



House of Commons
Public Administration Select
Committee

Public Services and the Third Sector: Rhetoric and Reality

Eleventh Report of Session 2007–08

Volume I

*Ordered by The House of Commons
to be printed 26 June 2008*

HC 112-I
Published on 9 July 2008
by authority of the House of Commons
London: The Stationery Office Limited
£0.00

The Public Administration Select Committee

The Public Administration Select Committee is appointed by the House of Commons to examine the reports of the Parliamentary Commissioner for Administration and the Health Service Commissioner for England, which are laid before this House, and matters in connection therewith, and to consider matters relating to the quality and standards of administration provided by civil service departments, and other matters relating to the civil service.

Current membership

Dr Tony Wright MP (*Labour, Cannock Chase*) (*Chairman*)
Mr David Burrowes MP (*Conservative, Enfield Southgate*)
Paul Flynn MP (*Labour, Newport West*)
David Heyes MP (*Labour, Ashton under Lyne*)
Kelvin Hopkins MP (*Labour, Luton North*)
Mr Ian Liddell-Grainger MP (*Conservative, Bridgewater*)
Julie Morgan MP (*Labour, Cardiff North*)
Mr Gordon Prentice MP (*Labour, Pendle*)
Paul Rowen MP (*Liberal Democrats, Rochdale*)
Mr Charles Walker MP (*Conservative, Broxbourne*)
Jenny Willott MP (*Liberal Democrats, Cardiff Central*)

Powers

The powers of the Committee are set out in House of Commons Standing Orders, principally in SO No 146. These are available on the Internet via www.parliament.uk.

Publications

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the Internet at <http://www.parliament.uk/pasc>

Committee staff

The current staff of the Committee are Steven Mark (Clerk), James Gerard (Second Clerk), Pauline Ngan (Committee Specialist), Louise Glen (Committee Assistant), Miguel Boo (Senior Office Clerk) and Anne Woolhouse (Secretary).

Contacts

All correspondence should be addressed to the Clerk of the Public Administration Select Committee, Committee Office, First Floor, 7 Millbank, House of Commons, London SW1P 3JA. The telephone number for general enquiries is 020 7219 3284; the Committee's email address is pasc@parliament.uk

Contents

Report	<i>Page</i>
Summary	3
1 Introduction	5
The third sector	5
Scope of the inquiry	6
2 Government and the third sector	9
A tradition of service provision	9
Financial relations between government and the third sector	10
3 The Government vision	13
The context: public service reform	13
The goal: transformation of public services	14
The method: commissioning	15
4 The scale of third sector involvement	18
Rolling back the State?	18
5 Third Sector distinctiveness	22
The characteristics of the sector	24
Assessing the evidence on distinctiveness	27
Does size matter?	30
“Added value”	32
Conclusions	33
6 Levelling the playing field	36
“First do no harm”: eliminating perverse practices	38
Short-term contracts	39
Full cost recovery	41
Judging the scale of contracts	43
Financial disparities	46
Access to capital	46
Other disparities	49
The role of the Compact	52
Conclusions—careful contours	54
7 Intelligent commissioning	55
Commissioning for distinctiveness	55
Commissioning for added value	58
Commissioning for independence and innovation	61
Intelligent commissioners	63
8 The risks of third sector provision	66
Risks to the service user	66
Standards of service	66

Accountability	68
Risks to civil society	72
Distortion of mission	73
The role of grant funding	75
Freedom to campaign	77
Public disengagement from government	78
9 Conclusions	79
Appendix: Matching public service requirements with third sector organisations' strengths	81
Conclusions and recommendations	82
Formal Minutes	92
Witnesses	94
List of written evidence	95
List of Reports from the Committee during the current Parliament	97

Summary

Government is commissioning ever more public service delivery from organisations in the third sector—charities and other not-for-profit organisations, as well as social enterprises. In this report, our first since acquiring responsibility for scrutinising third sector policy, we have attempted to assess the impact of that policy approach. In particular, we have tried to look not just at the effect on government and on the sector, but more importantly the effect on service users and the public at large.

The central claim made by the Government, and by advocates of a greater role for the sector in service delivery, is that third sector organisations can deliver services in distinctive ways which will improve outcomes for service users. We were unable to corroborate that claim. Too much of the discussion is still hypothetical or anecdotal. Although we received a great volume of response to our call for evidence, much of it admitted that the evidence was simply not available by which to judge the merits of government policy.

As the initiator of a significant policy change, the onus is on the Government to demonstrate the evidence base supporting its actions. However, attempting to identify general distinctive characteristics of an entire sector is not necessarily the most constructive way forward. We suggest that the Government's priority ought to be understanding the needs of the users of particular services, and then working out what organisations might be best placed to meet those needs.

