

2020 Public Services Trust
at the RSA

Better Outcomes



Lauren M. Cumming, Alastair Dick, Lord Geoffrey Filkin, Gary L. Sturgess

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About the 2020 Public Services Trust

The 2020 Public Services Trust is a registered charity (no. 1124095), based at the RSA. It is not aligned with any political party and operates with independence and impartiality. The Trust exists to stimulate deeper understanding of the challenges facing public services in the medium term. Through research, inquiry and discourse, it aims to develop rigorous and practical solutions, capable of sustaining support across all political parties.

In December 2008, the Trust launched a major new **Commission on 2020 Public Services**, chaired by Sir Andrew Foster, to recommend the characteristics of a new public services settlement appropriate for the future needs and aspirations of citizens, and the best practical arrangements for its implementation.

For more information on the Trust and its Commission, please visit www.2020pst.org.

The views expressed in this report are those of the authors and do not represent the opinion of the Trust or the Commission.

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2020 Public Services Trust at the RSA
8 John Adam Street
London WC2N 6EZ

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Contents

Authors	5
Acknowledgements	6
Foreword	10
Executive Summary	12
1 Introduction	16
2 What is outcome commissioning?	19
The outcome commissioning strategy	19
Means of commissioning outcomes	21
Outcome commissioning as a performance management tool	24
3 Why outcome commissioning?	25
Achieving better outcomes in a constrained fiscal environment	25
The reasons for poor outcomes of public services	27
How can outcome commissioning lead to better outcomes?	28
Summary	29
4 Outcome commissioning in action	30
Streetscene	30
Welfare to Work	31
Long term condition management	32
Foster care in the United States	33
Value-based drug purchasing	35
Summary	36
5 The outcome commissioning process	37
Selecting the outcomes	38

<i>Departmental Silos</i>	39
<i>Observable and measurable outcomes</i>	41
<i>Target population</i>	41
<i>Duration</i>	41
Establishing the baseline	42
<i>New services</i>	42
<i>Rapidly changing circumstances</i>	42
Developing a theory of the service	43
<i>Understanding the linkages</i>	43
<i>Extraneous variables</i>	43
<i>Co-production</i>	45
<i>Controlled environment</i>	45
Managing the process over time	45
<i>Gaming</i>	45
Summary	46
6 Transitioning to outcome commissioning	48
‘Big Bang’	48
Staged implementation	49
Summary	51
7 The Way Forward	52
Rethinking state action from outcomes	53
A model for paying for outcomes	53
Where to begin to implement outcome commissioning	54
<i>Previously piloted services</i>	55
<i>Services where outcome commissioning should be a priority</i>	56
<i>Services where outcome commissioning has the potential to drive better outcomes, but where further study by practitioners is required</i>	58
8 Conclusion	60
Appendix	62
References	64

Authors

This study was undertaken by Lauren M. Cumming, Alastair Dick, Lord Geoffrey Filkin and Gary L. Sturgess.

Lauren is a Researcher to the Commission on 2020 Public Services. Prior to working for 2020, she was a research assistant at The Serco Institute, publishing a briefing paper on behavioural economics and public service contracting, and conducting research comparing education markets in six OECD countries. Lauren has a Masters in International Security from Sciences Po Paris and an MSc in International Political Economy from the London School of Economics.

Alastair is the Honorary Treasurer of the 2020 Public Services Trust. He is a senior manager at Serco where he has held a number of roles developing new strategies for public service delivery. Prior to joining Serco, Alastair was a Fulbright Scholar at Harvard Business School and held strategy roles within the UK Labour Party and the Boston Consulting Group.

Geoffrey is the Chair of the 2020 Public Services Trust which he founded in 2008. He has worked as a manager of services, as a Chief Executive and then as Secretary of the Association of District Councils where he helped create key policies for local government, including Best Value. He was one of the founders of the New Local Government Network in 1996 and founded the Parliament Choir in 2000. From 2001-2005 he was a government minister. He is currently Chairman of the Merits Committee in the Lords, of St Albans Cathedral Music Trust, of the Parliament Choir, a trustee of other charities and an adviser to several companies.

Gary has been Executive Director of The Serco Institute since January 2003, driving its research and publication agenda. He played a key role in the establishment of the Public Services Strategy Board at the Confederation of British Industry and is former Cabinet Secretary in the New South Wales state government in Sydney, Australia.

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Project sponsor

- Partnerships UK

Commissioner project lead

- Lord Geoffrey Filkin

Advisory Board members

- David Behan, Director General for Social Care, Local Government and Care Partnerships, Department of Health
- Andrew Cozens, Strategic Adviser for Children, Adults and Health Services, Improvement and Development Agency (I&DeA)
- Seb Elsworth, Director of Strategy, ACEVO
- Rebecca Harrington, Assistant Director, Housing and Adult Social Care, London Borough of Camden
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- Ian Keys, Managing Partner, Gradus Consulting
- Andrew Mckeon, Managing Director Health, Audit Commission
- Azad Ootam, Director Commercial and Services, UK Border Agency
- Greg Parston, Director, Accenture Institute for Health and Public Service Value, Accenture
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- John Tizard, Director, Centre for Public Service Partnerships, University of Birmingham
- Nigel Walker, Director, Creative Commissioning

Corporate Advisors

Amey

- Nick Sharman, Managing Director - Local Government
- Derek Stewart, Development Director - Local Government
- Christopher Wong, Development Consultant

Capgemini

- Graham Colclough, Vice President, Global Public Sector
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- Robin Vasudeva, Vice President, Finance Transformation and Performance Management

Ernst & Young

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- Richard Lewis, Director, Health Advisory Practice

KPMG

- Alan Downey, UK Head of Healthcare
- Neil Sherlock, Partner, Public Affairs

Neil Stewart Associates

- Neil Stewart, Chair and Chief Executive

Partnerships UK

- James Stewart, Chief Executive Director
- David Harrison, Project Director, Partnerships UK

Pinnacle

- Barry Simons, Board Member

PricewaterhouseCoopers

- Nick Jones, Global Director, Public Sector Research Centre
- David Padwick, Director, Procurement - Government & Public Sector

Case studies

Benefits Based funding

- Ian Pretty, Vice President - NL Public & Health, Global Public Sector, Capgemini

Camden mental health

- Miia Chambers, Social Investment Manager, London Borough of Camden
- Milla Gregor, Outcomes Programme Manager, London Borough of Camden
- Rebecca Harrington, Assistant Director, Housing and Adult Social Care, London Borough of Camden

Employment Zones, Pathways to Work and Flexible New Deal

- Alan Cave, Delivery Director, Work, Welfare and Equality Group (WWEG), Department of Work and Pensions
- Lord David Freud, Shadow Minister for Welfare, House of Lords
- Mike Hope, Delivery Directorate Senior Analyst, Department of Work and Pensions
- Richard Johnson, Managing Director, Serco Welfare to Work
- Amanda McIntyre, Director, Employment Related Services Association
- Jane Mansour, Director, Ingeus Centre for Policy and Research
- Jenny Ross, Manager, Ingeus Centre for Policy and Research
- Sean Williams, Development Director, Serco Welfare to Work

Failed asylum seeker and illegal migrant removal

- Azad Ootam, Director Commercial and Services, UK Border Agency

Foster care

- Peter May, Researcher, The Serco Institute

Long term condition management

- Mike Sadler, Chief Operating Officer & Medical Director, Serco Health
- Alexis Sotiropoulos, Researcher, The Serco Institute

Offender management

- David Griffiths, Head of Offender Management System Strategy, Ministry of Justice
- Julie Taylor, Director of Offender Management Strategy, Criminal Justice Group, Ministry of Justice

Value-based drug purchasing

- Alexis Sotiropoulos, Researcher, The Serco Institute

Social care

- David Behan, Director General for Social Care, Local Government and Care Partnerships, Department of Health
- Janet Walden, Head of Personalisation and Innovation for Social Care, Local Government and Care Partnerships, Department of Health

Streetscene

- Robin Davies, Marketing Director, Serco Government Services

Report preparation

- Maria Athanassiou, Capgemini and Heidi Hauf, 2020 Public Services Trust (administrative support)
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Foreword

Many people have spent their careers struggling with how to improve public services and which policy context is most likely to make this happen.

Compulsory competitive tendering (CCT) was one such policy. In the 1980s and 1990s local authorities were forced by central government to put various services out to competition. For many in local government the experience was a revelation of the power of the threat of competition to drive change and productivity.

But CCT became exhausted as a policy, not least because it promoted competition purely on input costs, as most procurement processes still do. Reducing the costs of inputs has value, but if the problem is how better to convert inputs to outcomes, then competition around the costs of the inputs will not solve it.

Reflecting on this led me to argue for a system which incentivised outcomes by paying for them and so creating powerful drivers for innovation. I set out this argument in a chapter I wrote, “Better Outcomes”, for the book *Public Matters* in 2007.

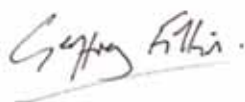
That same year we decided to found 2020 Public Services Trust to explore key issues about the role, form and performance of publicly-funded action. The Commission on 2020 Public Services is the central project for the new charity.

Registering a charity, recruiting staff, raising £1 million and setting up the Commission under the Chairmanship of Sir Andrew Foster took Director Ben Lucas and me some time and effort but I was keen to go back to the question of how to pay for outcomes, not for inputs. I discussed this with James Stewart, Chief Executive Director of Partnerships UK, and was pleased and grateful when he and PUK offered to support the study.

I was then delighted when three extraordinarily capable people, Lauren Cumming, Alastair Dick and Gary Sturgess agreed to join the team. We have worked, debated argued and laughed our way through this project for nearly eighteen months. It has been an enjoyable project and my co-authors have put in enormous amounts of time for little reward and I am very grateful to them. That we have produced a short report is a consequence of wanting to make it accessible, not a reflection of the time given.

The report is one of a number of inputs to the Commission on 2020 Public Services. When I discussed the Commission with Francis Maude MP, I was heartened to find how central to his thinking this issue of paying for outcomes was; he has evidenced this by agreeing to speak at its launch.

I hope that the report, our input, can make a positive contribution. We urge politicians, policy makers and service managers to engage with these ideas and issues better to improve outcomes for the public.

A handwritten signature in black ink that reads "Geoffrey Filkin." The signature is written in a cursive style and is underlined.

Geoffrey Filkin

Chair of Better Outcomes Project

Chair and Founder, 2020 Public Services Trust

Executive Summary

At the heart of public sector reform is the question of how the state can get the best outcomes possible for the resources it allocates. Policy makers grappling with this have taken a range of approaches, from the targets culture of the early Blair years to the introduction of contestability and user choice. The results have been mixed. Some outstanding successes must be balanced against falling productivity in many areas and an increasing sense that the current delivery architecture cannot be relied on to deliver the desired outcomes.

The current fiscal environment has made this challenge even more critical. With enormous cuts in public expenditure required over the next ten years, the UK will need to become much more efficient at achieving its desired outcomes, or in many cases it will not be able to deliver them at all.

This report proposes a new approach, outcome commissioning. Outcome commissioning involves the state designing a system for delivery that incentivises the achievement of outcomes. This report has focussed on one way to do this, which involves transferring responsibility for the achievement of outcome goals to a delivery agency, whether public, private or voluntary, and holding this agent firmly to account for these outcomes. In other words, the state ceases to focus on the *how* and instead focuses primarily on defining the *what*, then pays for performance rather than processes.

Outcome commissioning has been piloted and in some cases rolled out in a number of areas, with increasing success. In Welfare to Work, the UK has tested the approach through Employment Zones and more recently Flexible New Deal. These programmes require providers from the public, private and voluntary sectors to assume responsibility for returning unemployed to the workforce – and they are paid a proportion of the total payment when they achieve it. In local government, it has been used to reward a street cleaning service for achieving the outcomes that residents really care about.

There is considerable political interest in this new approach. Both the Labour and Conservative political parties have recognised its advantages. The Labour

Government has implemented outcome commissioning in Welfare to Work through the Employment Zones programme. The Conservative Party's recently published Green papers propose specifying outcomes and paying by results in areas as diverse as health and offender management.

The results to date of outcome commissioning pilot programmes suggest that outcome commissioning could lead to substantial improvements if it were used more widely.

The **introduction** of this report defines outcome commissioning and its key benefits:

- Clear definition of the outcomes sought
- Powerful and focused incentives to achieve them
- Full responsibility for their achievement to the service deliverer
- Innovation to find better ways to realise outcomes
- Freedom to personalise services

Section 2 describes the processes and strategy associated with developing a system of outcome commissioning and the various ways in which governments can achieve better outcomes. The strategy has five stages: identify the aspirations of citizens and their communities, specify these to a delivery agent, allocate resources, decide the best means to achieve outcomes and monitor and evaluate performance.

