thinking about the nature of secondary education, the lack of competition in some areas is explained by the economies of scale of delivering secondary education. Because you need year groups of a certain size to deliver a broad curriculum at reasonable costs, secondary schools need to be a particular size. This interacts with the population density of an area to determine how many schools will be within travelling distance of a given student's home. At institutional level, the fact that there is no competition regulator or regulatory regime of any sort, means that local schooling quasi-markets can become over-concentrated. In the absence of a body to set and enforce rules about when a federation/merger is, and is not, acceptable there is always the danger of competition being diluted or even eliminated in this way.

This is partly a product of the way the Academies Programme has developed and DfE's approach to implementation.[214] The focus has been heavily on encouraging and enabling schools to convert to academy status and facilitating the entry and expansion of chains and federations. This short-term focus has sometimes come at the expense of thinking through potential unintended consequences of actions, for example, allowing academies to federate to the extent that they create local monopolies. When reform occurs at this pace planning and delivery occur simultaneously – a fact that also limits the ability of the department to adjust its internal structures, processes and personnel to ensure that they are capable of implementing the programme effectively.

Coasting schools and slow exit

The inherent characteristics of secondary education help explain the presence of coasting schools. Because it is hard to measure causal effects of schools on pupil attainment, coasting schools can often appear to be doing fairly well on their raw GCSE scores, but actually add little value. This means that parents considering raw scores may not identify the best school for their child and commissioners cannot appoint a new sponsor for a school because it hasn't been measured as falling below the floor standard. As a result, both 'user-chooses' and 'commissioner-chooses' systems of choice become less powerful. In addition to the issue of measurement, the presence of high switching costs means that parents will face an added obstacle to moving their child once they have had some direct experience of the quality of education on offer. This 'locks in' the initial choice, meaning parents are unlikely to switch even as they acquire more information on quality.

This is exacerbated at institutional level because coasting academies are protected from intervention, unless they fail an Ofsted inspection or fall below the floor target (currently 40% 5A*-C including English and maths, rising to 50% in 2015.) Because the floor target is currently expressed in raw scores however, badly-performing schools with a high-quality intake are often not picked up by it. Because they are autonomous, local authorities cannot force them to join collaborative networks, co-operate with teaching schools, or join a chain. As a result, these schools can simply continue to coast.

Second, academy funding arrangements are agreed between the Education Funding Agency and individual academies for a period of seven years. This period defines the length of time for which an academy (which does not fail an Ofsted or fall below the floor target) has free reign. A recent study on charter schools in the USA by Raymond et al (2008) found that, for most charter schools, the success or failure of a school can be predicted by its performance after three years.[215] In the words of Margaret Raymond, the author of the report, 'If you start wobbly, chances are you'll stay wobbly.' This suggests that a seven-year-long 'contract' may be too long.

The government is consulting on new minimum performance standards (floor standards) for schools.[216] The new standards will be likely to include the existing floor standard (minimum proportion of students achieving 5A*-C GCSEs including English and Maths) but may also include a progress floor standard, which stipulates the minimum acceptable level of progress (see Annex 2 for a definition of this measure). The explicit rationale for this is that 'coasting schools… will be exposed as underperforming by this type of measure'.[217] For more details see Annex 1 for a diagrammatic representation of how the proposed floor standard would work.

We would expect this to reduce the number of bad schools who are not caught by the floor standard because many of the coasting schools would fail on the value-added standard. It is unlikely to catch all of them however,

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[214] Institute for Government Interview SCH016

[215] Raymond, M., et al, *Charter School Growth and Replication Study*, Stanford University website, January 2013, retrieved 8 June 2013, http://credo.stanford.edu/pdfs/CGAR%20Growth%20Executive%20Summary.pdf

[216] Department for Education, Secondary School Accountability Consultation, Government website, 2013, retrieved 5 June 2013, https://www.gov.uk/government/consultations/secondary-school-accountability-consultation

[217] Ibid. Para 5.12

because it remains an inaccurate measurement of the causal effect of the school. In particular, it fails to account for any contextual factors such as parental wealth or levels of education. The downside of the proposed double-floor standard is that there may also be additional non-bad schools that fall foul of the floor standard and therefore shut down. For more details see the diagram in Annex 1.

The limitation under which the government's proposed reform is straining is that it has to be based on hard data. This is partly mitigated by Ofsted inspections but these inspections are themselves based partly on the very same performance metrics and only occur periodically.[218] Prior to the existence of academies, a local authority could monitor the performance of a school and come to a judgement about whether its performance was unacceptable, given the intake. Academies were introduced partly because many local authorities failed to do this effectively. But if some local authorities were willingly blind to the poor quality of schooling in their area then central government is also part blind – because the statistics that they rely on are not accurate measures of the causal effect of schools.

The most effective local authorities that we studied, even where they had a highly academised system, retained a massive amount of soft knowledge[219] about the schools in their area, including the capacity of leadership teams and the direction of travel of the school, even between exam-result releases. The DfE now employ a network of regionally-focused 'sponsor development advisers' but the extent to which they can fulfil this role is unclear. There may therefore be a case for giving local authorities the right to declare a school as failed (being in need of a new sponsor), even if it has not yet fallen below the floor standard or failed an Ofsted inspection. If local authorities neglect to use this right in the face of poorly-performing schools then nothing will have been lost compared with the current system. If they do use it then they could help turn around failing schools more quickly.

Lack of expansion of high-quality providers

Lack of onsite expansion is partly explained at service-characteristics level by the fact that it is hard to measure the causal impact of schools on pupil attainment. Because of this – and the fact that many schools face declining 'quality' of intake as they extend their catchment areas outwards – schools will be reluctant to expand for fear of their raw score performance indicators declining as a result. In relation to multi-site expansion, difficulties in measuring the causal impact of schools on pupil attainment makes it hard to take a rational approach to awarding sponsorship rights to the best sponsor.

At institutional level, it seems problematic that school governing bodies have responsibility for appointing a new sponsor because they are implicated in the failure of the school, and are therefore unlikely to have an objective analysis of the type of change required or the best sponsor. In addition, it is questionable whether the governing body of a school, which has just overseen the failure of that school, has the capacity to decide who runs it next.

In reality the DfE takes an interest in advising on sponsors and the school governing body cannot unilaterally choose a sponsor. However, several of our interviewees said they had observed appointment processes in which governing bodies appeared to be selecting a sponsor that posed less of a threat to current ways of working in the school, despite apparently having a less impressive academic record. We also heard complaints that schools often prefer to be sponsored by a local school despite the fact that it may be inferior to a more distant alternative or may not have the capacity to sustain its own performance while sponsoring the failed school. The Academies Commission have studied this issue in some detail and recommend that the DfE should make the process of appointing sponsors 'open, fair and rigorous, and supported by clear criteria'.[220]

The evidence suggests that multi-site expansion, usually through federation, is the most realistic way of getting good schools to expand. This gets round problems of space and capital constraints, and the risks of decline in measured performance for schools which face a lower attaining intake just outside their current catchment area. Multi-site expansion also avoids some of the problems of balancing teacher/pupil ratios when one school expands and another contracts by a whole form of entry. The commissioner-chooses mechanism may therefore be the most potent force for expanding high-quality provision, rather than user choice. Bearing this in mind, it is particularly important that the process for appointing sponsors to take over failing schools can accurately identify and appoint the most effective sponsoring organisations.

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[218] Ofsted, *School Inspection Framework*, p16-19, 2012.

[219] Peterson, A., (2004) *Information: Hard and Soft*, University of Sienna website, July 2004, retrieved 8 June 2013, http://www.disas.unisi.it/mat_did/gabbi/729/10.1.1.126.8246[1].pdf

[220] Gilbert, C., Husbands, C., Wigdortz, B., and Francis, B., *Unleashing Greatness: Getting the Best from an Academised System,* p. 12, Academies Commission, 2013.

Uneven funding

The DfE has shied away from introducing a uniform national funding formula for schools. Indeed the Department has decided not to even enforce a minimum threshold for the proportion of funding that is channelled through pupil-led factors. Instead the DfE has delayed action until the next spending review period. Some of our interviewees suggested that this might simply be due to the political costs of implementing larger funding reductions in some areas than others.

Gaming

The existence of gaming is explained by the imperfect performance metrics on which school accountability is based. Bevan and Hood (2006) analyse the use of performance metrics in a target-driven system.[221] An adapted version of their framework is used here to shed light on school performance metrics and gaming. Bevan and Hood point out that using performance metrics to manage public services assumes that you can measure the performance which you wish to see.

The causal effect of a school is hard to measure, which opens the door to gaming because providers can take action that is not in itself desirable but which allows them to increase their measured performance. First, they can reduce the effort they put into activities for which there are no measures, even when the activity is desirable, to focus on things that are measured – for example by switching teaching resources away from those who have little chance of securing a C to those who are near the C/D borderline. Second, they can engage in behaviour that boosts their performance on the imperfect measures but is not really related to good schooling (e.g. entering pupils for easier-to-pass qualifications, which are less valuable for entering further education or employment). Third they can engage in activity which, though it boosts their performance on imperfect measures, is totally unrelated to good schooling and may even be detrimental (e.g. informal exclusions).

In summary, the flaws in the performance measures create opportunities for gaming. Engaging in this sort of behaviour is particularly tempting for schools which face serious competition from competitors, or risk falling below the floor target and being decommissioned.

The government is currently consulting on new performance measures for the school accountability framework to tackle problems associated with crowding towards the target and equivalent qualifications. The list of qualifications which count as equivalent to GCSEs for the purpose of league tables has been restricted. The 5A*-C measure is also set to be replaced by the 'average point score' measure. This gives an average score across eight subjects including five 'EBACC' subjects (sciences, computer science, geography, history and languages) and three others from the approved list. A summary of the proposed metrics for the new school accountability framework is given in Annex 2.

These changes are generally to be welcomed and should eliminate most of the problems with crowding towards the target. It remains unclear however, whether the DfE will stop publishing 5A*-C. If they do not then it is likely that this will remain the focal-point indicator reported on independent websites and in local newspapers. Given that there is a clear track record for performance measures creating unintended gaming behaviour, the government should also consider funding research to track the way in which schools respond to the introduction of new performance measures, or a mechanism by which whistle blowers can report gaming behaviour.

Three of the Academies Commission recommendations relating to admissions appear to be sensible ways to ensure that competition takes place on a level playing field, without cream-skimming and parking. They argue:

- the secretary of state should identify an organisation that is well-placed to provide an independent appeals service to be instigated and run in a quasi-judicial manner
- the Local Government Ombudsman's powers should be extended to hear complaints concerning the maladministration of admissions and admissions appeals of all admissions authorities (whether from maintained schools or academies)
- parity should be established between maintained schools and academies in the mechanisms for dealing with complaints about admissions arrangements and the operation of local authority directions. The Chief Schools Adjudicator should consider and determine all appeals against directions, and complaints against variations and derogations from the School Admissions Code.

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[221] Bevan, G., and Hood, C., 'What's measured is what matters: targets and gaming in the English public health care system', *Public Administration*, Vol. 84, No. 3, pp. 517-538, 2006.

Areas for focus

Clarity on the role of choice and competition in improving standards

It has never been entirely clear whether, how, and to what extent, governments have expected choice and competition to increase standards in schools. Ministerial rhetoric has sometimes emphasised the inherent value of giving parents a choice, meaning that the instrumental value of using it to increase standards may at times have been of secondary importance.[222] Governments have also wavered between prioritising user choice and commissioner choice. It is also unclear to what extent governments have been trying to create a full quasi-market, as opposed to using competition simply to inject some degree of competitive pressure at the margins of the system. The gradual and piecemeal way in which quasi-market reforms have been introduced over a long period suggests it may not be the former.[223] However, recent changes suggest a shift to the latter.

The lack of a competition regulator, combined with the permissive approach to federation of schools, has clearly led to competitive pressure being significantly diluted in certain areas, with the possibility of this occurring elsewhere. If the Department is genuinely committed to the idea that diversity and choice increase standards then it should be more active in intervening in such cases. This should be done on a case-by-case basis where it believes the loss of competition outweighs the benefits of the proposed federation.

Information on sponsor performance

The Department for Education has now started to maintain a detailed database on the financial health, academic record, governance model and staffing capacity of different sponsor chains, but none of it is currently publicly available. Releasing this information would allow governing bodies to make a more informed choice and force them to justify their decisions against this evidence. Publishing this data would provide greater transparency in this important area of public interest. Publication would, however, need to be carefully considered – as parents may apply extreme pressure on schools to adopt sponsors who top any rating system, potentially to the detriment of market development and competition.

Role of the local authority

If school floor standards (which determine when a new sponsor will be commissioned) are administered centrally, then they will to a large extent have to be based on hard exam performance information. This potentially misses out on a lot of other useful information held by local authorities, who often know that a school is failing or in the process of failing, long before central government picks this up through exam results or a failed Ofsted inspection. DfE currently has regionally-based employees who operate on a somewhat devolved basis and consult with local authority officials. However, our research revealed complaints from local authorities that their concerns were rarely prioritised due to the need for DfE officials to concentrate on the few highest-profile difficulties (partly due to resource constraints). Decommissioning powers (declaring a school as failed) may therefore be better off extended to local as well as central government. This would fit nicely with the role that the government has assigned local authorities as being 'champions' for local pupils and would put local authorities in a more authoritative position when holding schools to account for their performance.

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[222] Exley, S., *Are Quasi-Markets in Education what the British Public Wants?* Paper prepared for the SPA conference 2012, retrieved 16 July 2013, http://www.social-policy.org.uk/lincoln2012/Exley%20P6.pdf

[223] Sims, S., *The Development of Quasi-Markets in Secondary Education*, Institute for Government website, November 2012, retrieved 8 June 2013, http://www.instituteforgovernment.org.uk/publications/development-quasi-markets-secondary-education

Annex 1

School performance cannot be perfectly measured because the floor standard cannot be specified in a way that catches all the bad schools (defined as those whose causal impact on the attainment of pupils is low). Figure 20 illustrates this. The area inside the blue line represents all the genuinely bad schools. However these do not all fall within the red area that represents failure on the floor standard. It is worth noting that the floor standard may also catch some non-bad schools represented by the area in the red rectangle but not inside the blue line.