Our report calls for a vigorous mixed economy of provision, with all prospective service providers judged on their merits. However, commissioning should not mean a return to Compulsory Competitive Tendering, where cost savings were the principal driver. While any barriers to third sector participation ought to be removed, it is unrealistic ever to expect an entirely level playing field. Instead, therefore, getting the best out of commissioning will rely on commissioning authorities designing service specifications which play to the strengths of the best placed organisations. Commissioners—the people who decide on the contents and results of tender exercises—are the key to ensuring the right results.

We use the term “intelligent commissioning” to suggest a way forward. Our understanding of intelligent commissioning is that it should be based on a knowledge of potential providers and of desired outcomes, based on user needs. Intelligent commissioners should be able to make judgements such as whether contracts or grants are the right way to fund a service, how important price should be in determining who wins a contract, and whether there is scope for innovative methods of delivery. The persistence of perverse practices, like unnecessarily short-term contracts, suggests that a culture change is still needed if the potential benefits of commissioning are to be realised. We support the Government's moves to train key commissioners, and also call for more incentives to encourage talented people to work as commissioners.

Just as the potential benefits of commissioning are unproven, so too are many of the risks which were identified to us. We do not believe some of the more alarmist claims made, such as the suggestion that the sector's ability to campaign independently has been

diminished. Nor do we believe that it is necessarily a problem that contractual funding is growing more quickly than grant funding. No third sector organisation has an inherent right to public money just because it does good work—the government is entitled to determine which organisations it wants to support, based on its understanding of what constitutes the public interest. In practice, government appears to recognise the importance of maintaining a healthy and diverse sector, although there are legitimate questions to be asked about the mechanisms used to achieve this, such as the Compact.

Nonetheless, there are risks to be addressed if policy is to continue to move in its current direction. Users' rights should not be affected by whether a service is provided directly by the State or contracted out. We identify in particular a need to extend the Human Rights Act and the Freedom of Information Act to cover all organisations providing public services. It is also essential that users are able to make complaints when service provision is inadequate. Meanwhile, there is also a challenge for commissioners in effectively monitoring service provision without insisting on overly onerous reporting requirements which waste time and resources that could be dedicated to helping people in need.

No policy, though, is without its challenges and its risks. We do not believe the risks we have identified are show-stoppers. This report sets out a number of improvements to be made to commissioning processes, but the general direction of government policy appears to us to be positive. Nonetheless, further steps along this path should be accompanied by the collection of much firmer evidence on the impact that third sector delivery is having. We might then be better placed to judge the potential benefits of third sector involvement in service delivery—and whether the rhetoric around transformation of public services is being matched by reality.

1 Introduction

The third sector

1. The third sector is defined by government as comprising ‘non governmental organisations that are value driven and which principally invest their surpluses to further social, environmental and cultural objectives.’¹ This is a deliberately broad term, comprising a wide range of organisations which take different forms and are regulated in quite different ways. These include:

- around 160,000 charities, which are voluntary (trustee) led organisations constituted to provide public benefits defined in law and regulated by the Charity Commission;
- other voluntary and community organisations, carrying out grassroots voluntary action, often on too small a scale to register as charities, and too numerous to count;
- approximately 55,000 social enterprises, which are businesses regulated under company law but which invest surpluses in social, environmental, or cultural objectives; and
- some 8,000 cooperatives and mutuals.

2. The breadth of the sector presents a real challenge for policymakers looking to design the relationship between the sector, citizens and the State. There may be commonalities of approach and of origin between all third sector organisations, but it can be challenging to find common experience between a multi-million pound social enterprise such as Café Direct and a small community organisation relying entirely on volunteer time. Even within the more narrowly defined voluntary and community sector, the small local charity may struggle to identify with larger national charities typified by an organisation like Barnardo’s with an annual income approaching £200 million and over 6000 paid staff.²

3. Despite the challenges raised by the sector’s diversity, governments have shown increasing interest in the third sector, and in harnessing the important contributions it makes to society. A particular landmark in the developing relationship between government and the sector was the publication in 1996 of the report of the Independent Commission on the Future of the Voluntary Sector in England.³ Much of the subsequent course of government policy has derived from that blueprint, including the launch of the Compact in 1998, which sought to agree a broad set of principles governing a better relationship between government and the third sector, and the adoption of a single inclusive definition of charity based around the concept of public benefit. Other significant developments have included an increased emphasis within government on promoting the

1 Cabinet Office, *The future role of the third sector in social and economic regeneration: final report*, July 2007 p.5

2 http://www.barnardos.org.uk/annual_report_and_accounts.pdf

3 NCVO, *Meeting the Challenge of Change: voluntary action into the 21st century*, July 1996

health of the sector, and latterly the appointment of the first dedicated Minister for the Third Sector in 2006.