The best means to achieve outcomes may be through regulation, subsidies, citizen empowerment, or procurement from public, voluntary or private sector providers. The results of the evaluation stage should then lead to further refinement of the outcomes sought. This section also sets outcome commissioning in the context of other performance management tools and explains how it differs by simultaneously focusing on outcomes, not processes, and paying on performance.

Section 3 explains why outcome commissioning is an attractive option. It analyses why current performance in public service may be poor and how outcome commissioning could change this. By focusing on outcomes and paying providers when these are achieved, outcome commissioning can drive improvements in many different service areas.

Section 4 illustrates how outcome commissioning works through a series of case studies. It identifies the improvements in outcomes achieved and some of the strategies for overcoming the inevitable challenges of this approach.

Section 5 proposes a four stage process for commissioning outcomes: select the outcomes, establish the baseline, develop a theory of the service and manage the process over time. There are practical complexities to outcome commissioning. Outcomes can rarely be delivered within a ‘clean’ environment where the delivery agent has full control over all the factors necessary to succeed. Many areas of public service have extraneous variables or require the joining up of different funding streams and delivery silos. Sometimes the state may not be able to join up budgets and processes to make good commissioning possible, in which case less ambitious outcomes that do not require joining up may need to be chosen.

Section 6 explores the transition challenges and choices for implementing outcome commissioning. There may be no pre-existing market or delivery experience to help commissioners define contractual specifications. There may also be a risk of political embarrassment if results are too good (and result in super-profits) or outcomes are poor. Identifying these challenges up front to manage the risks and putting the right political leadership in place can help to ensure that these challenges are overcome.

Section 7 proposes areas where outcome commissioning could most fruitfully be applied, looking at significant public policy problems where a focus on outcomes may offer real efficiency benefits and quality improvements over the current approaches.

Areas where this approach has already been piloted include:

- Returning long term unemployed and Employment Support Allowance claimants to work
- Managing long term health conditions
- Ensuring safety and stability of children in foster care
- Improving street maintenance and cleaning

Areas where outcome commissioning should be a priority include:

- Improving health outcomes
- Increasing waste management and recycling
- Implementing effective punishment
- Reducing substance misuse
- Processing asylum claims
- Removing failed asylum seekers and illegal migrants

Areas where outcome commissioning has the potential to drive better outcomes, but where further study by practitioners is required, include:

- Reducing re-offending
- Improving literacy
- Implementing benefits based funding for a wide range of internal systems and processes

This list is only illustrative as there may be many other areas where outcome commissioning could drive improvements. It does, however, demonstrate the broad applicability of this approach to both front-line services and the improvement of government processes such as the efficiency of its internal systems.

This report argues that outcome commissioning represents a radical new way to address some public service delivery challenges. Many lessons for how to implement the approach can be learned from the case studies and will be crucial to fully understanding how outcome commissioning can address challenging societal issues, thereby driving dramatic improvements in outcomes.

1

Introduction

In April 2000, the UK Department of Work and Pensions began to trial a programme aimed at returning long term unemployed individuals to work. The Department commissioned independent providers to deliver employment counselling services in several regions of high unemployment.¹

“Employment Zones” is one of the earliest UK examples of outcome commissioning and illustrates the two main characteristics of this approach. First, the commissioner clearly specifies the outcomes the service is intended to achieve. In the case of Employment Zones, the Department pursued two outcomes: to return participants to work as quickly as possible and to ensure participants were sustained in employment for at least 13 weeks. Second, the commissioner incentivises the delivery of these outcomes by paying providers based on actual performance and not on promises. Outcome commissioning involves incentivising the achievement of outcomes by stipulating rewards for success and penalties for substandard performance. Employment Zones had two types of rewards: allowing providers to keep the saved unemployment benefit of participants who found work before 21 weeks, and giving additional payments if participants stayed in work for 13 weeks. The penalty took the form of the provider making a loss of as much as five weeks of unemployment benefit if they failed to return a participant to employment within 21 weeks.² These incentives ensured that providers were accountable for achieving the specified outcomes.

- 1 Hales *et al.*, *Evaluation of Employment Zones: Report on a Cohort Survey of Long-Term Unemployed People in the Zones and a Matched Set of Comparison Areas* (National Centre for Social Research, 2003): 6-7.
- 2 Hales *et al.*, *Evaluation of Employment Zones: Report on a Cohort Survey of Long-Term Unemployed People in the Zones and a Matched Set of Comparison Areas* (National Centre for Social Research, 2003): 8.

Outcome commissioning has clear benefits. The approach:

- increases certainty about the outcomes sought by citizens and communities and enables the state to communicate these clearly to service providers through a contractual or quasi-contractual mechanism;
- focuses incentives on achieving desired outcomes;
- gives responsibility for achieving outcomes to those who can most effectively achieve them, namely the providers of services;
- encourages innovation, since providers are incentivised to explore new ways to achieve better outcomes; and
- allows providers flexibility in the way they deliver their service tailoring it to local and personal constraints and preferences.

Both major political parties have recognised the advantages of outcome commissioning. In 2004, the Labour Government established NHS Foundation Trusts which are paid for the outputs they deliver instead of being given a budget based on the funds required for inputs such as staff and premises.³ While this is paying for outputs not outcomes, it represents significant progress. The Labour Government went further in the employment services sector, starting with “Employment Zones” in 2000.

The Conservative Party has also expressed interest in this approach. Their Green papers are peppered with references to the need to “pay these new providers by the results they achieve, so there’s a real incentive to improve.”⁴ They propose:

- “agreeing on goals and outcomes [with the voluntary sector], not dictating methods of delivery”,⁵
- “introducing payment-by-results within the [health] system”,⁶
- enforcing “Drug Rehabilitation Requirements by contracting with private and third sector organisations... and paying them by results”,⁷ and

3 Department of Health, *A Short Guide to NHS Foundation Trusts* (London: Department of Health, 2005): 5.

4 David Cameron, “The age of austerity,” 26 April 2009, accessed online at <http://www.conservatives.com/News/Speeches/2009/04/The_age_of_austerity_speech_to_the_2009_Spring_Forum.aspx>.

5 Conservatives, “A Stronger Society: Voluntary Action in the 21st Century,” *Responsibility Agenda: Policy Green paper No. 5* (London, 2009): 79.

6 Conservatives, “Delivering Some of the Best Health in Europe: Outcomes Not Targets,” *Responsibility Agenda: Policy Green paper No. 6* (London, 2009): 15.

7 Conservatives, “Prisons with a Purpose: Our Sentencing and Rehabilitation Revolution to Break the Cycle of Crime,” *Security Agenda: Policy Green paper No. 4* (London, 2009): 14.

- paying “Prison and Rehabilitation Trusts and private sector prisons... by results - with a premium awarded on a national tariff if the offender or ex-prisoner is not reconvicted within two years.”⁸

Why, then, given the support of the two main parties and the apparent benefits, has outcome commissioning not been more broadly applied? The challenges are considerable, ranging from the complex political and commissioning requirements to other more technical measurement issues. However, this report argues that it is worth studying these challenges and exploring ways to overcome them because outcome commissioning has the potential to create better outcomes and do so efficiently.

This report will:

- discuss the advantages of outcome commissioning;
- analyse the political and technical challenges of implementing this approach and offer potential means to address them;
- consider how to transition to an outcome commissioning approach; and
- propose areas where outcome commissioning might be applied.

8 Conservatives, “Prisons with a Purpose: Our Sentencing and Rehabilitation Revolution to Break the Cycle of Crime,” *Security Agenda: Policy Green paper No. 4* (London, 2009): 15.

2

What is outcome commissioning?

Outcome commissioning is the process by which the state designs and implements a system that incentivises the successful delivery of outcomes. There is some disagreement about the definitions of the terms inputs, outputs and outcomes. This report has adopted the following definitions.

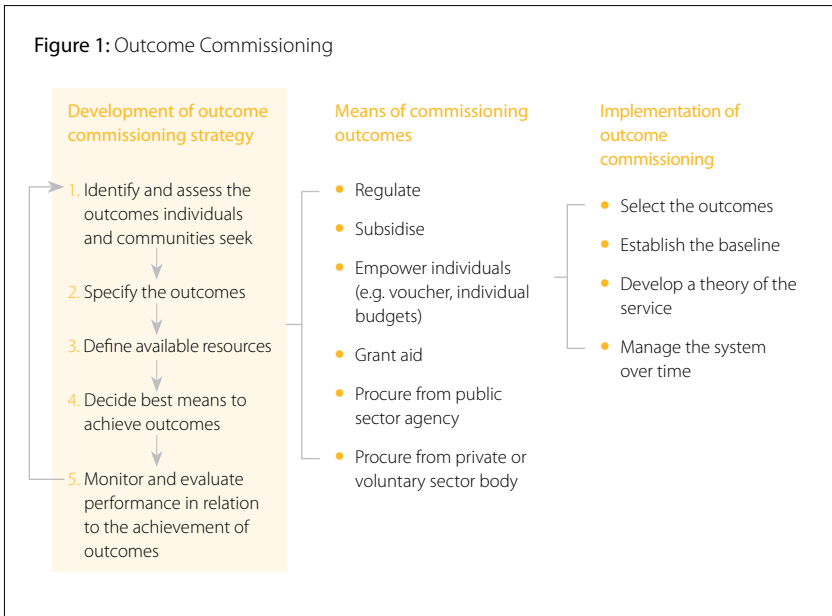
- *Inputs* are “the intervention[s] provided”; for example, an offender is provided with literacy training.
- *Outputs* are the “direct and tangible products from the activity”, such as the offender obtaining a literacy qualification or finding work upon release.
- *Outcomes* are the “changes that occur for stakeholders as a result of the activity”. The offender may, as a result of having a job, not re-offend.⁹

The outcome commissioning strategy

To better understand outcome commissioning it is important to clarify the meaning of the term “commissioning”. Some argue that all commissioning is about outcomes, and therefore the phrase “outcome commissioning” is redundant. However, as the research that informed this report made clear, most commissioning at present pays for inputs, which often have a weak and uncertain relationship to the outcomes. This report uses the term outcome commissioning to emphasise the radical distinction between the model of commissioning advocated here and that most commonly used at present.

9 Elizabeth Cox and Josh Ryan-Collins, “Sustainable Procurement and Commissioning – Overview,” *Whole Life Costing Working Group* (nef, 2008): slide 6.

Much valuable work has been done to understand the approach that must be taken in order to commission well, sometimes referred to as the “commissioning cycle”. This approach is illustrated in Figure 1. It involves five steps, beginning with identifying need, then specifying what must be done, allocating resources, deciding the best way to achieve the result and then evaluating performance.¹⁰ The results of the evaluation process should then re-inform whether or not the need is still present and the method is working well, and the cycle begins again.



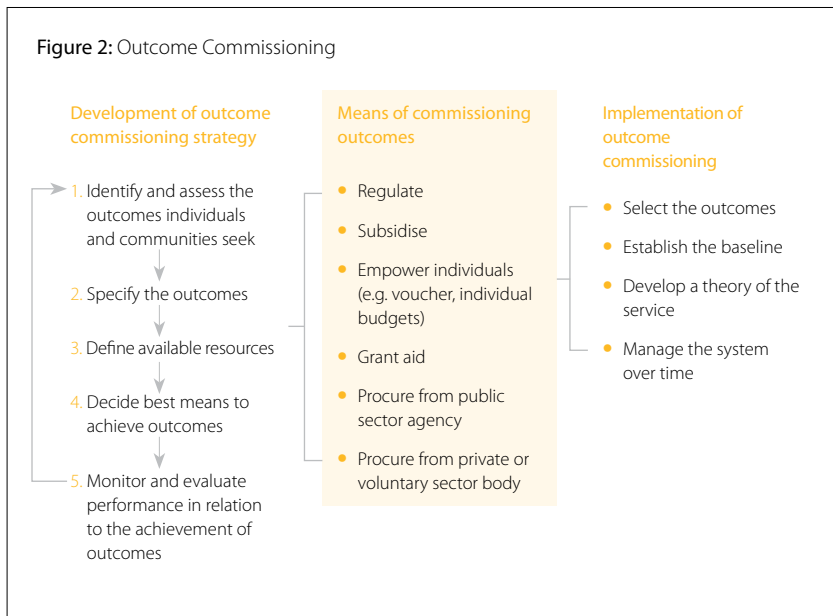
Outcome commissioning follows a similar pattern; however, at each stage of the process the focus is on the *outcomes* the commissioner seeks to achieve. Therefore, at the first stage, instead of assessing the services individuals and communities may need, the commissioner identifies the aspirations of the citizens for outcomes, such as cleaner streets, healthier individuals or less crime. Citizens will therefore play a critical role in defining the outcomes to be pursued. Individuals, families and communities know what is important to them and may

¹⁰ LGA and CBI, *Commissioning strategically for better public services across local government* (London: CBI, 2009): 9.

be best placed to prioritise goals. Commissioners will then need to find ways to ensure these outcomes are delivered. The commissioner then specifies this outcome and defines the resources available to achieve it. Next, she decides how the outcome is best achieved, using a variety of different means, including regulation, giving funds to individuals to empower them to achieve outcomes for themselves, grant-aiding or procurement. The final key distinction of outcome commissioning is that performance is monitored and evaluated in relation to the outcome specified rather than any specific processes used to try to achieve it. The commissioner knows exactly what has been achieved in terms of the outcome and takes further action on this basis.