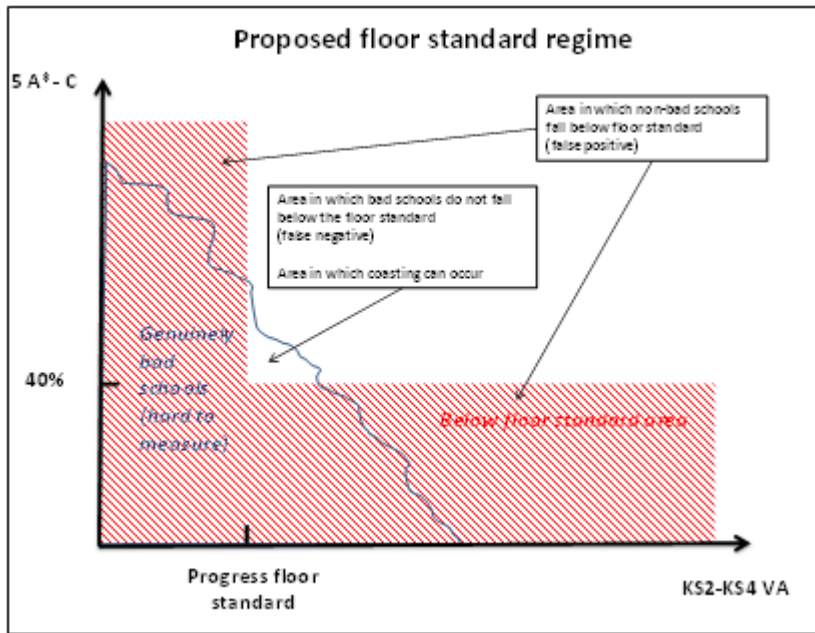*Figure 20: The current floor standard regime*[224]
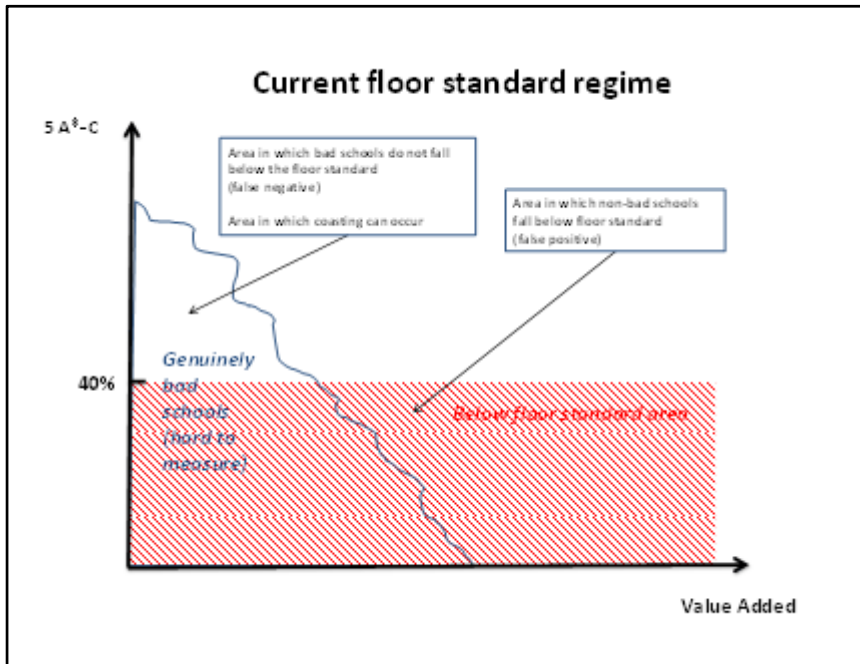
The genuinely bad-schools area appears where it does because bad schools will be more likely to have (correlated with) low '5A*-C' scores and a low 'KS2-KS4 VA' score. The line is drawn as wobbly to signify that it is a fuzzy boundary.

The new floor standard would also include a value added measure. This is shown in the figure 21 below:

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[224] Institute for Government analysis

Figure 21: Proposed floor standard regime[225]

Proposed floor standard regime

- 5 A* - C
- Area in which non-bad schools fall below floor standard (false positive)
- Area in which bad schools do not fall below the floor standard (false negative)
- Area in which coasting can occur
- Genuinely bad schools (hard to measure)
- 40%
- Below floor standard area
- Progress floor standard
- KS2-KS4 VA

[225] Institute for Government analysis

Annex 2: Complete set of DfE's proposed school accountability metrics[226]

	League tables (accountability to parents)	Minimum/floor standards (accountability to government)

Attainment	(A) Average point score
	
	(B) Extra-curricular awards
	
	(C) EBACC
		(D) % 'Good' English + Maths
		
		   - for pupil premium kids
		
		   - for non-pupil premium kids
		
		   - the gap between them

Progress	(E) KS2-KS4 progress
	
	(F) Maths progress KS2-KS4
	
	   - high prior attainment
	
	   - medium prior attainment
	
	   - low prior attainment
	
	(G) English progress KS2-KS4
	
	   - high prior attainment
	
	   - medium prior attainment
	
	   - low prior attainment
		(E) KS2-KS4 progress
		
		   - for pupil premium kids
		
		   - for non-pupil premium kids
		
		   - the gap between them

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[226] Collated from DfE (2013) Secondary School Accountability Consultation

Care for older people

Summary

The market in care for older people is well established and the foundations of the current system date back to the NHS and Community Care Act 1990. Central government sets the policy framework for social care and part-funds its delivery. Local authorities each set their own eligibility criteria and commission services or distribute personal budgets. Alongside publicly-funded provision, there is a large and growing privately-funded care sector (accounting for around 50% of provision) and a large amount of care provided by families and other support networks. State funding for care is increasingly passed to users (or their carers) in the form of direct (cash) or virtual budgets, which they then choose how to spend. But in other cases, local commissioners offer an often-narrow menu of options to users, usually purchasing these services in bulk from providers (private, voluntary or public) to secure discounts and increase the overall amount of care provided to the local population.

Certain characteristics of social care present particular challenges for delivering it through a market mechanism. It is hard to measure the value added (how much quality of life is improved by being in care) by particular care providers. Purchasing decisions are also often made quickly, with little preparation and in periods of emotional distress. Both the demand for, and the success of, care services depend on the quality of housing and primary and secondary medical care in the area. These challenges are not insurmountable, but do need to be taken into account in government's approach to the market's design and oversight.

Our research found that the majority of those working in the sector feel that the social care market has a number of strengths, including a diversity of suppliers and services and significant competition between these providers. However, there appear to be a number of weaknesses in the current systems of market oversight and commissioning, some of which may have contributed to recent scandals around low standards of care in specific homes.

First, users and commissioners are not always making informed choices. Although there are many sources of information on particular aspects of service quality, this is often not collected or presented in a way that allows easy and authoritative comparison. It also does not tend to cover a sufficient number of providers to allow for meaningful comparison. Lack of good information makes it harder for commissioners to make price/quality trade-offs and lessens incentives for providers to invest in the skills of their workforce. Government has an important role in providing some common standards for information to ensure this comparability.

Second, housing and healthcare services are often poorly co-ordinated with social care and this often leads to avoidable escalation in care needs, reducing quality of life and additional strain on services.

Third, the downward trend in funding over the last eight years has had a major impact on the way care is delivered. To manage budget pressures some local authorities have used their monopsony position to drive down prices, which has forced providers to cut costs with knock-on effects on quality. Local authorities have also raised eligibility criteria and are increasingly only providing intensive, residential, end-of-life services. This appears to run directly counter to central government's expressed aim of preventative early intervention.

We suggest that these difficulties relate to fundamental choices regarding the design and oversight of the market in care for older people. Crucially, it is sometimes unclear who has responsibility for ensuring that important market oversight roles are performed. This was clearly demonstrated in the failure to spot the financial collapse of Southern Cross Healthcare in advance, but is also evidenced by ongoing confusion about where responsibilities lie for setting the overall funding envelope and providing information to support effective choice.

In addition, the skills of local commissioners are often seen as being inadequate for the task of encouraging innovative new care solutions within ever-tighter budgets. Interviewees expressed serious concerns that commissioners in some areas treat the purchasing of care packages as they do the purchase of commodities, focusing far too heavily on cost and inputs, rather than finding creative ways of improving outcomes.

There are reforms underway to improve the way government stewards the social care market. We particularly encourage the development of provider-quality profiles as a one-stop shop for simple and comparable information on provider quality (broken down to the level of a single institution or facility). Health and Wellbeing Boards have been established to try and co-ordinate health and care services but the extent to which they are successful at doing so will largely depend on their ability to share information and data. However, institutional reforms that clarify who is accountable for funding social care and the development of better clinical indicators of care quality are also worthy of further investigation.

History

Prior to the 1980s there was little public assistance available for older people who required social care and the majority of residential care homes were run by charities. Local authority budget cuts in the late 70's led many local authorities to withdraw what little funding they had for voluntary homes. Central government then stepped in to fill this funding gap, but left local authorities in control of allocating places. With little incentive for local authorities to ration provision, total costs quickly ballooned from £10 million (m) in 1979 to £2.5bn in 1992.[227]

In 1990 central government passed the NHS and Community Care Act to bring social care spending under control. This devolved the budget for social care to local authorities and limited the amount they could spend on in-house provision. It also led to the replacement of grant funding with contractual arrangements. Reforms since the mid-90s focused on encouraging the personalisation of care services and further devolution of budgets down to users.

The funding available for social care has struggled to keep pace with rising costs of provision over the last 20 years. This has prompted many local authorities to raise the eligibility criteria for state-funded care and local authorities now pay for just over half of older care-home residents.[228] Local authorities have also steadily outsourced more and more provision to limit costs. Between 1992 and 2010 the number of places provided directly by local authorities fell by more than 70%, while the number of privately-operated care-home places rose by 17%.[229]

The social care market today is worth £23bn, about two-thirds of which is delivered in a residential setting, with the other third being delivered in people's homes.[230] Two-thirds of this spending comes from publicly-funded care, with the other third coming from 'self-payers'.[231] The market is highly dispersed with 90% of residential care providers having only one or two homes[232] and the top 10 providers accounting for only 24.8% of beds in care homes.[233] In total, there are 1.63m people employed in the provision of adult social care in England.[234]

The nature of residential care has changed. Older people now enter care homes later in their life, often with more complex needs, for shorter periods of more intensive care. Clive Bowman, formerly a Director at Bupa and now an Honorary Visiting Professor at City University, likens this role to a sub-acute hospital.[235]

Inherent difficulties

There are several characteristics of care for older people that create particular challenges for delivering it through mechanisms of choice and competition. These are by no means insurmountable barriers, but a well-functioning system of choice and competition will be designed to offset and mitigate these features.

[227] Gash, T., and Roos, T., *Choice and Competition in Public Services: Learning from History*, p. 20, Institute for Government website, 2012, retrieved 6 June 2013, http://www.instituteforgovernment.org.uk/publications/choice-and-competition-public-services

[228] Laing and Buisson, *Care of Elderly People UK Market Survey 2012/13*, Laing and Buisson website, 2012, retrieved 8 June 2013, http://www.laingbuisson.co.uk/MarketReports/MarketReportsHome/tabid/570/ProductID/548/Default.aspx

[229] NAO, *Oversight of User Choice and Provider Competition in Care Markets*, NAO website, November 2011, retrieved 8 June 2013, http://www.nao.org.uk/report/oversight-of-user-choice-and-provider-competition-in-care-markets/

[230] Ibid.

[231] Ibid.

[232] Behan, D., 'Social Care Provision: what can we learn from our diverse market?' *Guardian Professional,* 14 March 2012, retrieved 5 June 2013, http://www.guardian.co.uk/social-care-network/2012/mar/14/social-care-provision-david-behan

[233] Forder, J., and Allan, S., *Competition in the English Nursing Homes Market*, PSSRU website, August 2011, retrieved 10 June 2013, http://www.pssru.ac.uk/archive/pdf/dp2820.pdf

[234] Skills for Care (2012), *The State of the Adult Social Care Sector and Workforce in England,* Skills for Care website, October 2012, retrieved 8 June 2013, http://www.skillsforcare.org.uk/research/latest_research_reports/SOASCW_2012.aspx

[235] Institute for Government Interview SC004

First, it is hard to measure the value added (how much quality of life is improved by being in care) of care service providers. This makes it hard for service users to compare the different services on offer without having personally experienced them.[236] For this reason, we generally talk about quality instead of value added, by which we mean the standard of a particular aspect of a service (e.g. nutrition and dignity). Even this is hard to measure because of challenges in aggregating subjective ratings, getting enough people to rate the services to generate useful ratings, and the high turnover of staff which quickly make the ratings out of date.

Compounding this difficulty of measurement, purchasing decisions are often made quickly, with little preparation and in periods of emotional distress. Care is not something we generally like to think about in advance[237] meaning that decisions are often left until people are forced to take action by events (e.g. a fall). This can be a very emotionally demanding time for both users and their families, which can make the decision process more fraught. To add to this, the costs of switching providers are high, particularly for dementia sufferers, who find major changes distressing. This makes it important to make the best possible decision first time round.

The second interesting feature of care services is their interdependence with other services. Both the demand for, and the success of, care services are highly dependent on the quality of housing and primary and secondary medical services. Indeed care needs are almost defined by a combination of environment (where you live) and your personal capacities (of which health is a big part).

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[236] Netten, A., et al, *Measuring the Outcomes of Care Homes: Final Report*, PSSRU website, June 2010, retrieved 8 June 2013, http://www.pssru.ac.uk/pdf/dp2696_2.pdf

[237] See, for example, 'Older people heading for care-funding crisis by failing to plan', Bupa website, January 2013, retrieved 10 June 2013, http://www.bupa.co.uk/individuals/care-homes/news-2013/january-2013/care-funding-crisis

Figure 22: Characteristics of care for older people

In order to assess...	...Ask	RAG Rating	Details
The appropriateness and effectiveness of user choice mechanisms	Do consumers face high switching costs?	Highly Problematic	Very emotionally disruptive, especially for people with dementia.
	Are consumers often involved in distress purchasing?	Highly Problematic	Purchasing very often prompted by a crisis with little prior preparation and at an emotionally straining time.
	Is the service a merit good?	Problematic	Users systematically underestimate benefits of consumption (including low-level or preventative measures).
The costs and risks of using market mechanisms, and the need for regulation to mitigate these risks	Is it difficult to measure the value added of providers?	Problematic	One of the best attempts is here, but it encountered serious challenges http://www.pssru.ac.uk/pdf/dp2696_2.pdf
	Are service outcomes highly dependent on the performance of other services?	Highly Problematic	Depends on sensible interaction with hospitals and primary care, very often not coordinated properly.
	Does delivering the service require investment in highly specific assets?	Problematic	Higher in specialist dementia facilities, buildings can be sold for flats.
	Is the service characterised by high demand uncertainty?	Unproblematic	No, long demographic 'pipeline' and ageing population.
	Is the service characterised by high policy uncertainty?	Unproblematic	Generally perceived to be stable.
	Is the service essential for government's ultimate decision-making or coercive authority?	Unproblematic	No.
The ease and cost of transition from a fully government-owned and delivered service to one based on market mechanisms	Is there an existing supply of (high-quality) providers?	Unproblematic	
	Is there an existing workforce (either in the public or private sectors) with adequate skills and capabilities to deliver high-quality services?	Problematic	
	Does the government have the organisational capability to design and monitor the use of market mechanisms?	Problematic	
	Does the government have enough information about cost and quality to measure provider performance?	Problematic	

RAG Rating Key
- Highly Problematic
- Problematic
- Unproblematic

Market strengths and weaknesses

We found a number of strengths in the market for publicly-funded social care for older people including:

- a diversity of suppliers and services on offer
- outstanding examples of innovation and compassion
- some marked improvements in the delivery of more specialised dementia care.