4. Our interest as a Committee in the Government's policy towards the sector stems from the appointment of a dedicated minister, with the associated creation of the Office of the Third Sector in the Cabinet Office. Although we are not a departmental select committee, we examine the policy, administration and expenditure of the Cabinet Office as part of our wider task of scrutinising the operation of the Civil Service and of the public services it manages. The emergence of the Office of the Third Sector, bringing together responsibilities then held in the Home Office and Department for Trade and Industry, has both crystallised the development of government policy, and encouraged us to engage with that process of policy development. Scrutiny of the Office of the Third Sector, the Charity Commission and the wider relationship between the State and the sector has now become a central part of our role, and we are glad to have established a healthy relationship with key areas of government and representative bodies.

Scope of the inquiry

5. Our previous work on different aspects of public service reform has led us to a particular interest in one aspect of the developing relationship between government and the third sector—the role of the sector in delivering public services. Although there is a long history of both not-for-profit organisations and the State providing *services to the public*, the last decade has been notable for the increased emphasis on the delivery of *public services* by third sector organisations—a distinction we explain at paragraph 13. In particular, there has been an emphasis on *commissioning* services from the sector, as opposed to simply procuring services or providing funding to be used by organisations at their discretion.

6. The Government's push to do this is part of a wider policy agenda of contestability, or opening up markets for public services to new suppliers from the private and third sectors to create public service industries. However, the desire to involve the third sector in service design and delivery also reflects a belief that third sector organisations have distinctive strengths which, harnessed correctly, have the potential to contribute to the “transformation” of service delivery.

7. In this inquiry we set out to scrutinise the desirability and achievability of the Government's vision for third sector involvement in public service delivery. That vision is complex. Its central plank, according to the Office of the Third Sector, is that the sector deserves parity of treatment with other sectors:

At the heart of this action plan is the principle that where services are commissioned and procured by government, there must be a level playing field for all providers, regardless of sector.⁴

At the same time, the Government has argued that Third Sector Organisations (TSOs) bring many distinctive qualities to the table which can provide better outcomes for service users, and that therefore measures should be taken to encourage and enable more TSOs to take on service delivery. We have set out to consider these questions from the perspective

4 Cabinet Office, *Partnership in Public Services: an action plan for third sector involvement*, December 2006, p 3

of service users and of citizens. Our central question was whether the sector should be involved in service delivery to a greater, similar or lesser extent than it is now—and how the ideal position could be achieved. We address this over the course of the report:

- Chapter 2 provides a brief background to the current position, looking at the changing relationship over time between government and the third sector;
- Chapter 3 sets out the Government's vision of the third sector's role in public services delivery—broadly, that it has distinctive qualities which may help “transform” public services;
- Chapter 4 focuses on one aspect of the Government's vision, by concentrating on the proposed scale of change which is being suggested;
- Chapter 5 attempts to assess the claim that third sector organisations can and do offer distinctive ways of providing services with better outcomes for service users;
- Chapter 6 then looks at the barriers which may be preventing the Government from getting the best out of the third sector as a possible provider of services, and asks whether it is ever possible to achieve a level playing field;
- Chapter 7 sets out some constructive suggestions for improving commissioning; and
- Chapter 8 concludes our survey by examining some of the risks associated with involving the third sector in service delivery—whether to service users, to the Government, to the sector, or to citizens more widely.

8. This inquiry is the first we have undertaken since taking on responsibility for scrutinising third sector policy. We have benefited enormously from the support of the National Audit Office, itself still finding its feet in this developing policy area. We are particularly grateful to Andrew Denney, whose expertise has been invaluable and who has made a significant time commitment to our inquiry.

9. We are also grateful to all of our witnesses, and all those who submitted written evidence for our consideration. We received more than 50 written responses to our call for evidence, while other organisations were represented at a seminar we held in May 2007. Subsequently we heard oral evidence from:

- Front line third sector organisations, large and small;
- Third sector representative bodies, operating nationally and locally;
- The Office of the Third Sector and some of its sponsored bodies/contractors;
- Wider stakeholders, including trade unions, the Commissioning Joint Committee and the Confederation of British Industry (CBI); and
- The Minister for the Cabinet Office and Minister for the Third Sector.

10. We have also been able to draw on earlier work relevant to this inquiry. We and our predecessor Committees have been scrutinising the delivery of public services for some

time, most recently in our inquiry *Public Services: Putting People First*, on which we have produced two reports and will shortly produce a third.⁵ Many of the issues around commissioning services from the third sector are familiar to us from an inquiry into *Choice, Voice and Public Services* in 2004–5, which considered questions around the principle and practice of opening up the delivery of public services beyond public sector providers.⁶ However, we have avoided duplicating the work of those past inquiries, and we concentrate on issues specific to the commissioning of services from the third sector.

11. Public service delivery is only one aspect of the wider contribution the third sector makes to society. We have already taken evidence on other third sector-specific subjects such as the Charity Commission’s guidance on public benefit and the rules applying to political campaigning by charities, and we intend to maintain an ongoing programme of work relating to the sector.