Means of commissioning outcomes

There are many ways commissioners can achieve outcomes. Direct delivery of services is the most common but not the only method. A full evaluation should be made of the most efficient and effective means to deliver outcomes.



First, the state might regulate for outcomes. This could occur where society or the market has the potential to deliver outcomes similar to those desired by the state, without state funding. For example, certain gas and electricity suppliers in the UK are obligated to meet a carbon emissions reduction target in domestic properties, and are encouraged to do so through the most cost-effective means. This obligation contributes to outcomes related to both the Government's Climate Change Programme and Fuel Poverty Strategy.¹¹

Second, the state might subsidise for outcomes. Subsidies can encourage organisations to deliver more of the services they already provide, but they can also be used to incentivise organisations to achieve outcomes if part of the subsidy is made conditional on realising defined improvements in the outcome. For example, the Government has proposed that its goal of providing every household in the UK with high-speed internet access may be achieved partially through awarding subsidies to providers proposing to install “next generation broadband” to the final third of households that do not yet have access.¹²

Third, the state can give funds to individuals to purchase their own services, which empowers citizens to ensure outcomes are delivered for them personally. There are three common ways this occurs. Vouchers earmarked for the purchase of a specific type of service have become quite common in some countries and are used in Milwaukee, USA to give children in low-income families the choice of attending private school.¹³ Another form of voucher is where funding follows the individual, so that funds are never given to individuals but to the institutions they choose to attend. Since 1992, independent schools in Sweden have been funded based on the numbers of pupils enrolled.¹⁴ Finally, individuals can be given funds in the form of individual budgets, which gives them more freedom to purchase different kinds of services, within well-defined limits, as was piloted and is in the process of being rolled out for social care users in the UK.¹⁵ Giving funds to individuals can result in better targeted inputs, increased co-production, and potentially better outcomes.

11 Office of Gas and Electricity Markets, *A review of the first year of the Carbon Emissions Reduction Target* (London: Office of Gas and Electricity Markets, 2009): 1-2.

12 Department for Culture, Media and Sport and Department for Business, Innovation and Skills, *Digital Britain: Final Report* (Crown copyright, 2009):65.

13 Tony Hockley and Daniel Nieto, *Hands up for school choice!: Lessons from school voucher schemes at home and abroad* (London: Policy Exchange, 2004): 19.

14 Tony Hockley and Daniel Nieto, *Hands up for school choice!: Lessons from school voucher schemes at home and abroad* (London: Policy Exchange, 2004): 11.

15 Individual Budgets Evaluation Network, *Individual Budgets Evaluation: A Summary of Early Findings* (2007): 1.

Fourth, the state can pursue outcomes through grants, provided that there is an element of payment on performance, so that, for example, renewal of the grant is contingent on the achievement of certain outcomes. This implies the transformation of the grant into a contractual style of relationship. Embryonic forms of this type of grant-aiding are being developed in the voluntary sector and between different levels or departments of government.¹⁶ Government could also encourage proposals for outcome-based innovation grants. Providers could put forward new ways to achieve outcomes and, if the proposals had merit, government could award innovation grants, with payment for the achievement of the agreed outcomes.

Fifth, the state can procure outcomes from private or voluntary providers. Procurement involves identifying and selecting the providers of services,¹⁷ holding a competition, and developing, signing and managing a contract with those providers. Procurement thus becomes a key aspect of the commissioning process if used to achieve an outcome.

Finally, the state can procure from state-owned service agencies. The argument for paying for outcomes applies as much to the agencies that government itself owns as to private and voluntary sector organisations. However, outcome commissioning is not simply a new form of targets. Paying for outcomes requires the transfer of risk to providers and therefore a quasi-contractual relationship of some kind must be established. Commissioners will need to specify outcomes clearly and develop a framework for payment on performance in which the consequences for non-performance are firmly established in advance.

This report recognises that there is a place for each of these delivery models in achieving better outcomes. However, for reasons of focus, it examines just the last two of these approaches: the process by which an outcome is commissioned through procurement from a state or third-party agency. The report analyses the full process from the point at which a commissioning strategy is developed to procuring the achievement of the outcome from public, private or voluntary sector providers.

16 In the USA, the United Way of America has required the programmes they fund to identify and measure outcomes since 1996 (Michael Hendricks, Margaret C. Plantz and Kathleen J. Pritchard, "Measuring Outcomes of United Way-Funded Programs: Expectations and Reality," *New Directions for Evaluation* 119 (2008): 13.) In Australia, health care grants from the Commonwealth to the State governments specify health outputs and outcomes agreed by both parties which are monitored and reported annually during the period of the grant. (Commonwealth Department of Health and Ageing, *Public Health Outcome Funding Agreements (PHOFAs)* (Canberra: Commonwealth of Australia, 2002): 3-4.) While neither of these examples involves paying on performance, they are a step in the direction of pursuing outcomes through grants.

17 LGA and CBI, *Commissioning strategically for better public services across local government* (London: CBI, 2009): 9.

Outcome commissioning as a performance management tool

“To join interest with duty, and that by the strongest cement that can be found... is the object avowed to be aimed at by the act. The emolument of the Governor is to be proportioned in a certain way to the success of the management. Why? That it may be ‘his interest’ to make a successful business of it, ‘as well as his duty’.”¹⁸ – Jeremy Bentham, 1791, commenting on the Hard Labour Act

As early as 1786, Jeremy Bentham proposed a system of payment for outcomes for a new national penitentiary. Bentham was later given a draft contract and a substantial advance for the design, construction and management of the prison, under which he would have been paid a sum for the care of each inmate, and financially penalised based on escapes, deaths in custody, and re-offending.

Outcome commissioning is not new. It builds on a long history of public sector performance management and it is helpful to place this approach within the evolution of thinking about public management. In recent decades various techniques have been developed, including performance budgeting, performance contracting, targets, Public Service Agreements, Payment by Results and performance regulation.¹⁹

In general, most performance management techniques take one of two approaches but rarely both: they specify outcomes or they pay on performance. For example, performance contracting involves paying on performance, but specified as inputs or outputs, not outcomes. On the other hand, Public Service Agreements in the UK are outcome-focused but do not involve payment on performance (which would anyway be inappropriate at the departmental level and useful only at the level of the delivery agency). These tools help the state to incentivise the delivery of inputs and outputs, or monitor the achievement of outcomes but with limited consequences. Outcome commissioning seeks to integrate outcome specification and payment on performance into a single approach – making payment on delivery of outcomes. It matters because despite repeated efforts to improve public services, in many cases public expectations are still not being fulfilled.

18 Jeremy Bentham, ‘Panopticon, Postscript, Part II’ [1791], in John Bowring (ed.), *The Works of Jeremy Bentham* (Edinburgh: William Tait, 1843): Volume iv, 125-126.

19 The Serco Institute, *Public Sector Reform: An International Overview* (Hong Kong: Efficiency Unit, 2007): 16-19.

3

Why outcome commissioning?

Achieving better outcomes in a constrained fiscal environment

Over the last decade the UK has hugely increased the resources that it devotes to public services.²⁰ This increase has resulted in some improvements in public services, but not as much as had been hoped given the extent of increased funding. The UK now faces an intense fiscal squeeze so it is essential to find better ways to deliver improvements in outcomes.

It is easy to criticise the public sector for not improving public services dramatically without recognising the reasons it is challenging to do so. Public services are inherently difficult to deliver because of the diversity of the stakeholders they serve and government's need to demonstrate probity and fairness. The issues public agencies must resolve are most challenging, involving complex societal interactions and the need to address ethical and equitable sensitivities. While a private business can identify its goals of growth and profitability with relative ease, it is much more difficult for a public agency serving a diverse array of stakeholders, often with conflicting needs. The complexity of the challenge the public sector faces usually makes it impossible to focus service delivery exclusively on efficiency.

However, recognising this difficulty does not imply an acceptance of poor outcomes. This challenge lies in improving public sector delivery within these constraints.

The news is not all bad. Significant improvements in the quality of public services have been made in recent decades. British Crime Survey shows crime is down 48% since 1995 and was at its lowest level in 2008 since the survey was first published in 1981.²¹ Waiting times for elective surgery in the NHS have fallen

²⁰ Institute for Fiscal Studies, *Spending by function*, accessed online at <http://www.ifs.org.uk/ff/rr_spending.xls>.

²¹ Chris Kershaw, Sian Nichols and Alison Walker, *Crime in England and Wales 2007/08* (London: Home Office, 2008): 2.

substantially, with most patients being treated within three months and virtually none waiting longer than 12 months.²²

However, public services are still not producing the outcomes desired. Recidivism rates for offenders are still high.²³ Optimism about the future of the NHS dropped from 47% in spring 2000 to 17% in summer 2009.²⁴ Despite the achievement of delivery targets in many services, public satisfaction with public services has remained unchanged,²⁵ and failure of services to achieve desired outcomes may be affecting the public's willingness to fund them: in April 1997 more than three-quarters of respondents thought government services such as health, education and welfare should be extended, even if it meant some increases in taxes; by June 2009 that figure had fallen to less than half.²⁶

In spite of a massive increase in spending, public service productivity, the rate of conversion of inputs to outputs, declined by 3.4% between 1997 and 2007, suggesting that increased investment was associated with a decline in social savings.²⁷ Increasing the investment in public services may be a necessary but not a sufficient condition for improving service quality.

Moreover, the state now faces a fiscal crisis. As a result of the recession, GDP is forecast to fall by 3.5% in 2009²⁸, creating a simultaneous reduction in tax revenue and an increase in state liabilities that is contributing to a surge in state borrowing.²⁹ By 2013-14, public sector net debt will reach 79% of GDP.³⁰ The Institute for Fiscal Studies estimates that to balance the current budget by 2015-16 would require either raising taxes by £1,250 per family, a five-year real freeze in total public spending, or a combination of the two.³¹ The challenge is therefore absolutely clear: government will need to either significantly raise taxes or cut public services, unless

22 Sofia Dimakou, David Parkin, Nancy Devlin and John Appleby, "Identifying the impact of government targets on waiting times in the NHS," *Health Care Management Science* 1 (2009): 2.

23 In 2007, 39% of adult offenders re-offended in the first year after their release. (Ministry of Justice, *Re-offending of adults: Results from the 2007 cohort* (London: Ministry of Justice, 2009): 9.) Fifty-eight percent of those prisoners released in 1997 were reconvicted within two years, and this figure was much higher for certain groups such as males aged 18-20 (72%). (Social Exclusion Unit, *Reducing re-offending by ex-prisoners* (London: Social Exclusion Unit, 2002): 5.)

24 Ipsos MORI, *Public Perceptions of the NHS: Spring 2006 Tracking Survey* (June-July 2006): 9; Ipsos MORI, Ipsos MORI Public Spending Index, 2009: slide 18.

25 Cabinet Office: The Prime Minister's Office of Public Service Reform, *Customer Satisfaction with Key Public Services* (November 2004): 1.

26 Ipsos MORI, *Ipsos MORI Public Spending Index*, 2009: slide 12.

27 Office for National Statistics, *Total Public Service Output and Productivity*, 2009.

28 HM Treasury, *Budget 2009: Building Britain's Future* (London: The Stationary Office, 2009): 2.

29 Jobcentre Plus will receive an additional £3 billion to ensure everyone who needs it will have access to quality help to get back to work (HM Treasury, *Budget 2009: Building Britain's Future* (London: The Stationary Office, 2009): 7).

30 HM Treasury, *Budget 2009: Building Britain's Future* (London: The Stationary Office, 2009): 19.

31 Robert Chote, Carl Emmerson, Gemma Tetlow, "Budget 2009: Tightening the Squeeze?" *IFS Briefing Note BN83* (2009): 10.

it can find ways to deliver the same public services more efficiently. This report argues that the solution to this dilemma lies in part in a fundamental re-thinking of the way in which public services goals are pursued.