Nevertheless, this chapter looks forward and aims to analyse the areas that are not working as well as they could be, describes the trade-offs, and proposes some institutional solutions. Our interviewees identified five main weaknesses in the market for social care services for older people:

- care is often commissioned and delivered too late, and in the wrong setting
- there is a lack of training and professionalisation among those delivering care

- funding is low relative to need and stated policy aims
- provider quality is hard to compare
- procurement is overly-focused on price.

We review the evidence for, and nature of, each of these market weaknesses in this section. In the next section, we explain the existence of each problem by looking at the challenges created by the characteristics of social care as a service, followed by the particular way in which government is organised. In the final section, we draw some lessons for how government should oversee the social care market, and markets in public services more generally.

Care is often delivered too late and in the wrong setting

There is consensus that the design of the social care system is ineffective at managing demand. Interventions are not made at the right time and are not delivered in the right setting, causing preventable increases in peoples' care needs, reducing their quality of life and generating additional demand for services. Demand for services which is generated by the failure of those services is known as 'failure demand'.[238] This represents a poor use of resources because better outcomes could have been achieved at a lower cost by intervening at the right time and in the right setting.

To get an understanding of this process we mapped the different types of failure demand in the system by looking at the preventable and undesirable movements of older people across organisational boundaries. This is shown schematically in Figure 23 below. Please note that the figure below is not intended to claim that all intensification of care provision is a bad thing (in many cases it will be entirely appropriate) neither does it assume that in all cases, with the right intervention, older people can always be rehabilitated to a state in which they require less care.

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[238] Seddon, J., *Systems Thinking in the Public Sector*, Triarchy Press, Devon, 2008.

Figure 23: Preventable and undesirable institutional transitions in care for older people[239]
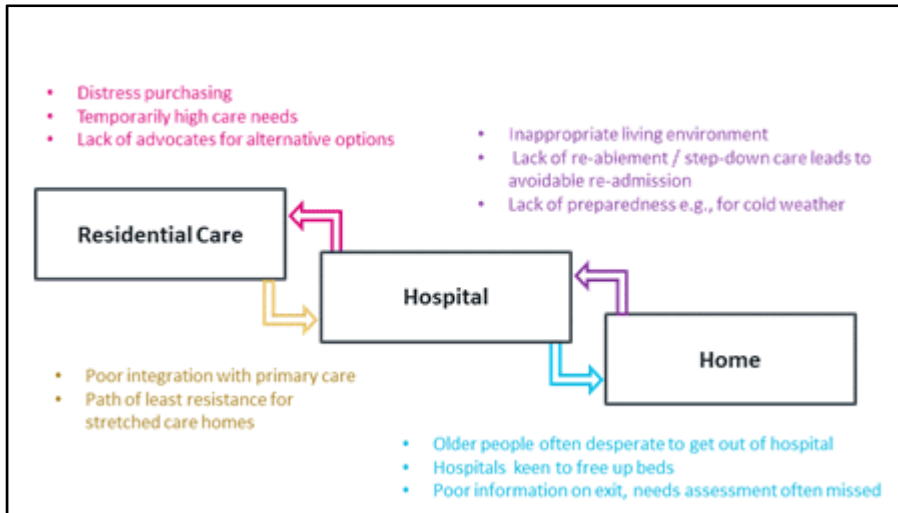
Home to hospital

Recent research suggests that around a quarter of all acute hospital admissions among older people are preventable.[240] Michelle Mitchell from Age UK told us that sometimes these admissions can be prevented by something as simple as preparing for cold weather snaps by helping older people ensure their windows are closed properly. Falls are also a major source of these admissions and many of them could be prevented by alterations to older people's home environments. A study by Dylan Kneale from the International Longevity Centre found that, when compared to a matched control group receiving domiciliary care, those living in housing designed specifically for older people were around half as likely to suffer a fall.[241] Research also shows that general 'reablement' interventions (which help people relearn the skills necessary for daily living that may have been lost through deterioration in health and/or increased support needs) improve older people's quality of life with no increase in costs.[242]

The Partnership for Older People Projects (POPP) ran from 2006 to 2009 and was designed to promote the health, wellbeing and independence of older people and prevent or delay their need for higher intensity or institutional care. The official evaluation of POPP found that overnight hospital stays were reduced by 47% resulting in £1.20 in savings for every £1 spent on the scheme[243] showing that it is possible to avoid illness and accidents while saving money at the same time. Once an avoidable admission to hospital occurs, older people are at increased risk of picking up infections.

Hospital to home (and back again)

> Elderly people find themselves on this treadmill of admission, re-admission.

<div align="right">Sarah Pickup, Director ADASS</div>

Hospitals are often pushed for bed space and this creates pressure to discharge older patients as soon as they no longer require high-frequency medical attention. Older people are understandably also very keen to go back home.

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[239] Institute for Government analysis

[240] Mytton, T., et al, *Avoidable Acute Hospital Admissions in Older People*, British Journal of Healthcare Management website, 18(11), pp 597-603, November 2012, retrieved 8 June 2013, http://www.bjhcm.co.uk/cgi-bin/go.pl/library/article.cgi?uid=95241;article=BJHCM_18_11_597_603

[241] Kneale, D., *Establishing the extra in Extra Care: Perspectives from Three Extra Care Housing Providers*, International Longevity Centre UK website, September 2011, retrieved 8 June 2013, http://www.ilcuk.org.uk/index.php/publications/publication_details/establishing_the_extra_in_extra_care_perspectives_from_three_extra_care_hou

[242] Francis, J., et al, *Re-ablement: a Cost-Effective Route to Better Outcomes, SCIE Research Briefing* 36, Social Care Institute for Excecllence website, 2011, retrieved 6 June, http://www.scie.org.uk/publications/briefings/briefing36/

[243] Windle, K., and Forder, J., *National Evaluation of Partnerships for Older People Projects: Final Report*, PSSRU website, December 2009, retrieved 8 June 2013, http://www.pssru.ac.uk/pdf/dp2701.pdf

In the words of Michelle Mitchell, Director of Age UK, 'Many older people are desperate, I mean desperate, to get out of hospital.' These combined pressures can lead to premature discharge from hospital.

On discharge from hospital all older people are supposed to be given a formal care needs assessment, but this is often missed leading to an increased chance of re-admission.[244] Signposting of additional care options, including step-down care to safely settle people back into their own homes, is also often missing. This can lead to avoidable re-admission when, for example, an older person who has picked up a bladder infection in hospital suffers a fall while trying to get to the bathroom at night.[245]

Hospital to residential care

When an older person is discharged from hospital they are often moved to a residential care facility when they would have been better off elsewhere, in terms of their welfare and care needs. Concerned family members will often make the decision to move their relatives to a residential care home because they feel more confident that they will receive the right care there as opposed to receiving domiciliary care. This is not always the best option but information about, and advocates for, appropriate alternatives are often not available in hospitals. People generally do not like to think about themselves or their relatives going in to care, which often leads to a lack of planning and informed decision making.

Andrew Kerslake, from the Institute of Public Care, argues that on discharge from hospital some patients have several medical conditions that make them look like a sensible candidate for residential care. But a week or two later many of these will have gone meaning the patient could, with some form of intermediate care, have gone back to their home. Several of our interviewees pointed out that doctors in hospitals often take a medicalised approach to care for the elderly, taking little interest in post-treatment care and opting for residential care as the 'default' option or 'path of least resistance'. For many older people, there will be no remedial option and a care home may be the safest and least isolated place for them to go. But for some there will be better options.

Residential care to hospital

Lastly, there are sometimes unnecessary and avoidable admissions to hospitals from care homes. Poor integration with primary care providers sometimes means that medical conditions are allowed to develop into acute hospital admissions.[246] Re-admissions after an initial hospital visit are also more likely among those living in care homes.[247] Challenging behaviour, which is a common occurrence among people in care homes,[248] can also result in avoidable admissions to hospital when care home staff feel they are no longer able to cope. Indeed, in some cases, busy care home staff may follow this route simply to manage their workload. One of our interviewees argued that a small minority of care homes develop a mentality of 'just ring 999'.[249]

There is a lack of training and professionalisation among those delivering care

> The social care workforce is bigger than the NHS workforce but doesn't get anywhere near as much attention.
>
> Sally Warren, former Director Social Care Policy, Department of Health

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[244] Care Quality Commission, *The State of Care and Adult Social Care in England 2011/12,* p. 63, CQC website, 2012, retrieved 5 June 2013, http://www.cqc.org.uk/public/reports-surveys-and-reviews/reports/state-care-report-2011/12

[245] Institute for Government Interview SC002

[246] Bowman, C., Elford, J., Dovey, J., Campbell, S., and Barrowclough, H., 'Acute hospital admissions from nursing homes: some may be avoidable', *Postgraduate Medical Journal*, January 2001, National Center for Biotechnology Information website, retrieved 5 June 2013, http://www.ncbi.nlm.nih.gov/pmc/articles/PMC1741862/

[247] Quinn, T., 'Emergency hospital admissions from care-homes: Who, why and what happens? A cross-sectional study', *Gerontology*, 57(2), pp. 115-120, May 2010, retrieved 8 June 2013, http://www.ncbi.nlm.nih.gov/pubmed/20484883

[248] Challenging behaviour includes any anti-social or aggressive behaviour. For evidence on prevalence see Centre for Policy on Ageing, *A Profile of Residents in Bupa Care Homes: Results from the 2012 Bupa Census*, CPA website, 2012, retrieved 5 June 2013, http://www.cpa.org.uk/information/reviews/Bupa-Census-2012.pdf

[249] Institute for Government Interview SC018

Skill shortages are a problem in social care. The UK Commission for Employment and Skills released a report in 2012 which found that 5.2% of all employees in the care sector are judged by their employers as unable to do their job to the required level due to a lack of skills specific to caring (rather than general skills).[250]

Skills shortages are reported to have a 'major impact' in 11% of health and social care establishments.[251] Eight out of 10 of these establishments said that these skills gaps pushed up workloads for other staff. Half said it made it more difficult to introduce new working practices. Four out of 10 said it made it difficult to meet minimum-quality standards and a third said it increased operating costs.[252] The most commonly cited reason for skills gaps is that staff are new to their role and/or haven't yet completed training, suggesting problems with staff turnover – which may be as high as 20% among those directly involved with care in private providers.[253] Although some staff turnover is a natural feature of any healthy organisation, this is having a noticeable effect on skills in the social care sector.

Nearly half of those raising staff retention difficulties in the survey put this down to low pay, though the emotionally demanding nature of the work is also likely to play a big role. According to the Skills for Care data set, average hourly wage rates for people directly involved in the delivery of adult care is £6.72,[254] the average salary for carers is £13,128 and almost 12% of those working in social care and over the age of 22 are paid at or below the national minimum wage (£6.08 per hour).[255]

Specialist training in dementia care is a particular problem. Around two thirds of care home residents in the UK have dementia and caring for them requires particular skills in communication and, sometimes, knowing how to deal with challenging behaviour. Research conducted in the North East by the Personal Social Services Research Unit (PSSRU) found that only 42% of staff in residential care homes had received external training on caring for people with dementia while 18% had no training whatsoever in this subject.[256] Almost two-thirds of the managers responding to an Alzheimers Society survey identified attracting care staff with the right skills as one of the biggest barriers to providing good dementia care.[257]

Many of our interviewees argued that there is also a problem with professionalisation and clear pathways for carer career development. This is in marked contract with the NHS where the Agenda for Change addressed some of the problems around career development and pay for nurses. It is perhaps not surprising therefore that 12% of those leaving adult care in 2011 went to work in the healthcare sector.[258]

There are clearly cost versus quality trade-offs to be made around the training of staff and a balance has to be struck. The fact that a third of survey respondents said that a lack of skills actually increased operating costs does however suggest that the current balance might not be optimal. Evidence on the relationship between staff turnover (which is a significant cause of cost for any business) and training would be useful in this respect.

[250] UKCES, *Sector Skills Insights: Health and Social Care*, Evidence Report 52, UKCES website, July 2012, retrieved 8 June 2013, http://www.ukces.org.uk/publications/er52-sector-skills-insights-health-and-social-care

[251] Ibid.

[252] Ibid.

[253] Hussein, S., 'The Size Roles and Stability of the Social Care Workforce in England,' *Social Care Workforce Periodical,* King's College London website, August 2009, retrieved 8 June 2013, http://www.kcl.ac.uk/sspp/kpi/scwru/pubs/periodical/2009/issue1.aspx

[254] Skills for Care (2012), *The State of the Adult Social Care Sector and Workforce in England*, Skills for Care website, October 2012, retrieved 8 June 2013, http://www.skillsforcare.org.uk/research/latest_research_reports/SOASCW_2012.aspx

[255] Ibid, P42.

[256] Reilly, S., Abendstern, M., Hughes, J., Challis, D., and Venables, D., *Care Homes for Older People with Dementia in the North East*, PSSRU Discussion Paper M062, May 2005, retrieved 8 June 2013, http://www.pssru.ac.uk/pdf/MCpdfs/Carehomes1.pdf

[257] Sharp, S, *Home from Home*, Alzheimer's Society website, 2007, retrieved 8 June 2013, http://www.alzheimers.org.uk/site/scripts/download_info.php?fileID=270

[258] Skills for Care (2012), *The State of the Adult Social Care Sector and Workforce in England*, Skills for Care website, October 2012, retrieved 8 June 2013, http://www.skillsforcare.org.uk/research/latest_research_reports/SOASCW_2012.aspx

## Funding is low relative to need and stated policy aims

> Older people have waited long enough. We must reform the farce that is our current system for funding long-term care.