5 Fifth Report of Session 2007–08, *When Citizens Complain*, HC 409, March 2008; Sixth Report of Session 2007–08, *User Involvement in Public Services*, HC 410, May 2008

6 Fourth Report of Session 2004–05, *Choice, Voice and Public Services*, HC 49, March 2005

2 Government and the third sector

A tradition of service provision

12. While the term “third sector” remains relatively new, the ethos it attempts to capture is well established. Independent, voluntary, altruistic action has deep traditions in the cultures and religions of this and other countries. A great part of that tradition—sometimes referred to as “good works”—is the provision of services to the public. Whether in the relief of poverty, the provision of education or rudimentary attempts at healthcare, there is a long and fine history of people in Britain and elsewhere voluntarily coming together to serve others who are less fortunate than themselves. Peter Kyle from the Association of Chief Executives of Voluntary Organisations (acevo), for example, told us that one of acevo’s member organisations had been delivering services to the public since 1273.⁷

13. Providing “services to the public”, however, is not the same thing as providing “public services”. Public services, crucially, are funded by the taxpayer, and the responsibility for ensuring that they are delivered to every citizen who needs them lies with the State. A hospice, for example, provides a very valuable service, not only to the individuals it cares for and their families but to the public at large, who are widely positive about the hospice movement—but hospices are not public services because the State does not guarantee that the services of a hospice are available to all those who need them. The State will, however, provide palliative care for terminally ill patients in NHS hospitals, and that means that palliative care is a public service. This terminological discussion is important because while the third sector has a long history in providing services to the public, the presumption since at least 1945 has been that public services were normally provided by the public sector.

14. There remain significant elements of the third sector that do not need to have relations with the State. The latest data from the National Council of Voluntary Organisations (NCVO) showed that in 2005–06 public funding for the third sector made up around £11 billion, while the sector’s overall income was just under £31 billion.⁸ Charitable income allows for independent action as varied as the provision of a children’s play area at a community level, right up to major disaster relief efforts at the international level. A majority of Third Sector Organisations (TSOs) do not derive any of their funding from the public purse, even when they are providing life changing services such as Guide Dogs for the Blind, or life saving ones such as the Royal National Lifeboat Institution.

15. A common sequence of events, however, has been that services to the public developed through voluntary action, and subsequently came to be taken on as public services—the responsibilities of the State. Obvious examples include social housing, schooling and hospitals; indeed, during the course of our inquiry the philanthropically founded Royal Free Hospital in London celebrated its centenary, while the National Health Service (of which it is now a part) turned 60. The charity Rainer told us that their predecessor body the Royal Philanthropic Society pioneered rehabilitative services for offenders as far back as

7 Q 422

8 National Council for Voluntary Organisations, *The UK Civil Society Almanac 2008*, p 1, p 5

1788. What grew from this and became known as probation services was subsequently adopted as the responsibility of the State. Tom Levitt, Member for High Peak, expressed this narrative succinctly:

It is the public sector that has arrived late at the feast. As it grew in power, reach and wealth throughout the 20th century it became the dominant force; taxation rather than charity became the embodiment of “from each according to his means to each according to his needs.”⁹

Financial relations between government and the third sector

16. As we have noted, some £11 billion in public funding flowed into the third sector in 2005/06. This financial support was usually for one of three things:

- Support for a third sector organisation in the round, to be spent however is seen as fit;
- Support for a particular project or service proposed by a third sector organisation; or
- Payment to a third sector organisation to deliver a specified service on behalf of the public sector.

17. Government has a long history of making funding available to third sector organisations, both to support their ongoing existence and to support specific activities which government feels can make a complementary addition to its own aims and objectives. Since 1968, for example, the Department of Health’s Section 64 grant programme has provided funding for projects that will complement statutory services and make a difference to health and social care in England in specified priority areas.¹⁰ The programme also provides unrestricted grants to contribute towards core administrative costs of national voluntary organisations operating in the health and social care sector.¹¹

18. Programmes such as these often support innovative ideas which go on to become statutory services in the way we have outlined. Rt Hon Ed Miliband MP, Minister for the Cabinet Office, reflected how this kind of process had been instrumental in developing childcare services which have increasingly been funded by the State.¹² In practical terms the role played by a public body in this kind of relationship, whether through an unrestricted grant or a funding arrangement which is more specifically tied to the delivery of a particular project or activity, is similar to that of any other private donor wishing to provide support for a good cause. The NAO calls these “donor type” relationships, building on the work of Julia Unwin who refers to them as “giving” relationships,¹³ but the critical distinction is that the idea or requirement for the project comes from the third sector itself.