The reasons for poor outcomes of public services

There are many reasons why public services are failing to deliver desired outcomes. The solutions to deeply entrenched social problems are often complex. The outcomes the public expects the state to deliver are inherently difficult to achieve because they often require not only high quality services but also behavioural change on the part of service users, cooperation within communities, a benign external environment and a variety of other factors beyond the control of politicians and public servants. Moreover, the bar continues to rise as the public's expectations of services increase over time.³² However, there are also aspects of the current architecture of public service delivery that contribute to poor outcomes.

Discussing welfare delivery agencies, Tony Butcher identifies four criticisms of the current model of public service delivery that help to explain why the outcomes of public services are sometimes poor. Although some structural reforms have been made since this book was published in 2002, the basic arguments are still applicable.

First, delivery agencies are often inefficient and wasteful.³³ In 2001, a senior Department of Health official claimed that at least one-sixth of the NHS's annual budget was lost through inefficiency.³⁴

Second, delivery organisations are “provider dominated and driven by the needs and wants of providers of services – welfare bureaucrats and professionals – rather than by the needs and wants of the users of those services.”³⁵ Julian Le Grand nuances this view, arguing that the behaviour of public service professionals, whether they act in their own self-interest as knaves or in the interests of others as knights, depends on their context, the “policy structures” in which they operate.³⁶

Third, delivery agencies are generally seen as not being “close” to their “customers”; that is, services are not sufficiently tailored to individual needs and

32 Paul Flatters and Michael Wilmott, *Drivers for Change: Citizen demand in 2020* (London: 2020 Public Services Trust, 2009).

33 Tony Butcher, *Delivering Welfare* (Buckingham: Open University Press, 2002): 8.

34 Tony Butcher, *Delivering Welfare* (Buckingham: Open University Press, 2002): 9-10.

35 Tony Butcher, *Delivering Welfare* (Buckingham: Open University Press, 2002): 11.

36 Julian Le Grand, *Motivation, Agency, and Public Policy: Of Knights & Knaves, Pawns & Queens* (Oxford: Oxford University Press, 2003): 40.

desires.³⁷ Osborne and Gaebler also argued that because public agencies are not funded by their customers, they are “customer-blind”.³⁸

Finally, there is a concern about a lack of accountability of delivery agencies and their staff. Osborne and Gaebler argued that monopoly providers have no incentive to be accountable to their customers.³⁹

While it is important to recognise the inherent difficulty, the commissioning and delivery of public services needs to be transformed in order to achieve better outcomes. Increased efficiency, responsiveness, accessibility and accountability would all help improve outcomes. Outcome commissioning is one way of making improvements across these four dimensions.

How can outcome commissioning lead to better outcomes?

Outcome commissioning is only beneficial insofar as it helps the state to better achieve its objectives. It has the potential to do so in three main ways.

First, outcome commissioning ensures that providers pursue the outcomes that are important to users rather than specifying inputs or outputs that may not ultimately lead to outcomes.

Second, outcome commissioning creates powerful incentives so that the most important goal of providers is to deliver the outcomes specified by commissioners. Paying on performance increases the incentive to achieve outcomes, even if only a small percentage of the total payment depends on the delivery of outcomes. Providers, if paid on achieving outcomes, have an incentive to deliver them. Payment on performance also helps address the criticism that providers are not accountable for their actions, since providers that do not deliver outcomes or cannot provide evidence of having done so are not paid some or all of their remuneration.

Third, by paying for outcomes rather than prescribing processes, commissioners give providers flexibility to use the inputs that work best, the incentive to innovate to improve quality and value for money and the scope to personalise services for individual users to improve the service experience and use resources more effectively. This means services are likely to be more responsive to users’ needs, since providers will be more willing to respond to customer feedback if it means they will achieve more outcomes.

37 Tony Butcher, *Delivering Welfare* (Buckingham: Open University Press, 2002): 13.

38 David Osborne and Ted Gaebler, *Reinventing Government* (Reading: Addison-Wesley Publishing Company, Inc., 1992): 167.

39 David Osborne and Ted Gaebler, *Reinventing Government* (Reading: Addison-Wesley Publishing Company, Inc., 1992): 167.

Summary

This section has demonstrated the need to find ways to improve the outcomes of public services and showed that outcome commissioning is one possible way to achieve this. The next section describes several examples of outcome commissioning already in practice, explaining how agreements were structured, noting the challenges commissioners and providers faced and evaluating the impact of the approach.

4

Outcome commissioning in action

A wide variety of services are trialling outcome commissioning and their experiences suggest the potential for substantial service improvements and provide important insights into how to approach future roll-out. The following case studies reveal valuable insights into the process of commissioning outcomes, the potential pitfalls and ways of overcoming challenges.

Streetscene

In recent years, local authorities in the UK have begun to improve the ‘liveability’ of their communities by focusing on the quality of outdoor public spaces. In some municipalities, this has resulted in the integration of council functions that were previously fragmented across different teams and between different providers – litter and street cleaning, refuse collection, vandalism, roads and pavements, public conveniences. ‘Streetscene’, as these integrated services are now known, is concerned with public spaces that have been called ‘the living room of the community’.

In 2003, the Borough of Woking elected to commission its streetscene services from a private company, on an outcomes basis. Under the contract, the provider is paid a base fee and has the potential to receive a performance-related payment based on the level of public satisfaction, measured on a quarterly basis by an independent research firm. The contract delivered demonstrable improvements in public satisfaction – from 65% to 80% within the first year or two. Measurement of outcomes has resulted in greater flexibility in the allocation of resources, so that localities are cleaned when needed, and not according to a pre-determined roster.⁴⁰

⁴⁰ Giorgia Iacopini, *The Word on the Streetscene: Transforming Local Neighbourhoods* (London: New Local Government Network, 2009): 60-61.

Among other things, commissioning for outcomes has forced providers to study the drivers of public satisfaction, recognising that in different local authorities, different factors cause concern. This, in turn, influences service design. For example, in one local authority, potholes were causing a high level of dissatisfaction among local residents, and yet when the contract was first designed, commissioners had not intended to include pothole filling amongst the group of commissioned services.

Welfare to Work

The Department of Work and Pensions has been driving innovation in outcome commissioning over the last 10 years, and “Employment Zones”, discussed above, is just one of the programmes it has commissioned on an outcomes basis.

“Pathways to Work”, introduced in 2003, aimed to address the spiralling number of individuals claiming Incapacity Benefit (now Employment Support Allowance) and led to the establishment of “Provider-Led Pathways” in 60% of the country.⁴¹ Providers now deliver Work Focused Interviews and are incentivised through outcome-based contracts to get claimants back into work. Providers are paid 30% of the total possible payment up-front, 50% when a claimant achieves 13 weeks employment and the final 20% when an individual has remained in work for 26 weeks.⁴² Pathways is currently the most heavily outcome-weighted programme in the UK to date, although “Flexible New Deal”, another programme run by the same department, is scheduled to overtake Pathways in this regard around February 2011.⁴³ Although Pathways has experienced some difficulties because the way in which it was procured put enormous pressure on the supply-side and there is uncertainty about whether it is achieving outcomes, it has delivered innovations in several areas and studying the perceived problems in the Pathways contracts provides valuable lessons for how outcome commissioning might be applied to reducing the number of Employment Support Allowance claimants in the future.⁴⁴

41 Katharine Nice, Jacqueline Davidson and Roy Sainsbury, *Provider-led Pathways: Experiences and views of early implementation* (Norwich: Department of Work and Pensions, 2009): 9.

42 Katharine Nice, Jacqueline Davidson and Roy Sainsbury, *Provider-led Pathways: Experiences and views of early implementation* (Norwich: Department of Work and Pensions, 2009): 11.

43 House of Commons Work and Pensions Committee, *DWP's Commissioning Strategy and the Flexible New Deal: Government Response to the Committee's Second Report of Session 2008-09* (London: The Stationary Office Limited, 2009): 6.

44 No quantitative performance studies of Provider-led Pathways were available when this report went to print, but a qualitative study noted that “the prevailing view from Contract Managers and TPPMs in most districts was that targets were set unrealistically high given the harder-to-help nature of the client group, and were therefore not being met. This was well illustrated by a Contract Manager who explained how one provider was getting more people into work than other providers, but because their targets were set even higher than others' this achievement was not reflected in their overall performance. There was a feeling that providers had been ‘set up to fail’ because the Department had not adequately scrutinised the targets submitted in providers' bids.” Katharine Nice, Jacqueline Davidson and Roy Sainsbury, *Provider-led Pathways: Experiences and views of early implementation* (Norwich: Department of Work and Pensions, 2009): 36.

“Flexible New Deal” is a new programme that introduces outcome incentives at the national level. It is designed to help the 174,800 long term unemployed benefits claimants back into work.⁴⁵ The Department requires people who are unemployed for more than 12 months to be referred to private, voluntary and smaller scale public sector providers operating the programme. It is thought that these providers will be better able to tailor their approaches to provide personalised services, which is hoped will improve the success rate.⁴⁶ These providers will be paid based on the number of unemployed they get back into “sustainable employment”, represented by working for 26 weeks.⁴⁷ When the programme was originally created, it was based on paying providers 20% of the total possible payment up-front, with 80% based on clients achieving sustainable employment. However, due to the recession, this has been changed to a 40% up-front payment with 60% outcome-based for the first 18 months of the programme, which began in the last quarter of 2009.⁴⁸ This demonstrates one of the challenges of outcome commissioning, extraneous variables, which is discussed in the section “Developing a theory of the service”. Flexible New Deal is too new for there to be evidence of its impact, but both the Department and providers are hopeful of the potential it offers for innovation and achieving better outcomes.

Long term condition management

Long term conditions such as diabetes, chronic obstructive pulmonary disease, heart disease, asthma, arthritis and dementia affect 17.5 million people in the UK and generally have been treated reactively and episodically through the use of secondary care services like hospitals.⁴⁹ They are therefore quite costly. According to the Department of Health, 30% of all people say they suffer from a long term condition and account for 72% of all inpatient bed days.⁵⁰ The Department of Health estimates that treatment and care of those with such conditions account for 69%, or almost £70 billion, of the total health and social care spend in England.⁵¹

45 Centre for Economic and Social Inclusion, “Labour Market Statistics: October 2009,” accessed online at <<http://www.cesi.org.uk/statistics/>>. Note that the total number of long term unemployed adults was 419,000 as of October 2009, but only 174,800 of these were benefit claimants.

46 Ian Mulheirn and Verena Menne, *The Flexible New Deal: Making it Work* (London: The Social Market Foundation, 2008): 8-9.

47 Ian Mulheirn and Verena Menne, *The Flexible New Deal: Making it Work* (London: The Social Market Foundation, 2008): 15.

48 House of Commons Work and Pensions Committee, *DWP’s Commissioning Strategy and the Flexible New Deal: Government Response to the Committee’s Second Report of Session 2008-09* (London: The Stationary Office Limited, 2009): 6.

49 Department of Health, *Supporting People with Long Term Conditions*, January 2005: 5.

50 Department of Health, *Raising the Profile of Long Term Conditions Care: A Compendium of Information*, January 2008: 15.

51 Department of Health, *Raising the Profile of Long Term Conditions Care: A Compendium of Information*, January 2008: 18; Department of Health, *Departmental Report 2009*, June 2009: 215.

Several outcome-based approaches to better managing long term conditions in the community have been piloted in the UK and the USA, but these are primarily oriented toward tracking outcomes; providers do not take on the risk of delivering outcomes, but simply monitor results. These pilots have sought primarily to decrease patient hospital utilisation through a variety of approaches. Patient hospital utilisation is a proxy measure for cost to the healthcare system and the frequency and severity of acute healthcare incidents. This measure is often combined with data on mortality/morbidity and patient satisfaction to ensure quality is maintained.

Assessments of these pilots have revealed mixed results. A study of a pilot using advanced nurse practitioners as case managers providing care to the frail elderly in their homes looked at emergency admissions, emergency bed days, and mortality but found that case management had no significant effect on admission as compared with the rest of England.⁵² However a similar model using community matrons to help care for those with long term conditions such as heart failure and diabetes was found to reduce emergency hospital admissions by 26%, accident and emergency attendances by 16% and visits to primary care and other health services by up to 57%.⁵³ Finally an interim evaluation of a pilot using telehealth to manage patients suffering heart failure, Chronic Obstructive Pulmonary Disorder and/or diabetes found that the programme decreased hospital admissions by 48%, accident and emergency admissions by 53% and GP visits by 32%.⁵⁴

Foster care in the United States

In both the UK and the USA, the state has a duty to protect children from abuse and neglect and intervenes when such cases are detected, sometimes by placing children in foster care. Foster care is a short term intervention and is widely accepted as being inadequate in meeting the physical, social and emotional needs of children in the medium and long term. Those children who do not find a permanent home tend to encounter problems later in life, typically committing more crime per capita, spending more time in jail and receiving proportionally high welfare assistance as adults.⁵⁵ As such, temporary foster care arrangements carry substantial social and financial costs.