Jane Ashcroft, Chief Executive of Anchor Trust[259]

The most commonly raised issue in our interviews was, perhaps inevitably, the level of government funding for care. In the late 1990s and early 2000's, local authorities linked annual fees to the Retail Price Index which gradually lowered care-home margins, as their costs rose faster than the general price level. Improvements in the economic position allowed local authorities to increase fees for a short period thereafter, but the economic situation has made this more difficult. Changes in funding also need to be seen in a demographic context. The number of people aged over 85, those most likely to use care, has increased by a quarter of a million since 2004-05 to 1.4m people in 2012.[260] This means that extra money has been necessary just to keep pace with need. The pressure on social care spending is set to intensify with the number of over-85s expected to double again over the next 20 years and the number of older people with moderate or severe disabilities projected to increase by 32% over the next decade.[261]

Respected market analysts Laing and Buisson have developed a sophisticated model for estimating a 'fair price for care' which takes into account 'reasonable operating costs of efficient care homes for frail older people… in any given locality… determining fee levels necessary to sustain delivery of adequate care services by independent sector providers, now and in the future'.[262] The charts below show how current fee levels match up to this standard. Laing and Buisson estimate that local authorities in England would need to raise nominal fee levels by between 5% and 8% per annum for three consecutive years to meet this standard.[263]

Figure 24: Fair fees relative to actual fees[264]
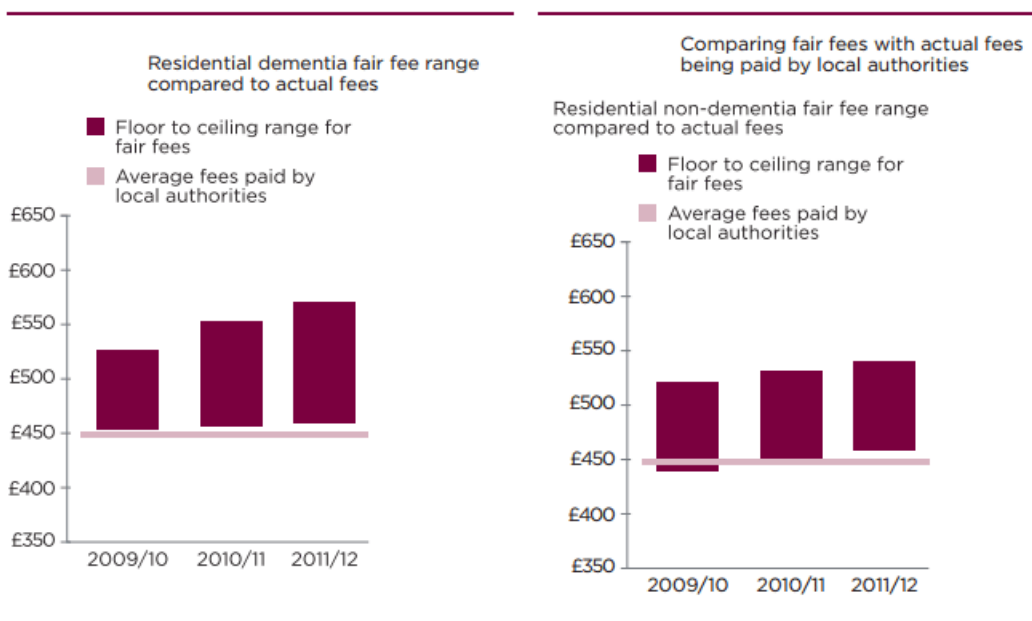
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[259] BBC News Health, 'Viewpoints: caring for the elderly', BBC online, 26 October 2012, retrieved 5 June 2013, http://www.bbc.co.uk/news/health-20079684

[260] Age UK, *Later Life in the United Kingdom factsheet*, Age UK website, 2013, retrieved 16 July 2013 http://www.ageuk.org.uk/Documents/EN-GB/Factsheets/Later_Life_UK_factsheet.pdf?dtrk=true

[261] Wittenburg, R., Hu, B., Comas-Herrera, A., Fernandez, JL., *Care for Older People*, Nuffield Trust in partnership with PSSRU, Nuffield Trust website, December 2012, retrieved 8 June 2013, http://www.nuffieldtrust.org.uk/sites/files/nuffield/publication/121203_care_for_older_people_1.pdf

[262] Laing and Buisson (2008) Calculating a Fair Price for Care A toolkit for residential and nursing care costs http://www.laingbuisson.co.uk/portals/1/media_packs/Fact_Sheets/Fair_Price_ThrdEd_2008.pdf

[263] Laing and Buisson, *A Fair Deal*, Bupa website, 2011, retrieved 8 June 2013, http://www.bupa.com/fairdeal

[264] Ibid.

Further evidence for underfunding comes from three judicial review decisions in which judges have ruled that councils have failed to take account of the legitimate costs of running a care home when setting fee levels. Almost three-quarters of directors of adult social services responding to a recent King's Fund survey felt either 'very pessimistic' or 'fairly pessimistic' about 'the financial state of the whole health and care economy' in their local authority.[265]

The level of funding available for social care will likely never be high enough to satisfy everybody. But the fact that eligibility criteria are being raised at the same time that fees are falling further below a 'fair price', suggests underfunding is now a serious problem.

Another criterion against which we can judge the amount of money available for social care is the policy goals of central government. In the 2012 Care and Support white paper[266] the government promised, 'The focus of care and support will be transformed to promote people's wellbeing and independence instead of waiting for people to reach a crisis point.' Because of falling funding however, local authorities have been forced to increase the eligibility criteria for state-funded social care and are increasingly only providing care at the very end of life. In 2005 half of councils provided support to people assessed as having 'moderate' needs (who would often be cared for in their homes). But, by 2011, the figure had fallen to just 18%.[267] With less money to work with, intervention is likely to occur later in the life-course, most likely after a crisis point has been reached and the opportunity for sustaining independence has been missed.

Provider quality is hard to compare

A choice-based system for delivering social care is fundamentally premised on the idea that consumers or commissioners will be able to compare the quality of care of different providers to select the best providers, driving up quality by incentivising lower-quality providers to improve. Without the necessary information choice becomes arbitrary or misguided and the pressure for improvement arguably disappears. Worryingly, a quarter of respondents to a recent Social Care Institute for Excellence poll say they have ended up with the wrong type of support, raising doubts about the quality of information on which choices are made.[268] Given that few people switch care providers after making an initial choice, and there may even be health risks for older people moving between care homes,[269] having the right information available before they make their first choice is crucial.

An important piece of context to this section is the introduction, and subsequent abolition, of the 'star ratings' system. Between April 2008 and 2010 the sector regulator (initially the Commission for Social Care Inspection and subsequently the Care Quality Commission) published star ratings which provided a reasonably authoritative judgement on the quality of a care home based on a range of information collected partly through inspection. The system was not perfect and was often criticised for creating a compliance oriented, box-ticking culture. In 2010, however, this system was abolished and the Care Quality Commission (CQC) began a consultation on a replacement system, in which providers would pay to be inspected and graded against replacement quality standards. The proposed system proved unpopular with providers however and was subsequently abandoned by the CQC.

The vacuum left by star ratings has been partly filled by a number of decentralised initiatives. To get a better understanding of the types of information that are available to inform people's choices we conducted an audit of the information relating to:

[265] Appleby, J., Humphries, R., Thompson, J., Galea, A., *How is the Health and Social Care System Performing? Quarterly Monitoring Report*, King's Fund website, June 2013, retrieved 8 June 2013, www.kingsfund.org.uk/publications/how-health-and-social-care-system-performing-june-2013

[266] Department of Health, *Caring for Our Future: Reforming Care and Support – White Paper*, Government website, 2012, retrieved 5 June 2013, https://www.gov.uk/government/publications/caring-for-our-future-reforming-care-and-support

[267] Care Quality Commission, *State of Care Report 2010 to 2011*, CQC website, September 2011, retrieved 5 June 2013, http://www.cqc.org.uk/public/reports-surveys-and-reviews/reports/state-care-report-2010/11

[268] SCIE, 'Public mystified by care system: SCIE launches service to help people find appropriate support', SCIE website, October 2012, retrieved 8 June 2013, http://www.scie.org.uk/news/mediareleases/2012/221012.asp

[269] Laughlin, A., Parsons, M., Kosloski, KD., Bergman-Evans, B., 'Predictors of mortality following involuntary inter-institutional relocation.' *Journal of Gerontological Nursing*, 33(9):20-6, quiz 28-29 2007.

- **attitudinal:** information based on service users (and their families) or inspectors' subjective ratings of services (e.g. the percentage of residents in a care home that are fairly or very happy with the standard of care they receive).
- **operational:** information on the deployment and use of resources (e.g. the ratio of carers to older people in a care home).
- **clinical:** facts about user's health (e.g. the prevalence of bed sores).

Attitudinal

In the 2012 Care and Support white paper the Government pledged to support the development of user-generated comparison websites.[270] An extended Google search shows just how many websites now offer these services (see Figure 25 below) and just how diffuse this market has become. This is a serious problem for a service which relies on network externalities to be effective – i.e. you need a lot of people using a single rating service before it has enough information on it to be useful to anyone. For user reviews to provide reliable and comparable information they need to be sufficiently concentrated in just a few portals.

We found that many of the websites had very few reviews. There is also a range of practice in terms of the quality assurance measures employed, for example, requiring reviewers to disclose their email address to website administrators, 'rate the rater' services, or a right of response from the provider. Many of them also rely on providers paying for premium content meaning that their impartiality cannot be completely guaranteed.

This proliferation of review sites and metrics may also make choice more difficult for users. As the decision science literature shows, multiple information sources and metrics do not help people make good decisions.[271] This is illustrated by research into how online reviews are used in social care. For example, Trigg finds that:[272]

- when presented with large amounts of complex information people resort to making more intuitive decisions, leading to disproportionate weight being given to particular comments or testimonials
- people tend to look at a relatively small amount of information, so it is important that they are presented with the most important information early.[273] Increasing the total amount of information available does not necessarily lead to better decisions
- information should be tailored to individual needs.[274]

The Government also wants to introduce a so-called 'friends and family test' for care settings. This is a short survey given to users of a service that asks whether you would recommend the service you have used to a friend or family member. This sounds straightforward, but detailed testing revealed that people found it hard to understand the question and interpreted it in very different ways.[275] The evaluators recommended adopting a 10-point scale instead with 'overall I had a very good experience' and 'overall I had a very poor experience' at each end.

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[270] Department of Health, *Caring for Our Future: Reforming Care and Support White Paper*, Gov UK website, 2012, retrieved 5 June 2013, http://www.dh.gov.uk/health/files/2012/07/White-Paper-Caring-for-our-future-reforming-care-and-support-PDF-1580K.pdf

[271] See, for example Trigg, L., *Using Online Reviews in Social Care*, PSSRU Discussion Paper 2836, PSSRU website, July 2012, retrieved 8 June 2013, http://www.pssru.ac.uk/pdf/DP-2836-Online-Reviews.pdf; Boyce, T., Dixon, A., Fasolo, B., and Reutskaja, E., *Choosing a High-Quality Hospital: the Role of Nudges, Scorecard Design and Information,* The King's Fund website, 18 November 2010, retrieved 5 June 2013, http://www.kingsfund.org.uk/publications/choosing-high-quality-hospital; Fasolo, B., Reutskaja, E., Dixon, A., and Boyce, T., 'Helping patients choose: how to improve the design of comparative scorecards of hospital quality', *Patient Education and Counselling*, Vol. 78, No. 3, pp. 344-349, 2010; Weber, E., and Johnson, E., *Mindful Judgement and Decision Making*, Columbia University website, 2009, retrieved 8 June 2013, http://www8.gsb.columbia.edu/sites/decisionsciences/themes/decisionsciences/css/files/MindfulJudgment.PDF

[272] Trigg, L., *Using Online Reviews in Social Care*, PSSRU Discussion Paper 2836, PSSRU website, July 2012, retrieved 8 June 2013, http://www.pssru.ac.uk/pdf/DP-2836-Online-Reviews.pdf

[273] Boyce, T., Dixon, A., Fasolo, B., and Reutskaja, E., *Choosing a High-Quality Hospital: the Role of Nudges, Scorecard Design and Information,* The King's Fund website, 18 November 2010, retrieved 5 June 2013, http://www.kingsfund.org.uk/publications/choosing-high-quality-hospital

[274] Fasolo, B., Reutskaja, E., Dixon, A., and Boyce, T., 'Helping patients choose: how to improve the design of comparative scorecards of hospital quality', *Patient Education and Counselling*, Vol. 78, No. 3, pp. 344-349, 2010.