9 Ev 283

10 Department of Health, *Section 64 General Scheme of Grants: Funding Priorities for 2008–09*

11 Department of Health, *Section 64 General Scheme of Grants: Notes of Guidance 2008–09*

12 Q 349

13 National Audit Office, *The implementation of Full Cost Recovery*, June 2007; Julia Unwin, *The grantmaking tango: Issues for funders*, Baring Foundation, June 2004

19. The alternative to this “giving” relationship is for third sector organisations to deliver services for which the idea or requirement comes not from the organisations themselves but from the State, as a customer rather than a sponsor. Sometimes this is a natural step when the State takes on responsibility for services first developed in the sector. As Joyce Moseley from Rainer described, her organisation developed bail and remand services for young offenders before it was a statutory responsibility, and then went on to deliver some services on behalf of government when it did become a statutory service.¹⁴ The Doncaster Supporting People Provider Forum similarly explain how Supporting People services delivered on behalf of government “grew up” in the sector in the same way.¹⁵

20. As well as adopting and continuing to run services developed outside the statutory sector, government’s move towards improving public services through competition and external provision provided third sector organisations with the opportunity to deliver mature, existing services previously delivered on a large scale by public authorities. Some major areas where this has occurred have included social care services and social housing. More recently, contracting out in areas such as waste and leisure services have provided opportunities for the foundation and growth of social enterprises. In either case the nature of the relationship is substantially different from the donor-type relationship outlined above. Here, demand for the service is coming from the State, which specifies what it requires and buys those services from a third sector provider. In practical terms the role of the third sector organisation is no different to a private sector provider; indeed they may be competing against such private providers to deliver such services. The NAO calls these “procurement type” relationships, while Julia Unwin refers to them as “shopping” relationships.¹⁶

21. The extent to which third sector organisations choose to partner with the State, whether under donor-type or procurement-type relationships, has an effect on the shape of the sector. The Charity Finance Directors’ Group describes how ‘two types of charities are emerging: those that raise significant income through government funding...and those operational charities that raise a majority of their income through voluntary donations.’¹⁷ A range of the frontline witnesses we heard from demonstrate this spread of approach:

- The social enterprise Turning Point told us they received 97% of their funding from contracts and grants from central or local government;¹⁸
- Barnardo’s receive 55% of their funding from the State;¹⁹
- The Emmaus UK Federation received just 2.4% of its funding in 2007 from the State.²⁰

14 Q 5

15 Ev 220

16 National Audit Office, *The implementation of Full Cost Recovery*, June 2007

17 Ev 198

18 Ev 116

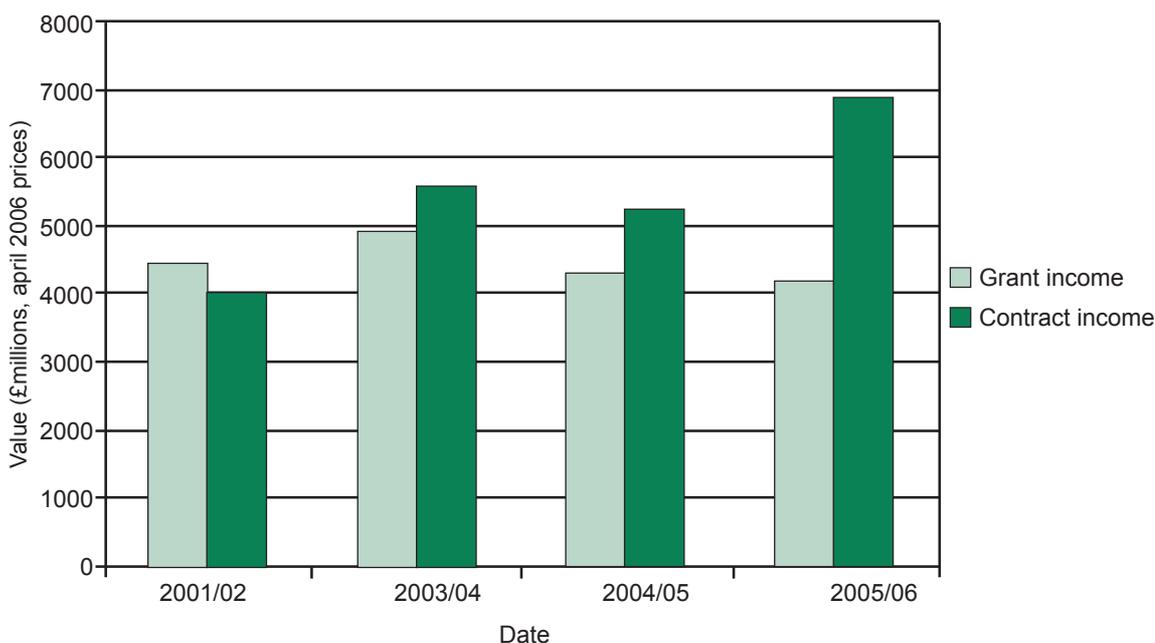
19 Ev 142

20 http://www.emmaus.org.uk/assets/files/EmmausAnnualReview_2007.pdf

22. In recent years there has been a significant growth in public funding flowing to the third sector through the range of relationships we have outlined. Stuart Etherington, the Chief Executive of the NCVO, told us that public sector funding had expanded from around £4 billion to around £10 billion in the 10-year period up to 2005–06.²¹ Crime Reduction Initiatives, an organisation delivering substance misuse outreach and treatment services on behalf of government, described how they and their users had benefited from this expansion, as funding their work through voluntary donations could be problematic as their service users’ ‘behaviour and life styles evince little public sympathy.’²² Even Barnardo’s, which in contrast enjoys tremendous public profile and sympathy, told us that ‘much of the work we do could not be done if there were not a public commissioner willing to pay for it.’²³