52 Hugh Gravelle *et al.*, "Impact of case management (Evercare) on frail elderly patients: controlled before and after analysis of quantitative outcome data," *British Medical Journal* 334 (2007): 31-34.

53 Serco, "Newham Community Matrons," 2009, accessed online at <http://www.serco.com/markets/health/community/Copy_of_index.asp>.

54 OwnHealth Birmingham, *Successes and learning from the first year* (Birmingham East and North Primary Care Trust, NHS Direct, Pfizer Health Solutions: 2007): 26.

55 Erwin A. Blackstone *et al.*, "Privatizing adoption and foster care: Applying auction and market solutions," *Children and Youth Services Review* 26 (2004): 1034.

In both foster care and adoption services, the essential desired outcome is the same: the identification and arrangement of safe, permanent homes for children.

In recent years there has been a shift to outcome commissioning in foster care and adoption services. In the US, such commissioning has taken place at two levels, between the federal government and the states and also between the states and private and voluntary sector organisations – so both states and their agents have had financial incentives to deliver outcomes. In 2000, the US federal government developed Child and Family Service Reviews (CFSRs) which measure state performance in terms of certain outcomes.⁵⁶ The states then specify these outcomes when commissioning services from the public, private and voluntary sectors.

The second round of CFSRs, which began in 2007, uses three measures: safety, permanency and child and family well-being. This combination of outcomes is important since using only one could lead to poor outcomes for children, such as placing them with adoptive families that have not undergone the appropriate approval procedures. The three main measures are then broken down into seven more specific outcome measures.⁵⁷ In addition there are seven systemic measures verifying capacity to meet these outcomes, such as the effectiveness of computer systems.⁵⁸ If a state has not achieved the required outcomes financial penalties are accrued against non-conformance with the 14 factors. Penalties can run into millions of dollars.⁵⁹

There is evidence that outcome commissioning between states and private and voluntary sector organisations has improved outcomes. A pilot using outcome commissioning in Florida resulted in a decrease in the average stay in foster care from about 20 months to 13 months and a doubling of the number of adoptions in a year from 20 to 40.⁶⁰ In Illinois, adoptions rose by 94%. In the period 1988-1997, 2-4% permanency was the norm; this rose from 12% to 23% from 1997, when outcome commissioning was introduced, to 2003.⁶¹ The rise in the permanency measure concurrently with the rise in the rate of adoption indicates that providers were not simply 'dumping' children in inappropriate adoptive homes.

56 Children's Bureau, "Children and Family Services Review: Fact Sheet," accessed online at <<http://www.acf.hhs.gov/programs/cb/cwmonitoring/recruit/cfsfactsheet.htm>>.

57 Children's Bureau, "Children and Family Services Review: Fact Sheet," accessed online at <<http://www.acf.hhs.gov/programs/cb/cwmonitoring/recruit/cfsfactsheet.htm>>.

58 Jim Novell, "Everything You Wanted To Know About the Federal Child and Family Services Review," accessed online at <<http://courts.michigan.gov/scao/services/cws/CFSRArticleWinter08Newsletter.pdf>>.

59 United States General Accounting Office, *Child and Family Services Reviews: Better Use of Data and Improved Guidance Could Enhance HHS's Oversight of State Performance* (Washington, DC: United States General Accounting Office, 2004): 7.

60 Lisa Snell, "Child-welfare Reform and the Role of Privatization," Reason Policy Study 271, 2000, accessed online at <<http://reason.org/files/60dbb93a64832e8624f4e2116383a0b0.pdf>>.

61 Erwin A. Blackstone *et al.*, "Privatizing adoption and foster care: Applying auction and market solutions," *Children and Youth Services Review* 26 (2004): 1040-1.

Value-based drug purchasing

A recent pricing innovation for pharmaceutical products has seen purchasers and pharmaceutical companies negotiating contracts that pay the manufacturer only in the event that the product provides the promised value to the patient. This has largely arisen from increased scrutiny of sharply rising health expenditures by funders and insurers. In the UK, several such agreements have been reached between the NHS and pharmaceutical companies, and insurance firms in the US are beginning to demand similar contracts.

One of the most common types of agreement involves pharmaceutical companies reimbursing the cost of their drugs if they do not have positive effects as defined by certain biomarkers, objective chemical features that can be used to measure the effects of treatment. For example, LDL cholesterol levels are considered an objective surrogate measure of the risk of coronary heart disease. As long ago as 1999, Pfizer agreed to refund the cost of the drug Atorvastatin if it did not reduce LDL cholesterol to a certain level in a certain proportion of patients in North Staffordshire Health Authority.⁶²

Another type of contract requires companies to reimburse the medical costs of dealing with the complications of diseases if patients are correctly taking their medication. For example, a US insurer, Health Alliance, recently announced a Fracture Protection Programme for an anti-osteoporosis drug sold by Procter and Gamble and Sanofi-Aventis called Actonel. Under this programme, the drug company reimburses the average medical expenses for non-spinal osteoporotic fractures in patients correctly taking their medication.⁶³ The US insurer Cigna is attempting to use a similar model and has approached the makers of cholesterol-lowering pills to agree to pay the medical expenses of patients who suffer heart attacks.⁶⁴

There are various benefits from these outcome agreements, depending on their exact terms. First, they transfer some of the risk to the manufacturer of their product working in the real world outside the strictly controlled environment of clinical trials, whilst protecting costly investment in innovative new treatments. Second, they can improve the value for money of branded drugs by market segmentation that selects the patients most susceptible to the product's effects. Finally, they incentivise a search for ways to improve patients' adherence to their medication instructions.

62 Stephen Chapman *et al.*, "Outcomes Guarantee for Lipid-Lowering Drugs: Results from a Novel Approach to Risk Sharing In Primary Care," *British Journal of Cardiology* 3 (2004): 206.

63 Reuters, "Health Alliance Announces First Fracture Protection Program for Actonel," 2009, accessed online at <<http://www.reuters.com/article/pressRelease/idUS154895+14-Apr-2009+PRN20090414>>.

64 Andrew Pollack, "Pricing Pills by the Results," *New York Times*, 14 July 2007.

Summary

These examples give an indication of the applicability of outcome commissioning to a wide range of services and its ability to achieve better outcomes and generate cost savings, while also illustrating some of the problems commissioners and providers have encountered in the early phases of implementing this approach. The next section examines in more detail how outcome commissioning works and ways to overcome these challenges.

5

The outcome commissioning process

The design of an effective system for commissioning outcomes is challenging, which helps to explain why such systems have been slow to develop. However, simply because outcome commissioning might be difficult does not mean it lacks merit. If commissioners have a realistic view of the challenges, they may take steps to overcome these by applying lessons learned from past experience. Drawing on insights from a number of case studies, including United Way of America's funding allocation model, this section discusses the process of implementing outcome commissioning, exploring potential challenges and ways to overcome them.

United Way of America's Funding Allocation System

United Way of America is the largest and one of the most influential philanthropic organisations in the United States. A federation of more than 1,300 community-based fund-raising organisations, it collected over \$4 billion in 2006.⁶⁵ The money it raises is then distributed to tens of thousands of local organisations.

In 1995 United Way overhauled its system of allocating funding, requiring applicants to certain United Ways to demonstrate the impact of their programmes;⁶⁶ that is, applicants must compare what they expected to achieve with data supporting the actual benefits of the programme.

United Way has developed its own unique approach to funding based on outcomes, which has several distinguishing features. United Way's approach:

- emphasises the use of quantitative data as evidence of programme performance. Outcomes should be measured at regular intervals to enable the accumulation of longitudinal data, and at each individual site of service provision, since "demonstration of effectiveness at national sites does not substitute for measurement of effectiveness in individual sites";
- encourages programmes to develop their own "program logic model" to discover and display the links between inputs and outcomes and to help identify indicators. This also helps programmes to

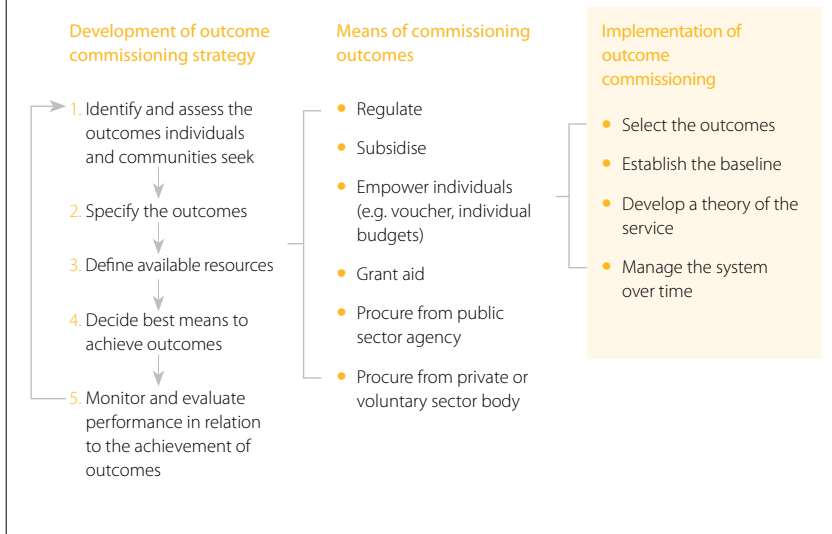
65 Michael Hendricks, Margaret C. Plantz and Kathleen J. Pritchard, "Measuring Outcomes of United Way-Funded Programs: Expectations and Reality," *New Directions for Evaluation* 119 (2008): 14.

66 Michael Hendricks, Margaret C. Plantz and Kathleen J. Pritchard, "Measuring Outcomes of United Way-Funded Programs: Expectations and Reality," *New Directions for Evaluation* 119 (2008): 15.

develop a “theory of change” to improve their outcomes. Many agencies have since commented on the usefulness of logic model thinking;

- encourages “practitioners and funders to expect a relatively long time horizon for developing, testing, and refining outcome measurement systems.” United Way asserts that a time lag of two to four years is realistic, from the time the idea of outcome measurement is introduced, to obtaining meaningful outcome data. This enables programmes to experiment with various approaches without the pressure to produce outcome data quickly; and
- advises against establishing performance targets until programmes have collected enough outcome data to know which targets are reasonable.⁶⁷

Figure 3: Outcome Commissioning



The process of outcome commissioning can logically be divided into four elements: selecting outcomes, establishing the baseline, developing a theory of the service and managing the evolution of the system over time. In practice, these elements are likely to occur simultaneously and/or iteratively.

Selecting the outcomes

Choosing which outcomes to pursue is an inherently political process that must be carried out in an appropriate way to ensure successful implementation. The state will

67 Michael Hendricks, Margaret C. Plantz and Kathleen J. Pritchard, “Measuring Outcomes of United Way-Funded Programs: Expectations and Reality,” *New Directions for Evaluation* 119 (2008): 17-18.

need to determine its priorities and balance competing demands when deciding how to allocate resources. There are many issues to consider, including questions of equity, access and personalisation. Depending on the service, the state may choose to:

- involve citizens in the formulation of outcomes, or transfer commissioning authority to service users so they can select their own outcomes, which happens increasingly in social care;
- distinguish between outcomes that are experienced at the individual level, as in services directed at the well-being of a single person such as chronic disease management, or that are indivisible and experienced at the collective level, as in services such as the safety and amenity of neighbourhoods, which are delivered to whole communities.

Outcomes must be sufficiently abstract to allow for innovation in service delivery, including the integration of previously 'siloes' services, yet specific enough to enable independent observation and objective measurement. They must be sufficiently ambitious to encourage innovation, but realistic enough that providers will be willing to assume the risk of delivering the outcomes.

Departmental silos

Government departments have different missions reflecting the conditions under which they were established. Thus, while government as a whole is concerned about the problem of alcoholism, scarce resources and different organisational missions and professional cultures will mean that different departments and agencies will view the problem in different ways. The Department of Health will be primarily concerned with the impact of excessive alcohol consumption on physical well-being. The Home Office will want to reduce the incidence of alcohol-related crimes. Social Services will be concerned about protecting children who are harmed by alcohol-related abuse. Each will commission different services and target different outcomes.

One way of overcoming this might lie in joining up the funding streams by creating a new budget that combines the proportion of each department's budget that is dedicated to solving that particular problem. However, this sort of joining up can be challenging and time-consuming, and may in certain instances not be feasible. Therefore it is worth considering other means of pursuing outcomes that do not fall within the remit of a single department.