[275] Graham, C., and MacCormick, S. *Overarching Questions for Patient Surveys: Development Report for the Care Quality Commission*, National Patient Survey Co-ordination Centre, NHS Surveys website, 2012, retrieved 7 June 2013, http://www.nhssurveys.org/Filestore/reports/Overarching_questions_for_patient_surveys_v3.pdf

A group of 13 of the largest care providers has now taken the unusual step of voluntarily commissioning MORI to survey the older people that use their services to allow consumers to compare their performance.[276]

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[276] Ipsos MORI, *Your Care Rating 2012 Survey*, January 2013, retrieved 8 June 2013: http://www.ipsos-mori.com/DownloadPublication/1530_sri-your-care-rating-2012.pdf

Figure 25: Social care user-review websites[277]

	Service Name	Est.	Website	Free to use?	Funding Model	Type of organisation	Quant/category ratings	Do complaints/ suggestions go to provider?	User generated?	Right of response?	Rate the Rater?	Contributor Identification?	Comments
1	Patient / care opinion	2005	https://www.patientopinion.org.uk/	Yes	Premium user subscribers	Social enterprise	No	Yes	Yes	Yes	Soon	Email	Setting up dedicated care version soon
2	Care home		http://www.carehome.co.uk		Advertising	For profit	Yes	No	Yes and No	Unclear	Unclear	Email, phone	'Recommendations' only
3	Care Quality Commission	2009	http://www.cqc.org.uk/	Yes	Publicly-funded	Official regulator	Yes	No	No	N/A	No	N/A	Used to do star ratings now pass/fail against minimum standards
4	Best Care Home		http://www.bestcarehome.co.uk/	Yes	Providers pay for premium profile features e.g. pictures		Yes	No	No	N/A	No	N/A	Use an index which they construct from facts and CQC ratings
5	Good Care Guide	2012?	http://www.goodcareguide.co.uk	Yes	Pay for premium profile content	Company limited by guarantee	Yes	No	Yes and No	Yes	No	Email	Does child and elderly care
6	Care Home Reviewer	New	http://carehome-reviewer.com	Yes	Pay for premium profile content		Yes	No	Yes	Unclear	No	Email	Very few ratings

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[277] Institute for Government analysis

7	Care Adviser		http://www.care-advisor.org.uk	Yes			Yes	No	Yes	No	No		Very few reviews, now defunct?
8	Find me Good Care	2012	http://www.findmegoodcare.co.uk	Yes	Subscription and pay for enhanced listing	Social enterprise?	Unclear	Yes/No	Yes and No				No ratings yet!
9	Your Care Home		http://www.yourcarehome.co.uk	Yes	Adverts		No	No	No	N/A	No	N/A	Simple directory of services

Operational

The CQC continues to inspect all registered care homes against 16 essential standards which can be grouped under the themes of involvement, treatment, safety, staffing and management.[278] These are only minimum standards however and, while they may be useful for indicating the existence of very poor care, they do little to assist in choosing high-quality care. In the absence of full information in this respect, some local authorities have begun to collect their own information to ensure the quality of the care they commission. Many providers claim that having to comply with multiple regulatory regimes across multiple authorities is a waste of resources. A director of a major care provider pointed out the inefficiencies involved:

> It's a few bits of paper here, a few bits of paper there, but the impact of that fragmentation is quite significant in terms of cost in our organisation and ultimately the costs that get passed on, in one way or another, to the eventual users….The lack of the opportunity for central direction just means that there's a vacuum that is left which is then filled in 126 different ways, or however many commissioning local authorities there are.

Clinical

The UK has very little clinical information on people receiving care services. Care needs are assessed by the local authority, either on the instruction of a GP or on release from hospital, against a basic four-point scale. They are then reassessed every six months thereafter unless a professional prompts an additional assessment. The four-point scale is:

- critical: where life is in danger, or serious abuse or neglect has occurred or might occur
- substantial: where abuse or neglect has occurred or might occur, or the individual is unable to carry out the majority of personal care or domestic routines and there is no-one available to assist
- moderate: where the individual is unable to carry out several personal care or domestic routines, or engage in routine family or social activities
- low: where the individual is unable to carry out one or two personal care or domestic tasks, or engage in one or two routine family or social activities.

This scale is designed to assess eligibility for local-authority-funded care and is adequate for this purpose. It is not, however, adequate for assessing the clinical outcomes/pathways of patients across different care homes. In the USA care providers are required to provide standardised and regular information on a range of individual clinical indicators as a condition of receiving money for the provision of state-funded care. This information is doubly useful as it allows for a complete picture of care needs to be established and powerful comparison of care quality to be made by asking 'how did the care needs of initially similar people develop with different providers?' If similar individuals consistently develop higher-care needs more quickly in certain institutions then this raises questions about that provider. It is also a powerful tool for providers to monitor performance across their care homes. Bupa have trialled the system for just this purpose and have found it to be a useful management tool.

Comparability

> There's no point in giving out lots of information because it won't necessarily be read or understood. It needs to be framed in an accessible way and presented in a standardised, comparable and meaningful manner that allows people to make the most suitable choices which best meet their needs.

Sue Aspinall, Assistant Director OfT

This brief review of the crowded information landscape suggests that the raw quantity of information on offer is not the main problem. Our analysis points instead to the need to ensure that common metrics are collected across many providers and are available in a disaggregated form that allows comparison across providers. Unless information allows a particular user or commissioner to compare the quality of a range of providers from which they can realistically choose, it is not particularly useful. The table below summarises the different information sources, mapped against the three types of information, and the level at which they allow comparison.

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[278] Care Quality Commission, *The State of Care and Adult Social Care in England 2011/12,* CQC website, 2012, retrieved 5 June 2013, http://www.cqc.org.uk/public/reports-surveys-and-reviews/reports/state-care-report-2011/12

Figure 26: Sources of information on care quality[279]

	Comparable across different branches within a single provider	Comparable across some providers within an LA	Comparable across all providers within an LA	Comparable across all providers
Attitudinal		Mori survey / P2P user info		CQC star ratings / CQC ES
Operational	Provider MI		LA 'regulatory' data	CQC star ratings / CQC ES
Clinical and needs	Bupa trial			MDS-RAI

Currently publicly available　　　　Not currently publicly available

Attitudinal data is comparable across some providers, but not on a particularly wide or systematic basis. What is comparable across all providers is the information on compliance with CQC essential standards but, as before, these are only minimum standards. Operational data is collected within providers but this information is generally not publicly available. Local authority regulatory data allows comparison of providers within a local authority but this is partly duplicated by the CQC essential standards leading to waste and confusion, and is generally not available to individuals making choices. Data on clinical matters has been systematically collected by Bupa and standardised tools to allow complete comparability have been developed and used in other countries, but are not currently employed in the UK.

In summary, despite choice-based systems relying on users/commissioners having enough information to reliably compare the quality of providers, there are still serious gaps in the information users/commissioners can draw on. This is the case across all three types of information. Clearly difficult trade-offs need to be made when deciding whether to collect data, not least the financial costs involved for both providers or taxpayers in collecting the data. Further, overly onerous data-collection requirements may create a 'box ticking' culture in which service user needs become obscured by paperwork. Nevertheless, there remains room for improvement in this area.

Procurement is overly focused on price

We heard three complaints about local-authority-commissioning practices raised time and time again during our interviews.

First, we heard that local authority commissioners are so focused on reducing the price they pay for services that they often fail to take other considerations into account. One director of a care provider was withering in their assessment.

> Commissioning approaches are appalling, appalling, appalling… In the worst cases it's like they are buying bananas rather than services for people. They concentrate on price rather than quality... Their objective is purely a financial objective…Sometimes it is just so short sighted.

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[279] Institute for Government analysis

Second, we were told that many local authorities tend to adopt an arms-length approach to contracting at the expense of extensive engagement, dialogue and information-sharing with providers. In the words of Martin Routledge, from the charity In Control, 'The purchaser-provider split has become a purchaser-provider yawning chasm'.

Third, we consistently heard complaints about a lack of creativity in commissioning practices and a failure to understand how commissioning can be used as a tool to drive innovation among providers. Some local authorities reportedly treat commissioning decisions as if they are limited to determining who wins this contract, rather than also influencing the broader 'ecology of supply' and the options they will face next time they come to commission a service.

Explaining the strengths and weaknesses

The problems we have identified may be familiar to those involved in the social care sector. We traced the causes of each of these five weaknesses back to either the inherent characteristics of the service (see Figure 22) or to underlying institutional features relating to the way in which the social care market is organised. Once we had repeated this process for all five market weaknesses we were left with a rich explanatory map. In many cases the underlying institutional factors help explain why these weaknesses in the social care market have persisted and which institutional changes need to be made to help government better steward the market.

In this section we explain the existence of each problem by looking at the challenges created by the characteristics of social care as a service, followed by the particular way in which government is organised. We also highlight some areas which we think are worthy of further investigation as potential solutions.

Care is often delivered too late, and in the wrong setting

At service-characteristics level, poor demand management is explained by the fact that social care is not the sort of thing people like to think about in advance,[280] meaning it is often subject to distress purchasing and opportunities for preventative measures are missed. This is clearly a problem in a choice-based system where users are, to some extent, intended to be the prime mover in accessing services.

Unfortunately, the institutional arrangements are not designed in a way that deals with this challenge effectively. The division between health and social care often means that professionals do not have the incentives or information to co-ordinate services effectively around the individual. Resources are wasted because poor trade-offs are made across institutional boundaries as cost and workload are, knowingly or unknowingly, shunted on to other parts of the system.

Lack of standardisation of information also plays a key role in inhibiting better co-ordination of care. Without shared information and common standards, care providers and the NHS have different 'views' of the same individual. Although there are efforts to join up patient records around an individual's NHS number, we still do not have data showing an individual's route through the home–hospital–care pathway. This makes it hard for commissioners to understand what constitutes an effective care pathway and what does not. As one of our interviewees put it 'you would think if that was a private sector company, you would know every single detail about what is driving that big cost'.[281] It remains to be seen whether or not the new Health and Wellbeing Boards may be able to help progress these data-sharing efforts.

Fundamentally, without some capable person or body responsible for case management it is unlikely that sensible trade-offs will be made around when and where care is delivered. At the moment family members work as an army of unpaid case managers. There are clearly benefits to this in terms of upfront cost savings. It is questionable, however, whether well-meaning amateurs with little experience and variable amounts of information will co-ordinate care in a way that is effective either at maintaining the independence of older people, or in the efficient use of resources.

Poor demand management is also exacerbated by low per-person funding, which has a particularly pernicious effect on the way that resources are allocated in social care. *The Care and Support White Paper*[282] set the

[280] See, for example, 'Older people heading for care-funding crisis by failing to plan', Bupa website, January 2013, retrieved 10 June 2013, http://www.bupa.co.uk/individuals/care-homes/news-2013/january-2013/care-funding-crisis

[281] Institute for Government Interview SC002

[282] Department of Health, *Caring for Our Future: Reforming Care and Support – White Paper*, Government website, 2012, retrieved 5 June 2013, https://www.gov.uk/government/publications/caring-for-our-future-reforming-care-and-support

objective of intervening earlier to help people retain their independence. Because local authorities have had their funding reduced however, they have been forced to reduce eligibility criteria. In 2005 half of councils provided support to people assessed as having 'moderate' needs, but by 2011 the figure had fallen to 18%.[283] This means that local authorities are increasingly only providing care for higher levels of need, usually in the later stages of life. We call this process retrenchment. Michelle Mitchell pointed out the irony of the situation:

> Local authorities are increasingly only delivering the things they are legally obliged to… They only have enough money for people to go into care homes, for those in critical need. So while the policy objective tells you that you need to invest in intervention…. What's actually happening is that local authorities are increasingly only focusing on the very, very highest in need. People are going into hospital, there isn't wrap-around support getting them out of hospital, so they either go back into hospital or into a care home.

Without care and support during periods of 'moderate' care need, people are more likely to progress to severe care need thus undermining their independence.

## Funding is low relative to need and stated policy aims

One of the main reasons for the persistence of underfunding is due to the institutional arrangements for how social care is funded. This funding pipeline is summarised in Figure 27 below. The Department for Communities and Local Government (DCLG) provides formula grants to local authorities which are predominantly based on an estimate of the relative needs of the population, based on demographic information. Social care funding is a non-ring fenced element of this grant. Local authorities then combine this with local revenues. In theory local government can top this money up with local revenues but in practice their revenue-raising powers are constrained.[284]

The money passes through so many different decision points, in so many different institutions, that it is impossible to say who is responsible for the adequate funding of social care. As one director of a care provider put it, 'The vested interests of both local and central government are powerful. It suits both to not have ring-fencing because then local can blame central and say they don't give them enough and central can say that they do give them enough but its local government's decision making which takes [the funding] away from social care.'

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[283] Care Quality Commission, *State of Care Report 2010 to 2011*, CQC website, September 2011, retrieved 5 June 2013, http://www.cqc.org.uk/public/reports-surveys-and-reviews/reports/state-care-report-2010/11

[284] See, for example, 'Local councils want full control over setting council tax bills, study finds', *Guardian*, Guardian online, February 2013, retrieved 10 June 2013, http://www.guardian.co.uk/money/2013/feb/28/local-councils-want-to-set-tax-rates?INTCMP=SRCH

Figure 27: The social care funding pipeline[285]
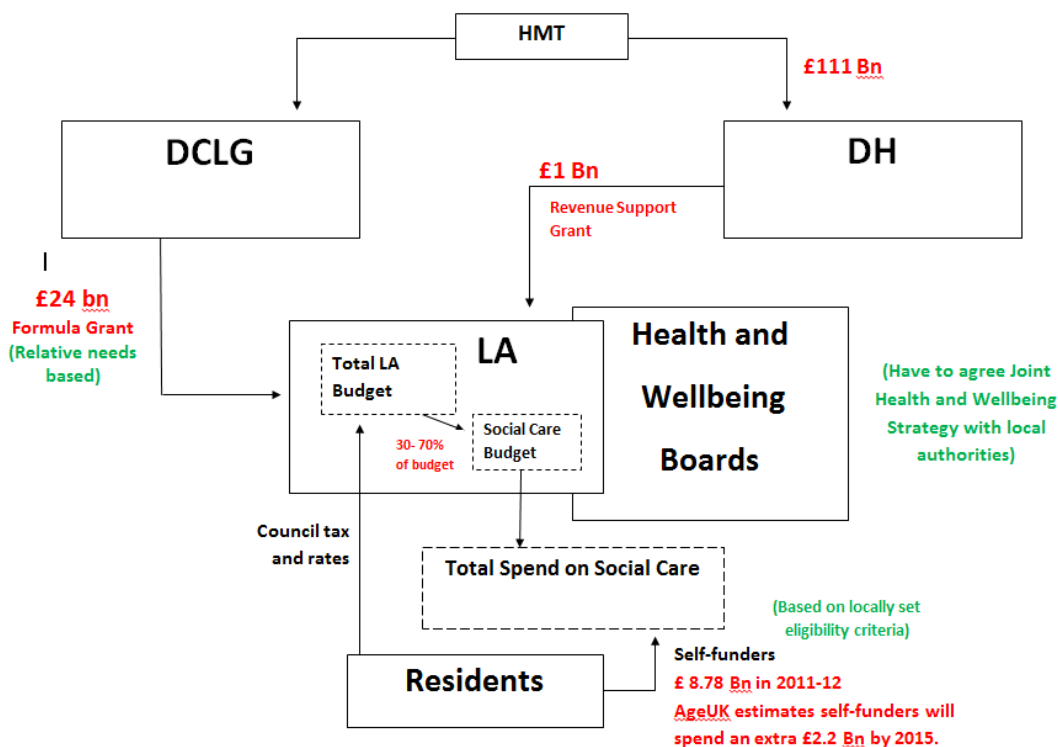
This failure of accountability is exacerbated by the weaknesses around information. Because there is no consistent, data-driven picture of actual social care need, it is impossible to allocate funding based on this, which makes it very hard for those involved in social care to make a robust, evidence-based plea for adequate funding. As one of our interviewees put it, 'One of the reasons why if you were in the Treasury you would be very reluctant to sign big cheques is that you don't know what you're paying for.'[286]

Education is funded in a similar way but doesn't suffer from the same chronic underfunding. What is different about social care? First, education funding is actually ring-fenced making central government clearly accountable for the level of funding. Second, the social care funding problem is made worse by the fact that social care for older people is not something that attracts a lot of political attention. We are generally reluctant to think about how we will spend the last months of our lives, often in a state of significantly reduced mental and physical capacity. The BBC documentary *The Year the Town Hall Shrank*[287] followed a year in the life of Stoke-on-Trent City Council as the administration implemented large spending cuts. A group of passionate and organised local parents campaigned hard to keep their local children's centres from being closed. Local councillors, conscious of the looming elections, decided that some of the centres should indeed be saved but with a finite budget the cuts had to fall somewhere and care for the elderly bore the brunt. This was a dynamic that was also described by many of interviewees.