23. Most of the recent growth in the public funding of the third sector has been driven by an increase in the procurement type relationships. Table 1 demonstrates the extent to which “shopping” relationships are outgrowing “giving” ones:

Table 1: Trends in voluntary sector income through grants and contracts, 2001–06



Source: NCVO, UK Civil Society Almanac 2008

24. It is clear that the State is commissioning more services from the third sector than ever before, and is increasingly doing so through procurement-type relationships. These commissioning trends, and their impact on the third sector, are at the heart of this report.

21 Q 428

22 Ev 219

23 Q 260

3 The Government vision

25. The Government's vision for the involvement of the third sector in public service reform has developed across the last three Spending Review rounds through a series of policy statements:

- The Government first set a target for the contribution of the voluntary and community sector to public service delivery in 2002, after a “cross cutting review” of the role of the voluntary sector in service delivery which was part of that year's Spending Review (SR02). The target was to “increase the contribution of the voluntary and community sector to the delivery of public services ... by 5% by 2005–06”.²⁴ The Active Community Directorate (ACD) at the Home Office received £188m over the three years to 2005/06—an annual average real terms increase of 20%—and a further £125m was earmarked for the creation of Futurebuilders, then described as “a new one-off three-year fund to assist VCOs in their public service work”.²⁵
- The quantifiable element of the Government's target was shelved in the 2004 Spending Review (SR04), but the target of increasing the capacity and contribution of the sector was renewed. Responsibility for achieving that target has subsequently been passed to the Cabinet Office, which reports that it is “too early to tell” whether the target is on course to be met.²⁶
- A series of commitments were made in December 2006's public services delivery action plan, which remains the definitive guide to the Government vision.²⁷ These commitments included training 2000 key commissioners, creating a range of standard contracts, and developing departmental commissioning frameworks.
- The most recent articulation of the Government's vision came in autumn 2007's Third Sector Review—government's largest ever consultation of the sector.²⁸

26. There appear to be two main propositions recurring in all of these publications: that the third sector brings distinctive qualities to public service delivery, and that the use of third sector deliverers in certain circumstances can transform public services. Such propositions can only be understood properly in the context of the Government's general approach to the delivery of public services.

The context: public service reform

27. The emphasis on involving the third sector in the delivery of public services is part of a wider public service reform agenda. This agenda is fluid and clearly the subject of debate within and outside government, with some argument over whether the change of Prime

24 <http://www.homeoffice.gov.uk/documents/>

25 http://www.hm-treasury.gov.uk/spending_review

26 Cabinet Office, *Autumn Performance Report 2007*, December 2007

27 Cabinet Office, *Partnership in Public Services: an action plan for third sector involvement*, December 2006

28 Cabinet Office, *The future role of the third sector in social and economic regeneration: final report*, July 2007

Minister in 2007 has brought significant changes of direction. We do not need for the purposes of this report to get involved in that argument; it is sufficient to say that some principles were set out in March 2007's Policy Review for the future direction of public services, and that those principles still appear consistent with the direction of government policy today. The review said that the Government should:

- Take further steps to empower citizens to shape services around them;
- Open up the supply side, where appropriate;
- Foster workforce innovation and development, and engage with public service workers;
- Help the hardest to reach; and
- Balance rights and responsibilities.²⁹

We have considered the appropriateness and application of some of these principles in previous inquiries, most recently in our inquiry Public Services: Putting People First, on which we have produced two reports and will shortly produce a third.³⁰

28. Involving the third sector in service delivery is part of opening up the supply side; but that is not the only justification for the Government's promotion of the sector as service deliverer. The sector is also seen as having particular strengths which will aid the achievement of some of government's other objectives for public services. Notably, the Government believes that the third sector has particular strengths in empowering citizens, in innovation, and in helping the hardest to reach. These strengths, and others, are often summarised as the "distinctive" qualities of the third sector. We look in more detail at the question of distinctiveness in chapter 5.

The goal: transformation of public services

29. The benefits of opening up the market in public service delivery are intended to be more than just financial. While in the past the development of a market has been justified on the grounds of driving down costs, which is a legitimate goal in itself, the aim of involving the third sector is also about improving the quality of services for their users. Government hopes—ambitiously—that the distinctiveness of third sector organisations will have a "transformative" effect on public service delivery. The Office of the Third Sector Action Plan sets out opportunities for "transformation" in five key policy areas, shown in the box below.