The Department of Work and Pensions has integrated funding streams through the process of outcome commissioning itself. The prime contractor model used for Pathways and the Flexible New Deal allocates responsibility for managing the entire delivery chain to large providers who provide some services themselves and subcontract others from smaller delivery organisations. This system effectively transfers the risk of joining up funding streams to the prime contractors, who can petition for funds from departments other than the one that commissioned them. For example, prime contractors delivering employment counselling services have also received funding from the European Social Fund, which was created to support employment and help people enhance their training and skills. This may suggest a model for other services such as offender management.

Another problem is that often services normally provided by different departments need to be integrated in order to deliver an outcome. For example, Employment and Support Allowance claimants may need mental health counselling or physiotherapy (Department of Health) in addition to employment skills training (Department of Work and Pensions) as part of the process of preparing to return to work. It can be very difficult for the service user to identify where to access these different services. The prime contractor model may be one solution. Often, prime contractors will deliver the core services but will buy complementary services from other providers and either have those services delivered on-site or refer the service user, effectively joining up various services on behalf of the user. For example, some providers of the Pathways programme subcontract for various health services, identify users that demonstrate a need for these and refer them accordingly. Others have brought certain health services in-house.

Another option might lie in selecting a somewhat less ambitious outcome that does not require the integration of funding streams or services across different departments. For example, instead of commissioning a reduction in re-offending rates, which would require funding and services from the Ministry of Justice, the Department of Work and Pensions and the Department of Health, among others, one might commission a reduction in the rate of unemployment among ex-prisoners, which is likely to have a significant positive impact on re-offending rates and requires funding and services only from one other agency, the Department of Work and Pensions. The key step for this to be effective is to identify those limited outcomes that best drive the larger overall objectives.

Observable and measurable outcomes

In some cases, it may prove impossible to use the desired outcomes as a basis for commissioning the service because they do not fulfil the criteria of being independently observable and objectively measurable. Outcomes may not fulfil these criteria because of a long time lag between the intervention and the expected outcomes.

In such cases it may be more productive to specify the results in terms of an output or a cluster of outputs that are objectively measurable and closely enough linked to the outcomes to serve as a reliable surrogate. Such an approach requires the commissioner to have a sound understanding of the linkages between outputs and outcomes.

Education is one area where surrogate output indicators are required, since many of the important outcomes will not be verifiable for many years. In the UK, the Department of Children, Schools and Families relies on outputs such as exam results to evaluate the quality of education. This may not be a very good surrogate measure, however, since a child's exam performance at 16 years of age may not be an accurate indicator of the myriad of outcomes society expects children to achieve as a result of the education system, such as developing a passion for learning, becoming good citizens or acquiring the soft skills that enable children to become productive members of the workforce. Using outputs as measures of performance means that commissioners assume the risk that achieving the outputs might not actually result in the desired outcomes. Providers retain the risk of transforming inputs into outputs.

Target population

Where outcomes are to be measured in statistical terms, the population must be sufficiently large to eliminate artificial distortions. In some cases, it may be desirable to segment the population so as to create several separate groups, each relatively homogeneous. Segmentation can be difficult where the characteristics that differentiate one client from another are not obvious. Welfare to work schemes have historically separated clients into different groups based on the benefit they receive, and most experts agree that some segmentation is necessary in this market but dispute whether this particular method is the most appropriate.

Duration

The time period over which the outcome is to be achieved, and thus the duration of the contract, may be difficult to determine. Too short a period may leave providers

with insufficient time to make a return on their investment. It may also make it difficult to eliminate statistical aberrations. On the other hand, too long a time span will mean that commissioners have less flexibility to make necessary amendments to the contracts as learning occurs. Longer time periods increase the risks for commissioners and providers (with outcomes being either much harder or easier to achieve than anticipated at the outset), and they will provide more opportunities for extraneous variables to intrude.

Establishing the baseline

Commissioners will need a thorough understanding of the results the service is achieving before the change to outcome commissioning. Successful commissioning requires intimate knowledge of the initial quality of the service as it enables the commissioner to set appropriate benchmarks for service improvement, informs an understanding of the risks providers will be asked to assume and gives providers a better understanding of costs.

New services

In the case of new services, the baseline may be unknown so data will need to be collected before outcome commissioning is attempted. Learning might be accelerated by commencing with a performance regime based on inputs or outputs.

Rapidly changing circumstances

For services facing rapidly changing circumstances, the baseline may be known but not reliable. One solution in such cases is to express outcomes in terms of relative improvements rather than absolute measures.⁶⁸ This would entail modelling expected performance based on the current rate at which outcomes are being achieved and incentivising providers to do better. This would reduce the amount of risk providers would have to assume initially and allow a period of experimentation and observation. Specific outcome targets can wait until commissioners have sufficient information about what is realistic, and providers have had time to get comfortable with their client group and the service to be willing to assume more risk.

It would also be feasible to incentivise providers on their performance relative to other delivery organisations. Such a system of yardstick competition would avoid a

68 This idea of rewarding relative improvement is similar to Mark Friedman's "turning the curve" model. See Mark Friedman, *Trying Hard is Not Good Enough* (Santa Fe: Fiscal Policy Studies Institute, 2005).

situation in which providers were unfairly penalised for failing to achieve unrealistic results and would allow commissioners to collect data and develop an understanding of what can be reasonably expected of providers. Of course, care would be needed to avoid collusion among providers, through transparency, regulation, and incentive structures that discourage collusion.

Developing a theory of the service

The theory of the service is a hypothesis about how inputs are most effectively connected to outputs, and outputs to outcomes. It is thus a theory about the most efficient and effective ways of improving the ratio of outcomes to inputs.

One reason commissioners choose to use an outcome-based framework is to encourage providers to explore alternative models of service delivery. It may therefore appear contradictory to say that commissioners must develop a theory of best practice in service delivery. Of course, providers will need to have a much more intimate understanding of the linkages between inputs and outcomes, but commissioners will also need to develop a theory of the service, at least for the linkages between outputs and outcomes. Unless commissioners have some understanding of these relationships, they will find it difficult to frame appropriate statements of outcomes, select effective output surrogates for the desired outcomes, or evaluate the merits of alternative proposals. Finally, they may not recognise gaming behaviour, where providers exploit the system by generating returns for themselves without delivering the desired outcomes.

Understanding the linkages

There are several challenges involved in developing a theory of the service. The first is the need to understand how inputs, outputs and outcomes are connected, which may prove difficult with complex services such as reducing re-offending. Moreover, the most effective linkages may vary over time and from person to person. In the case of offending, seven pathways to reduce re-offending have been identified, but there is no way of predicting which of these pathways will be most effective for an individual offender.

Extraneous variables

A second challenge lies in extraneous variables. Without adequate control over sufficient factors impacting the outcomes they are obliged to deliver, providers will be unwilling to accept financial and reputational risks.

There are several ways of mitigating risk in these circumstances. In some cases, providers could reasonably be expected to take control of extraneous variables through some budgetary or structural re-organisation. ‘Streetscene’ provides an example of this. In one local authority, potholes, for which the provider was not responsible, were seen by local residents as contributing to poor service outcomes. There was a risk that providers would fail to meet their outcome targets, regardless of how well they were delivering the services under their control, because stakeholders perceived the ultimate service differently from the commissioners. Commissioners changed the contract with the provider to include pothole filling, thereby giving them control over that key variable.

Some variables may always remain outside the control of providers; for example Welfare to Work providers cannot control the economic climate, even though it is one of the key factors that will affect their outcomes. This does not mean that outcome commissioning is impossible, although it does necessitate a different and possibly less ambitious approach.

One way of mitigating the risk posed by extraneous variables might be to reduce the proportion paid for outcomes and increase payments for inputs and outputs. To cope with the rapidly deteriorating labour market conditions in the summer of 2009, the UK Department of Work and Pensions reduced the percentage of revenue of providers contingent on getting clients into sustainable employment from 80% to 60%.⁶⁹

Another way might be to pay for outcomes based on yardstick competition. Yardstick competition entails comparing the performance of two or more providers operating in the same conditions, effectively neutralising the effect of variables outside providers’ control. For example, in Welfare to Work, providers operating in the same geographical region face the same labour markets conditions, so commissioners can compare their performance knowing that one does not have an unfair advantage (more favourable labour market conditions) over the others. However, yardstick competition requires commissioners to manage the benefits of increasing competition with the risk of compromising economies of scale and/or duplicating services and infrastructure, and, as previously noted, provisions must be made to prevent collusion.

⁶⁹ House of Commons Work and Pensions Committee, *DWP’s Commissioning Strategy and the Flexible New Deal: Government Response to the Committee’s Second Report of Session 2008-09* (London: The Stationary Office Limited, 2009): 6.

Co-production

The behaviour of service users is one of the variables over which providers may have limited control. However, outcome commissioning may be easier where service users are obliged to cooperate with service providers to produce the outcome, as in Flexible New Deal where there is a requirement on the unemployed person to search for and accept reasonable offers of employment, or where they have a strong incentive to cooperate, as in some cases with chronic disease management. Outcome commissioning is more difficult when providers have less influence over users because they are not required to cooperate, as in Pathways to Work where those receiving Employment Support Allowance have no legal obligation to seek or accept employment, but providers are nevertheless paid based on the number of people they return to work. One of the main challenges facing providers in this situation is to motivate users to cooperate. Yardstick competition may be one way of solving this.

Controlled environment

In some cases, outcome commissioning may be more effective where providers deliver the service in a controlled setting where they may have more influence over the behaviour of users. Managed health care delivered in nursing homes may be more effective than care delivered in the users' homes. Drug misuse counselling may be more effective if commenced while an offender is in prison.

Managing the process over time

Outcome commissioning is an iterative process, not an event. Commissioners will need to monitor and evaluate the behaviour of providers and the levels of achievement of outcomes, and make changes to the system according to their findings.

Gaming

One of the most important elements of evaluation lies in monitoring, learning from and preventing, or at least reducing, harmful gaming behaviour.

The move to outcome commissioning will be developed, supported and exploited by the entrepreneurial behaviour of service providers. Entrepreneurial behaviour may develop two kinds of innovation.

The most welcome form of improvement will come through service innovation, the exploitation of technological or process innovation to provide more effective linkages between inputs, outputs and outcomes. Pharmaceutical companies are

experimenting with microchips that can be implanted under the skin of patients to remind them when to take their medication.⁷⁰

In other cases, providers may achieve outcomes through market segmentation, the identification of a sub-population amongst whom their intervention has a higher rate of success or a lower cost of delivery.

Market segmentation may be desirable because it will focus specific interventions on the members of the population where the impact is highest. The NHS is contracting for expensive new pharmaceuticals on the basis that the companies reimburse the healthcare provider if the drugs fail to produce a certain result for a given proportion of patients.⁷¹ This implies an acceptance on the part of public sector commissioners that some interventions may be highly effective with only some service beneficiaries. The challenge lies in identifying those individuals (and thus segmenting the market), and performance incentives can assist in this process. Market segmentation that helps identify the individuals for whom interventions will be most effective is beneficial.

However, market segmentation is unwelcome where it results in cream-skimming and parking, where providers are paid for delivering services to those in greatest need, but focus instead of those who are easy to serve. Commissioners should seek to avoid this type of gaming, whilst recognising that they are unlikely to prevent it entirely the first time they commission a service on an outcome basis. Where gaming occurs, commissioners should seek to learn from it by letting short term contracts and building these insights into a redesigned procurement model.

Summary

This section has described the process of commissioning outcomes, which includes selecting the outcomes, establishing the baseline, developing a theory of the service and managing the process over time. It has also identified some challenges associated with this approach and ways to resolve them. When implementing outcome commissioning, commissioners should ask themselves the following questions:

70 Andrew Jack, "Chip on your shoulder will ensure bitter pills are easier to swallow," *Financial Times UK*, 22 September 2009, accessed online at <<http://www.ft.com/cms/s/0/146dcbde-a710-11de-bd14-00144feabdc0.html>>.

71 Stephen Chapman *et al.*, "Outcomes Guarantee for Lipid-Lowering Drugs: Results from a Novel Approach to Risk Sharing In Primary Care," *British Journal of Cardiology* 3 (2004): 205.

Selecting the outcomes

- 1 How many funding streams are required to achieve this outcome and how can they be joined up?
- 2 Are the outcomes objectively measurable and independently observable?
- 3 What is the target population and appropriate time frame?

Establishing the baseline

- 4 Is the baseline well-understood?

Developing a theory of the service

- 5 Is there a well-established theory of the service?
- 6 How many of the variables that influence the outcomes desired do providers control? Are they operating in a controlled environment or could it be made more controlled? Are users likely to cooperate to achieve outcomes?

Managing the process over time

- 7 Has gaming behaviour been anticipated and avoided? Is gaming behaviour evident? If so, is it harmful or beneficial to service users? What can be learned from it?