Provider quality is hard to compare

> There is this kind of belief that the more we put on the internet the easier choice becomes… I don't feel we should judge quality by the quantity… Somehow we have to arrive at an agreed set of benchmarks.

> Andrew Kerslake, Associate Director, Institute of Public Care

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[285] Institute for Government analysis

[286] Institute for Government Interview SC004

[287] BBC documentary, *The Year the Town Hall Shrank,* November 2012, retrieved 10 June 2013, excerpts available at http://www.bbc.co.uk/programmes/b01nqc0g

Inadequate Information is explained at the institutional level by the low standardisation of data collection, which means data is often not comparable at the right level, and a regulatory approach that creates overlap and duplication. Good information is particularly important because social care is often subject to distress purchasing and high switching costs.

There is now a growing consensus that the 'let a thousand flowers bloom' approach (see Figure 25) to user-generated rating sites has serious weaknesses on the grounds that it spreads rating too thinly across different portals. Wikipedia and Trip Advisor only work because they don't have any major competitors. It also makes the task of finding the right information more difficult for prospective service users. Fundamentally, unless there is an institution capable of presenting information in a fairly simple way that creates the comparability required for competition to push up standards, comparability will remain a problem.

Measuring value added is extremely hard[288] which makes collecting comparable attitudinal data on perceived service quality essential for informing user choice. There is therefore a strong case for making available valid attitudinal measures of performance that allow comparisons to be made across a range of providers. The IPSOS Your Care Rating survey is a strong start but needs to cover far more providers. Those currently involved have a key role to play in persuading others to join up. The Department of Health should also focus on persuading the other providers to sign up, not least through giving the results a prominent position on its new Provider Quality Profiles (PQPs). There may be a critical mass at which the number of providers signed up to Your Care Rating means that other providers cannot afford to stay out. Put another way: why would you choose a care provider whose user satisfaction rating you cannot view over one that you can? The Provider Quality Profiles are a potentially useful institutional development which provide a single, authoritative and simple portal for users to compare services. There is however, quite a way to go before the PQPs include good enough information to really aid decision making.

Procurement is overly focused on price

This is partly explained by the fact that social care has relatively low economies of scale which puts many small providers in a weak bargaining position with a single local authority commissioner.

The key driver of price-focused procurement is probably underfunding, which puts pressures on commissioners to drive down price. There is an interesting point here about the psychology of contracting. When under pressure to cut budgets councillors face very tough decisions and trade-offs. One way to simplify this is to reduce the budget allocated and leave the providers who are awarded the contract to make the trade-offs. This was captured neatly by one of our interviewees who argued that what happens after a reduction in price has been negotiated 'is a level of detail which perhaps is not required'.[289] When providing services in-house, government is forced to take an overt position on price/quality trade-offs. When delivering them through commissioning, it becomes particularly important that government can be held to account for the trade-offs it makes in commissioning decisions.

Lack of comparable information also exacerbates price-focused procurement. In the absence of comparable information about provider quality, price inevitably takes on a larger significance in decision-making processes when local authorities are awarding contracts. It is hard to justify paying more for a high-quality service when it's hard to observe the quality of that service. In the words of one of our interviewees 'On the supply side, for me, the major problem was poor commissioning behaviour on the part of local authorities – basing decisions on price rather than quality… There aren't the quality indicators out there so there aren't the incentives.'[290]

There is a lack of training and professionalisation among those delivering care

This is largely the result of other market weaknesses: price focused procurement means that prices are often driven down to a level that cannot sustain much additional training on the part of providers. This is in turn exacerbated by underfunding which forces local authorities to put downward pressure on prices. In a market-based system, you don't get more than what you pay for, meaning that commissioners need to take all price/quality trade-offs, including skills, into account during the commissioning process. With downward pressure on prices and commissioners failing to prioritise highly-skilled carers in their purchasing decisions, it is perhaps unsurprising that many provider organisations choose not to invest sufficiently in the skills of their workforce.

[288] Netten, A., et al, *Measuring the Outcomes of Care Homes: Final Report*, PSSRU website, June 2010, retrieved 8 June 2013, http://www.pssru.ac.uk/pdf/dp2696_2.pdf

[289] Institute for Government Interview SC018

[290] Institute for Government Interview SC020

Lack of skills is also partly explained by the lack of clear accountability for improving workforce skills. This point was neatly captured by one of our interviewees when we asked them who is responsible for increasing skills in social care.

> It depends who you ask. If you ask the local authorities they would probably say the providers. And if you ask the providers they would say yes we do have some responsibility, but the local authority also has responsibility and we also want some help from the central agencies. [And the central agencies?] They would probably say, 'We are here to support the providers to do that.'[291] Nobody is quite sure who is responsible for improving the skills of staff in care providers.

In a sense it is strange that this conversation would even occur in relation to social care. It is paradoxical that in a service delivered through a market mechanism there should exist government-backed organisations (such as the Social Care Institute for Excellence and Skills for Care) tasked with improving the quality of care delivered by independent providers. Central government or local authorities could easily improve the skills and expertise of staff by imposing contractual requirements for staff in care providers to have particular levels of training or types of training (e.g. in dementia care). Instead of doing this, the government's strategy seems to centre on persuading providers to increase the skills of their workforce, but by paying so little (see Figure 24, p.94) it is unlikely many providers can afford to do so. The government may be pursuing this approach for cost reasons, but is unlikely to achieve desired improved service outcomes.

Areas for focus

Clarity on roles and responsibilities

In the short term, the funding problem is underpinned by fiscal pressure, but, even in the longer term, it is unlikely to be fixed primarily because it remains unclear who is responsible for funding social care. It is essential that accountability for funding social care is clarified to ensure that those making decisions about the funding of social care face some public pressure and electoral incentive to fund it adequately. One way to achieve this would be through reinstating the ring fence for care funding which would shift responsibility squarely onto central government. National eligibility criteria would also close off the 'safety' valve of local authorities increasing eligibility thresholds and would also help bring the issue of funding into the light of day. Another route would be to ensure clearer local responsibility for spending on social care through wider reforms to local education revenue-raising powers and spending responsibilities.

In the recent past, the Department of Health's preference for a 'sector-led' approach has allowed certain functions or responsibilities to fall through the cracks. Without a market steward – an organisation with ultimate responsibility for the way in which the market develops – the sector-led approach appears to allow long periods of inactivity in which each of the players in the market (regulators, agencies, local authorities and providers) wait for each other to act. This does not mean that the department shouldn't employ such an approach, but it should think of itself as the market steward with ultimate responsibility for ensuring that important functions are performed.

In order to perform market oversight roles, officials appear to need a specific set of capabilities – including an understanding of the policy environment, market dynamics, financial literacy, and commercial understanding. There is also a need for an open style of engagement given the diversity of organisations influencing the development of social care. It is therefore valuable when the department and regulators articulate the skill-sets required for specific roles – as the Care Quality Commission has recently done in relation to inspection regimes.

Information

The shortage of useful information on which consumers can base choice is a serious problem in the social care market. Reforms aimed at improving this should be prioritised. User-generated rating sites rely on a critical mass of people using a particular rating service, if this doesn't happen automatically then the government may have a role to play in creating a focal-point portal for ratings. Without government taking a role in curating and presenting it, information is likely to remain patchy and overly dispersed, inhibiting comparability. This does not mean that the process needs to be top down, however. Additional metrics on the PQPs should be developed in conjunction with providers and commissioners. Central government simply provides the stimulus to these efforts and then enforces the standards agreed to maximise the gains from them, in terms of increased comparability.

Regulatory information should once again be made the sole responsibility of the CQC under the umbrella of a reformed, and more robust, star-rating system and local authorities should then minimise the use of parallel

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[291] Institute for Government Interview SC001

measures. This will reduce wasteful regulatory overlap for providers. The CQC's consultation,[292] which implies this direction, is to be welcomed and the CQC should be confident in trialling new approaches to regulation that are proportionate to risk to free up resources to this end.

There is also huge potential to make more use of clinical data in social care.[293] In the course of our interviews we heard a standardised system for collecting data on clinical indicators described as 'nirvana', the 'holy grail' and 'a wonderful place to get to'. The main drawbacks were seen to be the cost, in terms of resource required for providers to generate the information and the time it would take to put the system in place. This is an area worthy of additional attention.

A major lesson from this case study is that, without good information on quality, it is hard for commissioners to observe price-quality trade-offs. Any reasonable person would find it hard to pay for something which they can't see. This incentivises providers to compete heavily on price which inevitably leads to cost-cutting measures, which in turn are likely to undermine quality. Where users choose and pay, individuals usually have a relatively fixed budget so they do not have to make price quality trade-offs. When commissioners choose on users' behalf (especially when there is pressure on resources) it is essential that a commissioner can observe how quality changes as price changes.

Co-ordination

The co-ordination problems in the social-care market have serious consequences for the quality and efficiency of services delivered. This would undoubtedly be a problem even if the service was not being delivered through a market mechanism and there is no easy solution. Broadly speaking, there are two options for ways of improving co-ordination.

1. Joining up around the individual attempts to reduce the poor trade-offs made across organisational boundaries by helping the older person navigate the system more effectively. This approach works by helping the individual get the best from the current institutional arrangements and is exemplified by Age UK's 'Care Co-ordinator' pilot scheme. This uses volunteers, working closely with general practitioners, to proactively identify and help co-ordinate care for older people. The aim is to prevent patients who are at high risk of admission to hospital, but do not currently have high needs, having to move into institutional care. In reality this might involve having a cup of tea with them, perhaps gently reminding them about taking medication, liaising with the district nurse, checking the windows are closed before a cold snap arrives, organising transport to social activities, or encouraging them to do exercise classes. Care Co-ordinators can also help older people tap in to different services (public or charitable) in their local area. Age UK plans to evaluate the scheme rigorously and it will be interesting to see how cost effective it is. There are also questions around the scalability of schemes based on volunteer efforts and the accountability of volunteers.

2. Joining up around budgets attempts to align incentives by internalising the financial trade-offs in a single decision maker. This should reduce poor trade-offs across organisational boundaries. It is exemplified by Andy Burnham's proposal to integrate health and social care. In practice this will require a lead institution (acute hospitals in Burnham's proposal) to hold the budgets and lead the commissioning between the different institutions within the health and social care space. There are huge transition costs involved with all large reorganisations of this sort and so there should be a strong business case established before any reorganisation takes place. It is also important not to underestimate the challenge of harmonising the information architecture and ways of working that would be required to enable commissioners with a single pot to think about, compare and commission pathways, rather than episodes, of care.[294]

[292] Care Quality Commission, *Strategy Consultation for 2013 to 2016*, CQC website, 2013, retrieved 5 June 2013, http://www.cqc.org.uk/sites/default/files/media/documents/cqc_strategy_consultation_2013-2016_tagged_0.pdf

[293] Carpenter, I., Hirdes, J. *Identifying and Maintaining Quality of Long-Term Care: an International Case Study of the Inter-Rai Assessment System for the OECD*, 14 November 2012, retrieved 5 June 2013, http://www.rcplondon.ac.uk/sites/default/files/documents/identifying_and_maintaining_quality_in_long_term_care.pdf

[294] Jonas, S., Raleigh, V., Foot, C., and Mountford, J., *Measuring Quality along Care Pathways*, the King's Fund website, August 2012, retrieved 8 June 2013, http://www.kingsfund.org.uk/sites/files/kf/field/field_document/Outcomes-measuring-quality-the-king's-fund-aug-2012.pdf

Probation services

Summary

The Ministry of Justice (MoJ) has recently announced plans to 'open up' 70% of the probation service to competition from the private and voluntary sector. This is the latest in a series of attempts to implement the vision first set out in the 2007 Offender Management Act. Since then, the number of services that different probation trusts have commissioned from other providers has varied significantly, as have their approaches.

The qualitative research conducted for this report suggests that, in some areas, probation trusts have been effective in nurturing the capacity of new entrants, generating additional resources for offender-facing services and encouraging joined-up service provision. These practices, however, tend to be the exception rather than the norm. Generally, local commissioning has been piecemeal and limited, which has raised barriers to market participation for some potentially high-capability providers and led to fragmentation between services. And, there is no systematic evidence on whether or not these commissioned services have actually reduced re-offending rates.

What are the underlying reasons for this? We found that strong local leadership, relationships and networks are critical for enabling joined-up service provision that target multiple outcomes, but these tend to be fragile and highly dependent on a few key individuals. In most areas, systemic barriers to cross-sector collaboration, such as misaligned commissioning timescales and geographies, hinder the ability to co-commission widely. Most probation trusts also lack capabilities in commissioning, procurement and contract management, which explains the somewhat ad-hoc and fragmented nature of local commissioning. While those who have begun to develop these capabilities have identified effective ways of building the capacity of local providers to co-design specialist services, this has often come at the expense of nurturing a competitive market of providers that can potentially offer better value for money. Finally, the centrally-determined budget allocation process tends to limit the amount of budgetary flexibility trusts have to commission effectively and on a wide scale.

History

The term 'probation service' refers to a wide range of services to punish and reform offenders managed in the community. These include offender management (assessing and managing risk), providing advice to the court on sentencing, implementing the orders of the court (e.g. supervising community sentences or a drug treatment order), delivering rehabilitative interventions and liaising with victims.

In May 2013, the MoJ announced its 'Rehabilitation Revolution' reform plans. This will open up 70% of the probation service to competition from a diverse range of providers by Autumn 2014. The reforms include:

- establishing a national commissioning model based on 21 'contract package areas' (CPAs)
- contracting out the management of low- and medium-risk offenders
- paying providers on both a fee for service (to deliver the orders of the court) and 'payment by results' basis (to encourage reductions in re-offending rates)[295]
- extending statutory rehabilitation to offenders sentenced to less than 12 months
- implementing a new 'through the prison gate' resettlement service.

Under the plans, probation trusts will continue to be responsible for:

- the management of high-risk offenders
- initial risk assessments
- providing advice to the courts
- victim liaison
- approved premises
- potential breaches of court orders.

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[295] To be fully rewarded, providers will need to achieve both an agreed reduction in the number of offenders who go on to commit further offences, and a reduction in the number of further offences committed by the cohort of offenders for which they are responsible.

Although these reforms are by far the most ambitious to date, attempts to 'open up' probation to competition actually date back to the 2003 Carter Review. This recommended the creation of the National Offender Management Service (NOMS) to facilitate end-to-end management of offenders. This was established in 2004 and set the ambitious mandate of introducing greater 'contestability' across the prison and probation service.[296] However, little progress was actually made in this direction.

The 2007 Offender Management Act attempted to change this. This passed responsibility for the provision of all probation services to the secretary to state and triggered the conversion of all probation boards into probation trusts (hereinafter referred to as 'trusts'). These were non-departmental public bodies who were given greater local autonomy over the management, delivery and commissioning of probation services.[297]

From this point on, the National Offender Management Service (NOMS) would set out its annual commissioning intentions. It could choose to contract public-sector trusts or any other provider from the private and voluntary sector to deliver a set of specified services – with the exception of providing advice and assistance to the courts, which remained within the remit of the trusts. Under this new arrangement, trusts were allocated an annual budget from NOMS, to which they were accountable for their performance and delivery.

Soon after this the Home Office imposed an 'outsourcing' target of 7% of the total budget each trust held for offender-facing services. In April 2009, NOMS published its *Capacity and Competition Policy for Prisons and Probation.*[298] This included a statement of intent to market-test 25% of unpaid work and victim liaison provision that had been subject to 'best value' reviews over the previous couple of years.[299] Despite these initiatives, trusts largely retained their public-sector monopoly over all probation provision.

When the Coalition came to power in May 2010, there was a renewed drive towards increasing contestability in probation services. In July 2011, NOMS put the delivery of 'community payback' services out to market and London was identified as the first 'lot' – eventually won by Serco in partnership with the London Probation Trust. In March 2012, MoJ published *Punishment and Reform: Effective Probation Services*, the long-awaited consultation on the future of probation. This outlined proposals to devolve commissioning to trusts, diversify the market and encourage the development of new delivery models such as joint ventures, social enterprises and public service mutuals.[300]

The impact these initiatives have had on the amount of private and voluntary sector provision varies significantly across different probation areas. While the most radical trusts adopted a strategy of gradually increasing the amount of the budget spent on commissioned services to around 10%, others continue to deliver all – or almost all – of their services in-house.

There is also no uniformity between commissioning approaches. At one end of the spectrum, trusts hold grant agreements with small, local charitable providers,[301] while at the other, formal tendering processes are used to contract large, national providers, as in the London Community Payback scheme. In between, there are a number of short ad-hoc contracts (of a year or less). These might be services co-commissioned with local authorities, health or police, or preferred partner agreements in which a trust holds a contract with a lead provider who sub-contracts a range of specialist organisations to deliver local services.[302]

There are, however, some overarching principles that connect these very different approaches to commissioning. Trusts broadly tend to follow a three-step decision-making process when determining whether to commission a service, although in practice it is not as rigid or formal as described.

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[296] Carter, P., *Managing Offenders, Reducing Crime*, Home Office, Community Justice Portal, 11 December 2003, retrieved 5 June 2013,

http://www.cjp.org.uk/publications/archive/reducing-crime-changing-lives-the-carter-review-and-government-response-06-01-2004/

[297] There are currently 35 probation trusts across England and Wales.

[298] Ministry of Justice, *Capacity and Competition Policy for Prisons and Probation*, Ministry of Justice, 2009.

[299] The 'best value' framework required probation areas to review identified strands of service delivery (e.g. unpaid work) to assess their cost effectiveness and then compare performance against other probation areas. If there was evidence that the delivery was not achieving 'best value' these service areas would be 'market tested'.

[300] Ministry of Justice, *Punishment and Reform: Effective Probation Services,* Ministry of Justice, 2012.

[301] For example, Bedfordshire probation trust has provided a grant to a charity to run a mentoring scheme

[302] For example, West Mercia probation trust selected Youth Support Services (YSS), a voluntary sector provider, as its preferred provider on a three-year contract, who in turn manages the process of market engagement and sub-contracting specialist organisations.

1. What are the needs of our offender population?
2. Are the services 'core'?
3. Do we have the expertise to deliver these services?

Trusts tend to keep 'core' activities in-house (assessing and managing risk and providing advice to the courts). But they are more willing to commission 'non-core' services such as:

- rehabilitative interventions designed to reduce the risk of re-offending
- supervision of community payback
- employment, skills and training support
- mentoring programmes
- accommodation advice.

Trusts are also more willing to commission services which they cannot provide themselves, with commissioning often seen as a way to tap into the expertise that exists at the local level.[303]

Inherent difficulties

Contracting probation services is difficult due to 'inherent' features of the service. These create additional costs and risks that need to be carefully managed.
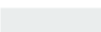
1) It is **difficult to measure re-offending outcomes** in binary terms making it difficult to specify what 'quality' consists of and how performance should be monitored. Although commissioners could use reconviction rates as a proxy, most in the sector argue that the link is not quite straightforward (as desistance from crime tends to occur gradually) and will simply increase the risk of providers focusing on what is measurable (and paid for) rather than what really matters.
2) **Re-offending outcomes cannot be controlled by one provider alone**, but depend on the performance of a range of other services such as health (for drug and alcohol treatment) and local authorities (for stable housing). This makes it especially difficult to attribute outcomes and therefore measure the value add of different providers, which increases the risk that contracted providers will be paid too much (and potentially for outcomes generated by other services) or, alternatively, too little (due to the poor quality of related services).
3) Where multiple providers contribute to achieving an outcome, it is also generally **harder to ensure that their activities are effectively co-ordinated across organisational silos**, particularly if these organisations have different ownership (i.e. public and private sector) or misaligned incentives. This could result in organisations competing for the same group referrals, withholding information and obstructing each other's performance, making it difficult for providers to control the outcomes they deliver.

As well as these inherent service features, the market for probation services is relatively immature and there are currently no private or voluntary sector providers that provide the full array of services. Commissioning providers which do not yet have this capacity is highly risky. The capacity may never develop, or it may develop in ways that do not necessarily improve service outcomes.

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[303] Interview with probation trust chief executive

Figure 28: Characteristics of probation services

In order to assess...	...Ask	RAG Rating	Details
The appropriateness and effectiveness of user choice mechanisms	Do consumers face high switching costs?		
	Are consumers often involved in distress purchasing?		
	Is the service a merit good?		
The costs and risks of using market mechanisms, and the need for regulation to mitigate these risks	Is it difficult to measure the value added by providers?	Highly Problematic	Re-offending outcomes are difficult to measure in binary terms as desistance from crime tends to occur gradually. This makes it difficult to measure the 'quality' of the services offered by providers. It is also difficult to establish whether outcomes are the result of a provider's effort or the performance of related services making it difficult to attribute (and therefore price) outcomes.
	Are service outcomes highly dependent on the performance of other services?	Highly Problematic	Reoffending outcomes cannot be controlled by one provider alone, but depend on the performance of other services such as local authorities and health.
	Does delivering the service require investment in highly specific assets?	Unproblematic	Although providers need to establish offices and recruit staff when they first establish an operation, the physical and human assets are not highly specific to the service.
	Is the service characterised by high demand uncertainty?	Problematic	The number of court orders a provider has to deliver can vary on an annual basis.
	Is the service characterised by high policy uncertainty?	Highly Problematic	Probation services have experienced extensive change over the last decade with repeated, but unsuccessful, attempts to 'open up' the service to competition.
	Is the service essential for government's ultimate decision-making or coercive authority?	Problematic	Elements of the service such as assessing risk, providing advice to the courts and ensuring public safety are essential to the government's ultimate decision making and coercive authority. However, other aspects of the service such as the delivery of rehabilitative interventions or providing accommodation advice are not.
The ease and cost of transition from a fully government owned and delivered service to one based on market mechanisms	Is there an existing supply of (high quality) providers?	Highly Problematic	The market for probation services is relatively immature and there are currently no private- or voluntary-sector providers that provide the full array of services.
	Is there an existing workforce (either in the public or private sectors) with adequate skills and capabilities to deliver high-quality services?	Problematic	New providers can rely on a large pool of existing probation trust employees, but it will take time to transfer them over.
	Does the government have the organisational capability to design and monitor the use of market mechanisms?	Highly Problematic	As only a small proportion of probation services have been subject to competition over the last few years, the government has not developed experience in designing and monitoring the use of market mechanisms.
	Does the government have enough information about cost and quality to measure provider performance?	Highly Problematic	There is little information or historical data on provider costs and quality.

RAG Rating Key

Highly Problematic	████ (pink)
Problematic	████ (tan)
Unproblematic	████ (teal)
N/A	████ (grey)

Market strengths and weaknesses

Based on our interviewee data, there is anecdotal evidence to suggest that in some areas trust commissioning has been effective in:

- **nurturing the capacity of new entrants.** We heard that some trusts have invested in the development of small, specialist organisations to deliver locally-responsive services. For example, one trust commissioned a local specialist organisation on a regular basis to work specifically with Asian offenders.[304]
- **enabling joined-up service provision.** Some trusts have developed joined-up approaches to offender management. For example, in West Mercia, ex-offenders with a history of substance misuse and poor mental health are placed on a long-term residential programme at a Care Farm, which is contracted to deliver the drug treatment orders of the court, a supervised, structured programme of farming-related activities, skills and educational training and sports facilities.[305] The qualitative evidence suggests that this programme of support improves participants' physical condition and behaviour, which could potentially reduce the likelihood of re-offending.[306]

These effective practices, however, tend to be the exception rather than the norm. Generally, local probation markets have been characterised by:

- high barriers to entry and expansion. Although some specialist providers have been able to deliver services in their local area, it has proven difficult for a number of potentially high-capability voluntary and private sector organisations to enter and expand in the market. This means that those delivering commissioned services are not necessarily the best performing, which increases the risk of expensive, but low-quality provision.
- fragmentation between offender-facing services. Although there are examples of joined-up service provision in some areas, we heard that the majority of local contracts tend to be unco-ordinated with one another, which increases the potential for duplication, fragmentation and inefficiencies in delivery.[307]

Not only is local commissioning ineffective in most areas, but the **actual impact of commissioned services on re-offending outcomes is generally unknown**. Critically, both trusts and NOMS have yet to develop systematic ways of assessing the effectiveness of the private and voluntary sector providers who deliver offending-reduction services, which makes it impossible to evaluate whether commissioning is actually improving services.[308] This means that decisions are often made on the basis of qualitative evidence with no real way of ensuring that there is a link between what is commissioned, who is commissioned and how it is commissioned, to the outcomes that are actually desired.

Explaining the strengths and weaknesses

Design and implementation choices

Although there is great diversity in local commissioning practices, the majority of our interviewees emphasised that there are some general design and implementation choices that explain the strengths and weaknesses observed.
- **Co-commissioning** practices generate additional resources for joined-up service provision (in some areas).
- **Partnerships with local, charitable organisations** stimulate entry for some providers, but raise barriers to market participation for others.
- **Short, ad-hoc contracts** undermine investment in service development (in most areas).

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[304] Interview with probation trust chief executive

[305] Interview with probation trust chief executive

[306] Elings, M., *Effects of Care Farms: Scientific Research on the Benefits of Care Farms for Clients*, Plant Research International, Care Farming UK website, 2012, retrieved 5 June 2013, http://www.carefarminguk.org/sites/carefarminguk.org/files/Effects_of_care_farms_Elings.pdf

[307] Interview with probation trust chief executive

[308] Interview with probation trust chief executive

Co-commissioning practices generate additional resources for joined-up service provision (in some areas)

Trusts often work in collaboration with local partners to co-commission services, for example by partnering with local authorities to commission employment and accommodation support services, or health services to commission substance misuse programmes for offenders. This enables them to join up a much wider range of services for offenders that can together help reduce recidivism, often for free or at a much lower cost, than would otherwise be possible.[309]

The process usually involves convincing other agencies to commit a proportion of their budget on re-offending outcomes. One interviewee explained to us, 'We try and ensure that offenders are specifically mentioned in the strategic plans or that their objectives meet ours.'[310] These efforts often result in crucial in-kind support, particularly valuable in this climate of austerity. For example, the Care Farm network commissioned by West Mercia probation trust enabled it to close down its general offending programmes and thereby make savings.[311] Another trust told us it received £5m support in kind through partners in addition to its annual £20m budget from NOMS.[312] This approach to commissioning is effective when addressing the challenges of high interdependencies between services that can often make reductions in re-offending outcomes more difficult to achieve.

Partnerships with local, charitable organisations stimulate entry for some providers, but raise barriers to market participation for others

Trusts tend to contract local voluntary- and community-sector organisations with an aligned ethos to deliver specialist and niche services. This is especially beneficial for trusts because charitable providers can work across government silos to connect otherwise disparate funding streams, which generates additional resources for offender-facing services.[313] Many of these organisations, however, do not have the capacity to deliver. As a result, some trusts have specifically invested in a range of capacity-building interventions. Examples include:

- providing training and guidance on a range of issues[314]
- allocating contracts on the basis of the capability to innovate, rather than price[315]
- seconding probation trust staff to the provider, who over time can be recruited by that provider in order to bypass costly TUPE obligations[316]
- providing longer, stable funding streams either through a grant agreement, preferred partnership approach or contract renewal[317]
- tailoring the payment model and avoiding 100% outcomes-based contracts.[318]

These interventions reportedly give providers the time and scope to develop their service offering. Trusts told us that the decision to offer primarily fee-for-service contracts (or grant agreements) as well as renew contracts helps to ensure that smaller, specialist organisations have a reliable cash-flow to continually learn, develop and invest in service delivery.[319] As one trust that partners with a local provider put it, 'that provider has grown over the years under our wing'.[320]

However, while these interventions have helped to nurture the capacity of a small pool of providers, we heard that contracts (or grants) are often awarded to providers that trusts have an existing relationship with regardless of the outcomes they deliver. This limits the number of providers that can enter and expand in the market and increases the risk of commissioning expensive, but low-quality provision.