Where the answers to these questions indicate a challenge, commissioners should reflect on whether any of the strategies recommended above might help overcome that challenge.

6

Transitioning to outcome commissioning

Despite the potential benefits of outcome commissioning, introducing such an approach will be quite challenging. The questions listed in the previous section are intended to give commissioners an idea of some potential difficulties and solutions. However, even in services where the answers to these questions indicate that outcome commissioning will be achievable, it will only work properly when service models have been developed, assumptions revisited and the range of appropriate institutional structures developed. The challenge lies in providing a good quality of service during the transition.

This is not an insurmountable challenge if approached correctly. One of the key roles of commissioners is to ensure the benefits of outcome commissioning are clear to everyone involved and to provide sufficient clarity of direction that the ultimate objectives are not lost in the complexity of the transition process.

Broadly speaking, there are two possible approaches to this, each with its own benefits and disadvantages. The first is the 'big bang' approach that aims to introduce a fully developed system in one attempt and deal with any unexpected consequences afterwards. The other is staged implementation, which allows for the incremental development of underlying factors through piloting, collaborative working and iteration. Of course, these approaches represent the extremes at the ends of a spectrum, and commissioners may find the best method lies somewhere between the two.

'Big Bang'

This approach has several advantages. First, it is quick. Rapid implementation means service improvements may become visible more quickly and on a larger

scale than would occur with staged implementation. Second, there may be a higher probability of fundamental change if the ‘big bang’ approach is used. The introduction of outcome commissioning is likely to be politically and organisationally challenging and will require political capital and organisational focus. An incremental approach in the face of these barriers may result in tinkering at the edges instead of a fundamental change to the status quo.

However, this approach also carries significant risks. One of the key benefits of outcome commissioning is its potential to stimulate innovation once the incentives in the system have been appropriately aligned with the desired outcomes. The problem with a ‘big bang’ approach is that it is likely to lock in preconceived views regarding the theory of the service and delivery infrastructure. Moreover, it may not allow time for an effective supply market to evolve. This could generate significant short term risks for the quality of the service in question, as alternative providers may not yet have developed the capacity to deliver the outcomes commissioned. There may also be a risk for providers, who, if unable to deliver the outcomes, could face threats to their financial viability.

Staged implementation

The primary benefit of an incremental approach is that it gives suppliers time to develop the capacity to deliver outcomes by gradually accepting greater risk. This gives providers more time to experiment with service delivery while a smaller part of their payment is at risk which may result in better innovation than the ‘big bang’ approach.

However, staged implementation has disadvantages. There is a risk that if commissioners begin with an interim stage of outcome commissioning and that system fails to deliver the desired results immediately, the entire project might be abandoned. Even if the interim phase is a success, a change of political focus for other reasons might stall the system at its interim stage. This is particularly an issue where commissioners aim to use trials to identify more politically sensitive aspects of a system such as gaming or cream-skimming, and the trials have embarrassing results. It is also possible that the approaches trialled at a pilot stage become part of the final structure of the service, even if there is further scope for innovation and improvement.

Staged implementation might take a number of forms.

- *Developing from a system of input - through output - to outcome commissioning.* In many instances, the first steps towards creating a supply market and understanding the theory of the service may require commissioners initially to develop intermediate systems. Often a first step may be to commission outputs through a base payment but provide some additional payments to providers if certain outcome targets are met. This limits the amount of public money at stake and limits the risk on the provider side while incentivising innovation in the model of service delivery.
- *Small-scale piloting.* Where a service can be tested at a small scale without the scale affecting the nature of the service in question, it may be possible to set up local pilots. This was the approach taken to the introduction of personal budgets for Social Care (an outcome-based approach that uses individual funding). This can help the commissioner to understand some of the parameters involved and start to develop alternative theories of the service. There are, however, questions about the extent to which small-scale pilots can really replicate the environment of full outcome commissioning for all services. Scale is important for some services, especially those where there is a need to invest in technology and innovation, as in the case of long term condition management. Moreover, it can be difficult to obtain sufficient managerial focus on the delivery of small pilots.
- *Regional piloting.* Where scale is more important, regional pilots can be a good halfway house towards full outcome commissioning if they are politically acceptable. Large-scale regional pilots can offer good examples of the likely benefits and challenges while limiting the risk for commissioners. However, regional pilots are large enough to be politically embarrassing but are by their nature experimental, so they are unlikely to be the first stage in the outcome commissioning process. Flexible New Deal has taken a phased approach to the introduction of outcome commissioning with a first phase that can inform the approach taken to subsequent regions. While this is more than a pilot, it does leave scope for learning from early experiences. This might be the most appropriate way to approach the introduction of outcome commissioning in Offender Management, for example.
- *Engagement with the supply market and users.* In developing a theory of the service, a long period of consultation with both the supply market and user

groups might provide an effective way of testing different commissioning approaches. However, this does have a key risk. One of the major benefits of outcome commissioning is that it challenges old assumptions about how a service is delivered. By engaging with the existing supplier base there is a very real risk of locking in old prejudices and creating a system that favours vested interests. Users may be committed to the providers who currently deliver services and particularly risk averse to changes to critical services. Therefore the approach to the engagement needs to be based upon a very clear picture of which outcomes are being pursued and a willingness to challenge the existing experienced and committed delivery organisations.

Summary

There are many prerequisites for successful outcome commissioning, many of which will require several iterations or staged implementation in order to develop properly. However, it would be unwise to ignore the substantial political and organisational barriers that confront the commissioner in delivering change. This might mean that there are a limited number of occasions where the political will and the organisational capacity coincide to support the introduction of a new system. Commissioners will need to grasp the opportunities that do arise to push as far forward as they can.

Appropriate staging is the key. Commissioners must ensure that individual stages offer both sufficient benefit and minimum risk to be attractive, but are large enough that the probability of achieving the goal of a fully functioning system of outcome commissioning is high. Most critically, commissioners will need to provide excellent leadership to ensure that staged development does not fall back into merely incremental change. This will only happen if commissioners set clear ultimate goals and explain how the stages will lead to full outcome commissioning. Thus, appropriate staging placed within a long term commissioning framework that offers clear direction likely offers the highest probability of success.

7

The Way Forward

Rethinking state action from outcomes

This report argues that government at central and local level, through deliberation with citizens, should be specific about the outcomes it is seeking to achieve. If it is unclear what outcomes are being sought then it is impossible to know if they have been delivered. If outcomes conflict with one another, then success is unlikely.

It also argues that government has to evaluate the current outcomes of public services and, where they are poor or improvements have reached a plateau, re-think how to achieve better outcomes. Increasing inputs may have been necessary but has not been sufficient to achieve outcomes commensurate with the public's expectations; this study proposes that the delivery mechanism be transformed so that it focuses on outcomes. While the quality of the relationship with the provider matters to the public, it is the outcomes that matter most and expenditure that does not achieve desired outcomes wastes the public's money.

This fundamental re-think of how to deliver better outcomes is needed because the current system is often inefficient, provider-dominated, not sufficiently citizen-focused and lacks effective mechanisms of accountability. Moreover, the UK faces severe constraints on public spending which means that in order to maintain even the current levels of outcome attainment, the system must become much more effective and efficient. There are several approaches to re-thinking state action to achieve better outcomes. Outcomes can be achieved through a number of means, including regulation, subsidies, citizen empowerment, grants and procurement.

Paying for outcomes matters because of the incentives it creates. This does not necessarily mean that all payments must be for outcomes. In some cases providers will be unwilling to assume *all* the risk for achieving outcomes, but even a

small percentage of outcome payment can provide a very powerful incentive if, for example, a substantial proportion of profit is at risk.

There are several ways to reformulate the payment structure to make outcome commissioning feasible in these circumstances. In some cases the payment structure might include base payments for inputs plus additional payments for outcomes achieved. If it is not possible to pay for outcomes, payment for one or more outputs closely linked to the outcomes would be a better option than paying for inputs as it still incentivises performance and innovation. As long as the output has a clear and significant relationship to the outcome, it is worth building a system that rewards its achievement.

Finally, delivering outcomes sometimes requires the joining up of government silos. This should not be an argument for doing nothing until these silos are brought together. Commissioners may be able to incentivise less ambitious outcomes or outputs. Alternatively, it may be feasible to pass the outcome responsibility to a third party agent who can join up the inputs themselves by contracting with each of the silos to try to draw in the necessary resources.

These alternative payment systems do not mean that an incremental approach based on current delivery models and systems is appropriate. Rather, several key principles for redesigning more effective publicly-funded actions should be followed.

A model for paying for outcomes

- Start with a clear definition of the outcome. If goals are in conflict, seek to resolve or prioritise. This will often require engagement with citizens.
- Conduct research to understand the baseline, then challenge the effectiveness of the current model of delivery.
- Decide how best to specify the outcome to providers. Is the outcome independently observable and objectively measurable? If not, can one or more outputs act as a surrogate?
- Consider whether the current service model includes all the inputs necessary to deliver outcomes. Do providers need to be given control of other inputs in order to achieve outcomes? If it is not possible for providers to control all the required inputs because other departments claim

responsibility for some of them, then commissioners must recognise the need to change this or it is unlikely to attain the outcomes.

- If, however, it is improbable in the short term that all the necessary inputs and funding streams can be joined up to allow for optimal commissioning, choose less ambitious outcomes that are achievable.
- Consider whether there should be customer segmentation. Do different clients or customers behave differently or need different services? This may help commissioners decide whether to pay for outcomes for only a segment of the population and will often provide insight into potential gaming by providers and how to manage it.
- Consider the time period providers should be given to achieve outcomes. How long might it take to make a change? After how long will other variables intervene, making it difficult to know whether to reward providers for outcomes or attribute them to another cause?
- Establish a process to explore alternative theories of the service in pursuit of those most effective. Scan research literature, have open dialogues with users, specialist interest groups and service providers to develop a thorough understanding of the linkages between inputs, outputs and outcomes.
- Consider to what extent users are likely to cooperate in achieving the outcome, and how they might be incentivised to do so.
- Transfer delivery risk to providers by designing powerful incentives into the system, paying for outcomes wherever possible. Engage with providers to ensure that the level of risk may not exclude certain providers such as small to medium-sized enterprises and the third sector.
- Monitor the effectiveness of the new system, wherever possible with a comparator group, and be prepared to redesign the system if it does not achieve outcomes or where harmful gaming is taking place.
- Put in place visible leadership to support the risk and respond to any problems.

Where to begin to implement outcome commissioning

The final section of this report suggests where government might implement outcome commissioning. Whoever wins the next election is likely to review the large landscape of agencies and Non-Departmental Public Bodies to consider if there is

sufficient evidence that they improve outcomes. Ministers and senior civil servants should systematically explore which of an agency's functions could be moved onto a pay-by-outcomes basis. Ministers will have to drive the change because existing providers will tend to overestimate the benefits of the system with which they are familiar and the risks associated with exploring alternatives.

In the interests of stimulating a debate over the services where outcome commissioning might be explored, the following pages suggest some policy areas that might benefit from such an approach. Some of these suggestions build on past experience or pilot projects; these should be prioritised since there is already evidence that outcome commissioning works in these areas. Others are areas where outcomes are poor that also display certain characteristics that suggest that outcome commissioning might help improve outcomes. This list is illustrative and is by no means exhaustive. The characteristics of the services suggested here are summarised in the appendix.

Previously-piloted services

Employment counselling for long term unemployed and Employment Support Allowance claimants

Welfare costs the state substantial sums of money each year; in 2006-07, the Department of Work and Pensions spent around £37 billion on working age benefits.⁷² The Department has made substantial progress in implementing outcome commissioning through the Employment Zones, Pathways to Work and Flexible New Deal programmes. The learning from implementing these programmes should be captured and applied to other areas, such as those suggested here.

Long term health condition management

Managing long term health conditions better in the community could generate enormous savings for the NHS by reducing the need for unplanned support from the acute sector. There have already been a number of pilots in which providers have monitored the number of hospital admissions and attempted to reduce them. These pilots have been based on different theories of the service; some relied on telehealth systems while others used community matrons to better manage long term conditions. The pilots have had varying levels of success. Further studies must be undertaken to understand when these different theories of the service work best, and then pilots could be extended. The key would be to move to paying

⁷² David Freud, *Reducing dependency, increasing opportunity: options for the future of welfare to work* (London: Department of Work and Pensions, 2007): 67.

providers based on their performance against a number of metrics, including hospital admissions, mortality/morbidity and patient satisfaction.

Stability for children in care

Providing safety and stability to children in care is one of the key goals of child protection action. In the USA, the federal government fines states that do not achieve outcomes. For this reason, states have begun to pay agencies for achieving outcomes. Experts in this area should look at the potential to develop a similar system in the UK.