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[309] Interview with two probation trust chief executives

[310] Interview with probation trust official

[311] Interview with probation trust chief executive

[312] Interview with probation trust chief executive

[313] Interview with probation trust chief executive

[314] Interview with two probation trusts chief executives

[315] Interview with probation trust chief executive

[316] Interview with probation trust chief executive

[317] Interview with three probation trusts chief executives

[318] Interview with probation trust chief executive

[319] Interview with two probation trusts chief executives and a probation trust official

[320] Interview with probation trust chief executive

Most trusts end up commissioning a number of providers to deliver similar services across the probation area on short, small-scale contracts. Or they commission one provider to a deliver a number of services, all governed by different contracts that come to an end at different times.[321] This increases the potential for duplication, fragmentation and inefficiencies in delivery. In addition, the unpredictable and short-term nature of contracts reportedly makes it difficult for providers to join up different services, invest in service development, recruit skilled staff and ultimately expand in the market. [322]

Underlying causes

The problems stemming from the design and implementation choices identified above will be familiar to all those involved in the sector. We argue that these choices can be traced back to underlying skills, incentives and ways of working. We highlight in particular:

- highly-personalised nature of local partnerships
- gaps in procurement and contract management skills
- constraining influence of centrally-determined funding streams.

The aim of this analysis is to uncover some general lessons about the way government should organise itself to effectively steward market mechanisms in probation services. This is particularly relevant given that the Ministry of Justice is about to embark on a large-scale reorganisation of the area.

Highly-personalised nature of local partnerships

The local partnerships that underpin effective co-commissioning practices are neither easy nor quick to build. As one interviewee put it, 'you really need to push it'.[323] Many trusts feel that the different commissioning systems seen across probation, health, police and local authorities – all of which operate according to different timescales, geographies and incentives – often make effective cross-sector partnership working highly challenging.[324]

Some pioneering trusts, however, have used a combination of formal and informal levers to actively nurture local relationships, align objectives and overcome organisational silos. For example, probation chiefs sit on different cross-agency boards such as the drug and alcohol action team (DAAT), integrated offender management (IOM), joint commissioning boards and community safety partnerships which commit a range of different agencies (sometimes up to 20) to work collaboratively to reduce re-offending.[325] But being invited to the table in the first place is often difficult and depends on the personal leadership, reputation and networks of individual probation chiefs.[326]

The [area name removed] IOM pilot was by no means easy to develop, but eventually succeeded due to the commitment and authority of the individual leaders involved. 'It took a leap of organisational faith to drag us from the status quo.'[327] Attempts to replicate the model in [area name removed] were initially less successful due to the absence of this local leadership.[328] This made it much more difficult to overcome the usual challenges associated with working across different organisational boundaries and geographies, which explains why effective co-commissioning practices are not widespread.

As such, the current approach to commissioning is based on a highly-personalised model of leadership. The key problem is that there are no institutional mechanisms that can support trusts (or providers under the new system) to overcome the systemic barriers to cross-sector collaboration. This increases the risk that effective co-commissioning practices will not survive beyond the efforts of individual leaders.

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[321] Interview with two probation trusts chief executives and a senior police officer

[322] Interview with probation trust chief executive and a probation trust official

[323] Interview with probation trust official

[324] Interview with probation trust chief executive

[325] Interview with three probation trust chief executives and a probation trust official

[326] Interview with three probation chief executives

[327] Interview with senior police officer

[328] Interview with senior police officer

Gaps in procurement and contract management skills

Given that trusts have only begun commissioning in the last three years, the majority do not have long-standing experience in commissioning, procurement and contract management. Some trusts have actively begun to address skills gaps by recruiting commercial and procurement professionals.[329] In other cases, trusts have relied on the expertise of local partners.[330] For example, the Bristol Integrated Offender Management (IOM) pilot built on the infrastructure, provider relationships and skills that Bristol City Council had already developed, and the council took the lead in scoping the service specification and tendering process requirements.[331] Another trust drew on the data collected by its local authorities to develop an understanding of the marginal costs of production and prepare a costing for an accommodation advice service.[332]

More ambitiously, eight probation trusts, co-ordinated initially by West Mercia probation trust, established Clarent – a joint social enterprise with a private-sector company, Excalibur – to enable them to procure on a much larger scale. West Mercia had previously outsourced its procurement to Excalibur and, under the initial three-year contract, paid the company to train the trust's' middle management teams in procurement to make them better contract managers of the services procured by Clarent/Excalibur, or to manage procurement more efficiently if it was brought back in-house.[333]

However, the majority of trusts do not yet have an established capability in commissioning, procurement and contract management. These skills gaps mean that those responsible for commissioning services do not tend to prioritise the same things as the procurement professionals involved in tendering the Work Programme – namely the need to buy services at the lowest price possible, maintain a competitive tension between providers and act in strict accordance with EU procurement law. This has led them to adopt a far more informal and relational approach to contracting, which involves a long process of dialogue with a small pool of providers to co-design services together rather than specifying upfront what must be delivered and how. As the chief executive of one trust put it, a lot of these contracts 'had been on a bit of a handshake'.[334]

These skills gaps mean, however, that trusts tend to be unfamiliar with the tools and techniques that can be used to robustly evaluate cost and performance. As such, they often end up awarding contracts (or grants) to the same pool of providers they have a relationship with regardless of the outcomes they deliver. Although this approach has enabled them to co-design innovative services in some areas, it does come at the expense of building a diverse and competitive market in which higher-performing providers enter and expand, while poorer-performing providers leave.

Constraining influence of centrally-determined funding streams

We heard that the NOMS budget allocation process constrains the ability of trusts to commission more joined-up, cost-effective and innovative services. Trusts complain that decisions on the total size of the annual budget are 'fairly unscientific', come very late in the day and provide no certainty as to what funding streams will be the year after.[335] This has made it difficult for trusts to make long-term planning decisions or invest in new approaches or interventions. In addition, as NOMS specifies what it expects trusts to deliver, many argue that they are left with little space or resources to 'do the proof of concept work'.[336]

These budgetary difficulties are often compounded by the three-way relationship between NOMS, trusts and the courts. NOMS may pay trusts to deliver a certain number of interventions, but the court may require them to deliver more than their annual budget allows for. This has historically been a major challenge for trusts. For example, one trust had to deliver more 'unpaid work activities' than NOMS had allocated in their budget due to the demands of the court.[337]

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[329] Interview with two probation chief executives and a probation trust official

[330] Interview with two probation chief executives

[331] Interview with senior police officer

[332] Interview with probation trust official

[333] Interview with probation trust chief executive

[334] Interview with probation trust chief executive

[335] Interview with probation trust chief executive and probation trust official

[336] Interview with probation trust chief executive and staff-representative body

[337] Interview with probation trust official

The combination of unreliable annual funding streams and the requirement to deliver both centrally-determined specifications as well as the orders of the court (which may not always match) has left trusts with very little budgetary flexibility. As a result, trusts feel that they often have to 'subvert the system in order to exploit the little flexibility they have, rather than it being [sic] encouraged'.[338] When trusts have attempted this, it has indeed been a long, burdensome process. For example, one trust was keen to commission a senior attendance centre, but it took three years to get approval from the local Directors of Offender Management (DOM) and NOMS finance team, align it with the policy direction and commissioning model at the national level, and finally EU procurement legislation. This process was referred to as a 'period of diversification at Whitehall', which eventually led the trust to abandon its attempt and instead commission the service through its preferred provider.[339]

If NOMS had moved to longer three- or five-year contracts with trusts earlier, this would arguably have provided enough stability and flexibility to allow for greater innovation and improvement in local-commissioning practices.

Areas of focus

In this section, we outline some areas where improvements could have a major impact on government effectiveness in delivering public services through market mechanisms.

Roles and responsibilities must be clear and assigned at the right geography

When introducing market mechanisms in a service area, it is critical to place the commissioning function at the right geographical level. The introduction of a national commissioning model could provide an opportunity to facilitate more coherent and co-ordinated commissioning and thus address the shortcomings associated with short, ad-hoc contracts that currently dominate the probation sector. However, while long, national contracts may achieve better economies of scale, they may in the process become unresponsive to local needs.

This is one of the key criticisms of the nationally commissioned Electronic Monitoring regime. NOMS awarded long contracts of six (EM1) and eight years (EM2) to two suppliers which have enabled them to establish regional monopolies. The regime has been criticised for locking in high costs and failing to incentivise contractors to improve the service, flex and adapt it according to local needs and keep up with the pace of technological change.[340] Although it has still encountered difficulties, trusts felt that the second electronic monitoring contract is far more effective due to the greater involvement of trusts and local agencies in the design and tendering process, as well as the establishment of effective information sharing protocols between providers.[341] If the commissioning function is assigned to an institution at the national level, it is therefore critical to involve statutory partners and local agencies in the design and delivery of services to ensure co-ordination with local needs.

Incentives and capabilities

Commissioning and oversight organisations must have appropriate incentives and capabilities to:

- **develop close, productive relationships with providers.** Trusts tend to adopt a relational approach to contracting which involves working collaboratively with a small group of providers regularly to co-design services together. Close relationships can sometimes lead to more effective, locally responsive provision, but, in the absence of robust monitoring and evaluation (as is currently the case), this is not always guaranteed. Therefore, under the new national commissioning model, it is important to build on the strengths of this collaborative approach while addressing its weaknesses. In particular, we recommend that the department thoroughly test contract design choices with commercially minded challenge boards that have an understanding of the provider perspective, but are not directly vested in the contracting process.

- **prioritise co-ordination.** Trusts are able to access a much wider range of services for offenders that can together help reduce re-offending, often for free or at a reduced cost. Given the need to manage reducing budgets across government, it is critical that this valuable in-kind support continues to grow under the new system. But this depends on local relationships, which are not only difficult to nurture in the first place, but

[338] Interview with probation trust chief executive

[339] Interview with probation trust chief executive

[340] Interview with three probation trust chief executives, probation trust official and staff representative body. Geoghegan, R, *Future of Corrections: Exploring the Use of Electronic Monitoring*, Policy Exchange website, 2012, retrieved 7 June 2013, http://www.policyexchange.org.uk/publications/category/item/future-of-corrections-exploring-the-use-of-electronic-monitoring

[341] Interview with two probation trust chief executives

fragile and highly vulnerable to disruptive changes in the system.[342] Some question whether private sector providers will be able to integrate into this 'messy world' and broker the local relationships that are critical to joined-up service provision.[343] Although government can use the payment structure to incentivise contracted providers to integrate services, local (and mainly public and voluntary sector) organisations may be unwilling to provide cost-free services for the benefit of profit-making providers. Therefore, it is important for government not to over-estimate what market mechanisms can achieve, and instead actively facilitate co-ordination across the system (for example, by encouraging joint ventures and a profit-sharing agreement).

Areas of focus

As outlined in the first section of this chapter Justice Secretary Chris Grayling's rehabilitation reforms will see the outsourcing of 70% of the current probation service by Autumn 2014. His expectation is that competing private, voluntary and public-sector providers will be able to deliver a better service at a lower cost. In many ways, the reforms bear resemblance to those that accompanied the Work Programme – particularly in terms of scale, pace and politics.

However, the probation reforms are far more complex. First, the service is inherently more risky to outsource due to the fact that outcomes are harder to measure in binary terms, more dependent on the performance of other services and difficult to robustly monitor. Second, the supplier community is relatively undeveloped and there are no private or voluntary sector providers that currently provide the full array of services. Third, there is a high risk that political priorities will change, which could result in the outsourced service being discontinued, scaled back or dramatically reconfigured – increasing the premium that providers will demand for their services now. Fourth, there is little historical experience or capability to draw on.

The Work Programme demonstrated that no matter how experienced a department is in commissioning on a large-scale, mistakes can be made. Given that the risks are higher in probation, and that service continuity is essential, government needs to find ways of actively mitigating them. Some strategies have been outlined above such as developing productive relationships with providers and co-ordinating with related services. It is also worth building in as much flexibility as possible to enable rapid learning and adaptation. One way to do this is to build in clear break clauses specifying the process by which changes to services or pricing can be agreed. Another option would be to delay the letting of some contracts to develop a better understanding of costs and quality.

Our research suggests that the Ministry of Justice may also benefit from systematically re-examining their approach to commissioning, adopting what we call a 'market stewardship' approach. Our *Market Stewardship* framework (figure 3, p. 19) identifies the main functions that need to be performed to effectively oversee and steward public service markets such as ensuring that it is clear how provider failure (in terms of performance or financial failure) will be managed. For each function, we urge the person responsible for the service to ask:

- does this organisation need to be impartial to perform this role?
- does or could this organisation develop the capability to perform this role effectively?

We also urge MoJ ministers and officials to consider the cross-cutting recommendations of this report (p. 7-10). Addressing risks early and developing professional capacity in this area is an essential prerequisite of success in this complex area of government policy.

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[342] Interview with probation trust chief executive

[343] Interview with probation trust chief executive

Conclusion

Over the past 30 years, we have seen a major transformation in the way public services are delivered. Users now have a greater say in who they receive public services from, and organisations from the public, private and voluntary sector compete for the right to provide these. The assumption is that competing, independent organisations will be able to deliver a better service at a lower cost. This has indeed proved to be the case in some areas – facilities management, waste collection and schools catering to name a few. But too often we have seen government overestimate the extent to which markets in public services are 'self-managing', leading to undesirable outcomes for citizens and taxpayers.

The most important lesson we have drawn from our research is the need for government to see itself as a 'steward' of markets in public services. This necessitates an active role in setting the 'rules' and incentives for actors in the system, as well as the willingness to adjust them if they prove ineffective. The need for such a role is only likely to increase given far-reaching reforms currently underway in more challenging and complex services such as probation and health.

This requires:

- building capabilities in new areas
- developing strategies to mitigate the inherent risks of using market mechanisms in certain services
- assigning the functions necessary to support effective oversight
- re-engineering the commissioning and procurement process to place greater emphasis on ongoing learning and adaption, collaboration with providers and co-ordination with related services.

This is by no means an exhaustive set of solutions and many more are offered in the main body of this report. We hope that the evidence and ideas highlighted will stimulate the improvement in government's oversight of public service markets that is urgently needed.

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