Street management

Several local authorities have contracted with private providers for the provision of streetscene services, with profit at risk based on the community's level of satisfaction with the cleanliness of their streets. As the model develops, commissioners and providers have been exploring the inclusion of a wider range of functions, such as graffiti removal, to deliver better outcomes.

Services where outcome commissioning should be a priority

Foundation Hospital Trusts and PCTs

Much can be learned from the *Payment by Results* programme in health; this must be studied and applied to other domains, including how PCTs could be paid for improving health outcomes.

Waste management and recycling

There are wide variations in the levels of recycling achieved in various regions of the UK. We should explore the scope for rewarding waste management agencies, whether public or private, on the basis of the minimisation of non-recycled waste.

Effective Punishment

Unpaid fines and incomplete community sentences damage the credibility of criminal justice and lead to more people being imprisoned for short sentences. In 2007, 55,443 adult offenders were given custodial sentences of 12 months or less, or 65% of all sentences.⁷³ The direct cost of imprisonment is estimated at over £35,000 per year per offender.⁷⁴ Short sentences are thought to *increase* the

⁷³ Matrix Knowledge Group, *Are short term prison sentences and efficient and effective use of resources?* (Matrix Evidence, 2009): 11.

⁷⁴ Tom Schuller, "Crime and Lifelong Learning," *IFLL Thematic Paper 5 (Leicester: National Institute of Adult Continuing Education, 2009): 15.*

likelihood of re-offending, because they are long enough to disrupt networks such as family and employment that may help prevent re-offending but too short to put in place any meaningful interventions to reduce the probability of re-offending.⁷⁵ Outcome-based offender management would involve paying an agent, whether a Probation Trust, or a private or third sector agency, according to their success in maximising fines paid and community sentences completed. A much more actively managed system might develop that would use a range of commercial debt chasing techniques, intelligent electronic monitoring and proportionate rewards and sanctions to stimulate compliance with the sentence. Such a system should be developed with judicial involvement to ensure that it had the right balance of retributive and rehabilitative focus. The goal would then be to use this new system to reduce the use of short prison sentences which would save substantial sums.

Reducing Substance Misuse

Drug abuse has a major impact on both users and society. Currently a range of providers argue over which approach to stopping drug misuse is best and the state pays for various intervention programmes. Paying providers for getting people off drugs rather than for running programmes would drive innovation and ensure the funding went to the most successful suppliers.

Processing asylum claims

In 2007 there was a backlog of 400,000 to 450,000 asylum claimants.⁷⁶ The NAO estimated “that this backlog cost nearly £600 million in 2007-2008, of which £430 million (72 per cent) was accounted for by accommodation and welfare support.”⁷⁷ In the past, some cases have waited years for determination.⁷⁸ An outcome-based system would reward agents on an outcome basis for gathering the information and documentation required to bring cases expeditiously to the point of adjudication. Provisions would need to be in place to ensure the just as well as fast processing of files. Such a system would save millions, help undermine migrant traffickers and make removal easier and more humane.

75 House of Commons Select Committee on Justice, “Short custodial sentences,” *Fifth Report*, 2008, accessed online at <<http://www.publications.parliament.uk/pa/cm200708/cmselect/cmjust/184/18407.htm#n155>>.

76 National Audit Office, *Management of Asylum Applications by the UK Border Agency* (London: The Stationary Office, 2009): 4.

77 National Audit Office, *Management of Asylum Applications by the UK Border Agency* (London: The Stationary Office, 2009): 4.

78 John Bourn, *Improving the Speed and Quality of Asylum Decisions* (London: National Audit Office, 2004): 6, 9.

Removing failed asylum seekers and illegal migrants

The removal of failed asylum seekers and illegal migrants requires a complex range of services. While the adjudication of cases is not suitable for outcome commissioning, all of the other services required would be very appropriate, paying for successfully and humanely removing individuals.

Services where outcome commissioning has the potential to drive better outcomes, but where further study by practitioners is required

Reducing re-offending

This is complex and challenging because the factors that help desistance, such as employment, relationships, housing, and drug interventions are controlled by a wide range of central and local government bodies, and there is no process to bring them together into an effective commissioning framework. Moreover, while it has been suggested that segmenting the offending population might help achieve better outcomes, there are still many conflicting theories as to which part of the offending population would be more likely to co-produce the outcome of desistance.

It might be possible to design experimental offender management systems, rewarded in whole or in part for success in reducing re-offending, by focusing on outputs or limited outcomes that could be delivered with the resources from one funding stream. These might also be focused on sub-groups of the offending population with key common characteristics. One such experiment for non-custodial sentences was illustrated above. Equally, by commissioning regional providers, as in Welfare to Work, it may be feasible to get the suppliers to integrate funding streams.

Illiteracy

Paying schools according to their examination success would not be equitable but that does not mean there is no place for payments for performance in the school system. Too many children still leave primary school with very poor literacy and numeracy skills, often compounded by other problems. Experimenting with paying charities or other agencies for success in getting such children to a standard of literacy that allows them to derive value from their secondary education and gain work and life skills would be of enormous value. This would involve paying for outputs (literacy), but outputs closely related to the long term outcomes that constitute success for children.

System improvement – Benefits based funding

Most of this report has explored how to attain the outcomes desired by the public. However, outcome reward mechanisms are also applicable to the processes and systems of government, which is important as these consume enormous amounts of expenditure. There is an increasing use at the state level in the USA of “Benefits Based Funding”, whereby funding is linked directly to outcomes and benefits. In a benefits based project a provider receives payment for services based upon measurable business benefits to the clients. Procurement will not only describe the requirements, it will also describe the benefits the Department or Agency is seeking to achieve. HM Revenue and Customs might want to increase tax revenues and reduce the tax gap or reduce the transactional costs associated with debt management; the Department of Work and Pensions might want to reduce the incidence of benefits fraud; the Department for Environment, Food and Rural Affairs might want to reduce the transactional costs associated with agricultural payments. What all these have in common is that they are tangible business benefits related to transactions undertaken by Government. With Benefits Based Funding, an IT provider would be paid a proportion of the total payment when the benefits set out in the contract were realised. No benefits, no additional payment. Ministers should signal they wish to move in this direction.

This list is only illustrative. There should be an active debate about where else and how outcome commissioning could be applied. In addition, providers from all three sectors should be encouraged to come forward with proposals for outcome reward systems to be trialled on an experimental basis and both central government and local authorities should actively begin to implement such pilots.

8

Conclusion

Outcome commissioning can improve the level of achievement of outcomes of public services in three main ways. It ensures providers focus on the outcomes that are important to users, creates powerful incentives to achieve outcomes and gives providers flexibility, incentives to innovate and the ability to personalise services.

When citizens' expectations of public services are rising, the current levels of achievements of outcomes are sometimes poor and the UK is facing constraints on public spending, it is crucial that the process of and challenges to implementing outcome commissioning are studied. This report has illustrated a four-step process of selecting the outcomes, establishing the baseline, developing a theory of the service and managing the process over time. Through the analysis of case studies, some of the challenges of this approach have been identified, including extraneous variables, lack of understanding of the linkages and gaming, and recommended strategies to overcome them, such as yardstick competition, research, and the proper segmentation of the population with appropriate incentives for different types of users.

Transitioning to outcome commissioning may not be easy. There is no one best approach to the transition process, and methods may fall somewhere between 'big bang' and a more incremental transition.

Finally, this report has identified a way forward, suggesting areas where outcome commissioning might be applied in the future. Areas where outcome commissioning has already been piloted should be priorities. The other recommendations will need to be more thoroughly considered in order to construct an appropriate framework for outcome commissioning in those areas. This does not mean, however, that commissioners should not act now; often, practitioners will be able to learn by doing and the benefits available are too large to delay. There is an urgent need to redesign systems based on outcomes, and this must be commissioners' foremost concern.

Some questions have been left unanswered. Further work will be needed in relation to understanding the best ways for the state to achieve outcomes, whether through regulation, subsidies, empowering individuals, grant-aiding or procurement. In particular, the questions of how and where to use citizen empowerment to achieve outcomes are important. Individual budgets are beginning to be rolled out in Social Care with excellent results but could be used in other areas.

Outcome commissioning is radical and will not be implemented without strong political leadership. Leaders and politicians will need to position themselves as champions of outcomes, not of providers or defenders of the current system. They will have to provide the challenge for change and make the case for experimentation to achieve better outcomes. If current outcomes are poor, or there is little evidence of improvement, then they will have to advocate for new approaches.

Politicians will recognise that some innovations will not produce the desired outcomes and may result in unintended consequences; however, remaining with the status quo guarantees no improvement. Progress may take time and experiments will require support to give them a fair chance, but the benefits to be realised could be enormous both in terms of efficiency and achieving better outcomes for citizens. Politicians and senior policy makers and managers must begin to explore radical innovation now, driving change to realise better outcomes.

Appendix

The outcome commissioning process applied

Outcome	CRITERIA			
	SELECTING THE OUTCOMES			
	Is it feasible to join up funding streams?	Are outcomes observable and measurable?	Is the target population easily identifiable?	Is the time period easily identifiable?
Reduce unemployment	Yes, most funding flows from DWP to providers, who get some funding from other sources	No, but can use surrogate of 26 weeks employment	Can be difficult to segment; differences btw. different types of claimants unclear	For long term unemployed, yes; more difficult for ESA claimants
Better manage long term health conditions	Yes, most funding comes from the Dep't of Health	No, but can use surrogates of decreased hospital admissions, morbidity/ mortality and patient satisfaction	Not always clear who will benefit most from interventions	Yes
Improve health outcomes by paying PCTs for outcomes	Yes, all funding comes from the Dep't of Health	No, but can use data from PCTs on patient outputs	Yes, it is everyone the PCTs serve	Yes
Better outcomes for children in foster care	Yes, most funding comes from the DCSF	No, but can use surrogates of safety, stability and permanency	Yes, all children in foster care	Yes, the duration of their time in foster care
Clean streets	Yes, all funding comes from the Local Authority	Yes, clean streets and residents' satisfaction	Yes	Yes
More recycling and less waste	Yes, all funding would come from the Local Authority	Yes	Yes	Yes
Effective punishment	Yes, most funding would come from NOMS	Yes	Yes	Yes
Reduce substance misuse	Yes, most funding would come from the Dep't of Health	Yes	Yes	No
Remove failed asylum seekers	Yes, all funding would come from the UK Border Agency	Yes	No	Yes
Reduce re-offending	There are multiple funding streams from different dep'ts; it will be difficult	No, not all who re-offend are apprehended	No, it is unclear which offenders are most likely to desist	No, it is unclear how long offenders must be tracked to ensure they do not re-offend
Better education outcomes for children with poor attainment	Yes, all funding would come from the DCSF	Yes, using the output of examination attainment	Yes	Yes

CRITERIA						
ESTABLISHING THE BASELINE			DEVELOPING A THEORY OF THE SERVICE			
Is the baseline known?	Is it an existing service?	Are the macro-conditions stable?	Are the linkages understood?	Are there extraneous variables?	Do users have strong incentives to achieve outcome?	Is the environment controlled?
Yes	Yes	No, so DWP has increased the amount payable for outputs	Yes, although inputs vary for each client	Yes, labour market conditions	Wide variation among users	No
Yes	No	Yes	There is some scientific evidence of linkages, but differences among individuals	Yes, user behaviour	Wide variation among users	No, not in the UK where these services tend to be delivered in the home
Yes	Yes	Yes	Yes, in general there is scientific evidence of linkages	Yes, user behaviour	Wide variation among users	Yes
Yes	Yes	Yes	Yes, evidence that three outputs are closely linked to the outcome	Yes, number of children in care and number of foster families	Yes	No
Yes	Yes	Yes	Yes, to clean the streets, but factors influencing satisfaction are still being explored	Yes, how much residents litter, but this is easily corrected	Yes	No
Yes	Yes	Yes	No, what makes people recycle is not well-understood	Yes, the consumption patterns of residents	No	No
Yes	Yes	Yes	Yes	Yes	No	No
Yes	Yes	Yes	What motivates each individual is not well-understood	Yes, users' motivation	Wide variation among users	Depends if it is in- or out-patient
Yes	Yes	Yes	Yes	Yes	No	No
Evidence about how many of the total population re-offend, but individual baselines unknown	Yes	No, many factors impact on the levels of crime	A little, although inputs vary for each client	Yes, number of offenders and behaviour of users	Wide variation among offenders	Depends if they are in prison or in the community
Yes	Yes	Yes	Yes, somewhat, although inputs vary for each client	Yes, the behaviour of students and involvement of parents	Wide variation among children	At school, yes, but not outside of the school

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