29 Cabinet Office, *Building on Progress: Public Services*, March 2007, p 7

30 Fifth Report of Session 2007–08, *When Citizens Complain*, HC 409, March 2008; Sixth Report of Session 2007–08, *User Involvement in Public Services*, HC 410, May 2008

**Opportunities for contributing to public service transformation
(identified in Office of the Third Sector Action Plan, December 2006)**

Correctional services: this includes probation services and offender learning schemes

Employment services: including training, information provision and supporting jobseekers through programmes such as Pathways to Work

Children's services, education and training

Health & social care

Local public services—such as local transport, waste management, and supporting vulnerable people

30. We asked Phil Hope MP, the Minister for the Third Sector, if a goal of “transformation” was realistic and credible. He told us that it was an aspiration:

It may be a hostage to fortune ... but I guess my feeling is that if we really do want to aspire to serve our communities to the very best then we should aspire to service transformation.³¹

31. The key sector representatives share the Government's language of aspiration and transformation. The NCVO has published a paper entitled “How voluntary and community organisations can help transform public services”,³² while acevo argue that ‘third sector organisations can and should play a major role in transforming public services’.³³ It is important that the suggestion made by government and by the sector is not that third sector organisations can transform public services themselves, but only that they can help to transform services. Nonetheless, even if the Government concedes that transformation of public services cannot solely be achieved by better use of the third sector, the proposition is that involving the third sector in some services can have a “transformative” effect. We consider what that might mean in chapter 4.

The method: commissioning

32. Much of the government's policy for getting the best out of the third sector can be summarised in one word: commissioning. There are other aspects—the Third Sector Review spoke of “multiple roles of the third sector in transforming public services”,³⁴ including as campaigners for change and as innovators from which the public sector can learn—but it is clear that commissioning services is the primary tool the Government intends to employ in harnessing the third sector's transformative potential. Unfortunately, it is less clear exactly what the term “commissioning” is taken to mean.

31 Q 354

32 Ev 155

33 Ev 151

34 Cabinet Office and HM Treasury, *The future role of the third sector in social and economic regeneration: final report*, Cm 7189, July 2007, para 4.10

33. In the context of public service delivery, the term “commissioning” has a specific technical definition. In the context of our inquiry into commissioning public services from the third sector, however, we have found the term to be used more broadly and in a varied way across the evidence we have received. It appears that a shared understanding across the sector of what commissioning means is still somewhat under construction.

34. The Baring Foundation were among several witnesses to suggest that the terms used to describe the various mechanisms for transferring funding to the sector are often applied in a confusing way. They interpret commissioning as synonymous with the Treasury’s definition of procurement:

The Select Committee’s inquiry defines its focus as “commissioning”. A recent HM Treasury report which sought to provide guidance on improving financial relationships with the third sector used the word “procurement”. We take both terms to mean the process of “acquiring goods and services in line with the government’s policy of value for money, normally achieved through competition”.³⁵

35. This approach has resonance with the use of the term commissioning in much of the evidence submitted to this inquiry by frontline organisations. However, the Treasury guidance from which the definition of procurement is drawn, while not defining commissioning separately, does appear to recognise it as something distinct from procurement. Specifically, it suggests that commissioning is a process that comes *before* procurement.³⁶

36. The Commissioning Joint Committee (CJC), a body drawing together representatives from across all the disciplines involved in the commissioning of local authority services, also draws this distinction, defining commissioning as:

the process of deciding what work or services are needed; whether they should be sought by delegation, the use or setting up of some new body, or by competition; and, if by competition, what sort of contract to use.

This definition is distinct from, though related to and overlapping with, the CJC’s definition of procurement:

the complete process involved in identifying the business need to make a purchase, including market research, specification, purchasing, and subsequent contract management.³⁷

The inference from these definitions is that commissioning is an “upstream” process of intelligence gathering and needs assessment which may then result in a “downstream” procurement process if competition is indeed thought to be the best way to provide the service needs identified. A fairly similar inference can be drawn from the preferred definition of the new Institute of Commissioning Professionals, which is that

35 Ev 174

36 HM Treasury, *Improving financial relationships with the third sector: guidance to funders and purchasers*, May 2006, p 14

37 Commissioning Joint Committee, *Glossary of terms used in Planning and Delivering Public Services* - http://www.cipfa.org.uk/pt/cjc/download/planning_services_glossary_dec_2005.doc

commissioning means “securing the services that most appropriately address the needs and wishes of the individual service user, making use of market intelligence and research, and planning accordingly”.³⁸

37. Inherent in this definition of commissioning is that it does not necessarily lead to a decision to launch a competition or issue a contract. It might be that the needs identified in the commissioning process are felt to be best met by statutory sector provision. Moreover, where external provision is thought appropriate, commissioners have opportunities to use procurement or donor type relationships as appropriate. In our evidence, however, use of donor-type funding and grants is often discussed as an alternative to commissioning rather than a potential outcome of it. In their thought-provoking submission to us arguing for ‘clearer, more discriminating thinking about commissioning’, Community Links attempted to square the circle by effectively laying the blame at commissioners’ doors:

If a very high proportion of the elements are pre-specified by the funder and there are no significant elements of flexibility, the use of the term “commissioning” is rhetorical and confusing and “tendering” would seem to be ... the more accurate description.³⁹

38. Lord Adebowale told us that the first thing that needed to be done to improve commissioning was to define it satisfactorily.⁴⁰ This is clearly important. Although there are some exceptions, many third sector organisations seem to see commissioning as coterminous with procurement, whereas most commissioners do not. Of course, Government also commissions services from the private sector. **If there is no common understanding of what commissioning means, that can only be a barrier to effective relationships. Government and the private and third sectors need to come to a commonly accepted definition of commissioning if it is to continue to be the State’s preferred method of interacting with the sector. In particular, Government needs to convince the third sector that commissioning is something distinct from procurement.**

38 www.iocp.co.uk

39 Ev 215

40 Q 33

4 The scale of third sector involvement

Rolling back the State?

39. The rhetoric of “transformation” could easily be taken to imply that the Government was looking to transfer whole swathes of services out of the public sector and in to the third or private sectors. Taken to extremes, this might suggest a reversal of the process of government taking responsibility for services first developed in the third sector (as described in paragraph 5). We heard evidence to this effect from Dave Prentis, the general secretary of Unison:

In a nutshell, is this really about rolling back the frontiers of the State or is it about public service improvement? We would argue very strongly that it is about an ideological rolling back of the frontiers of the State and not at all about improving services.⁴¹

40. It was beyond the remit of this inquiry to consider the ideological motivation behind the drive to open up competition between suppliers in a public services market. We have considered such issues before.⁴² This inquiry has been limited to the particular role of the third sector in the delivery of public services. As we have noted, the provision of services by third sector organisations is only one part of the service transformation agenda, but it is a growing part of that agenda. The value of government contracts for third sector organisations has been rising steeply: from around £2 billion in 1996/97 to £6.884 billion in 2005/06, the latest year for which such figures are available.⁴³ This is certainly of great significance to the sector.

41. The apparent pace of change has led many to question whether there has been a shift away from a tradition of the third sector providing valuable “niche” services—filling gaps in statutory provision, often with a view to those services eventually being provided by the State—and towards the provision of “mainstream” public services through third sector organisations. Martin Narey, the Chief Executive of Barnardo’s and an enthusiastic advocate of commissioning services, saw such a development as positive:

I do not agree with the niche point, there is no reason why the voluntary sector cannot work in very wide-ranging services and in a whole range of activities.⁴⁴

42. The suggestion that the sector is moving into mainstream service provision is further fuelled by the Government’s refusal to rule out any particular services as being unsuitable for provision by third sector organisations. Campbell Robb, the Director General of the Office of the Third Sector, told us that government had ‘never ruled anything in or ruled anything out’ in terms of areas where it would be inappropriate for the third sector to take on roles currently delivered by the State.⁴⁵ Ed Miliband echoed this, explaining that the five

41 Q 91

42 Fourth Report of Session 2004–05, *Choice, Voice and Public Services*, HC 49, March 2005

43 National Council for Voluntary Organisations, *The UK Civil Society Almanac 2008*, p 38; Q 428

44 Q 203

45 Q 171

broad policy areas identified for growth in the Third Sector Action Plan “were not a finite list but rather an indication of where some significant opportunities lie to use the skills and expertise of the third sector”.⁴⁶

43. Yet it was clear under questioning that ministers had drawn some limits, even if not clearly defined, to the scope for third sector involvement. For example, Mr Miliband thought that it was highly unlikely that the Fire Service would be run by the third sector during his political career.⁴⁷ Similarly, he mentioned national defence as an area where it made sense to have a uniform pattern of activity and centralised structure, not usually cited as strengths of the third sector.⁴⁸

44. Stuart Etherington, the Chief Executive of the NCVO, explained why, in practice, there were limits as to how far the Government might look to expand the role of the third sector:

I do not think there will be this massive step-change that is being talked about. I think it will be far more incremental than that ... You are talking about very different types of animal ...

The sector does not do everything that the public sector does or should. If I am a taxpayer, I would expect a similar type of service, with a similar response, in Newport as I would in Penzance. But we do not do everything. We do discretion. The voluntary sector is not about equity ...⁴⁹

45. The truth is that the scale of change being proposed is easily exaggerated. This may be down to the language of transformation and the refusal to rule out any services from transfer or to set a limit in terms of a proportion of public spending. Yet we heard that the actual proportion of public spending going to the third sector, although rising, is still in the region of 2%.⁵⁰ This figure puts the whole debate into context. Campbell Robb stressed that ‘the third sector is tiny in comparison to the public sector, and the amount that is delivered is still tiny in comparison to what is delivered by the private sector’.⁵¹ If the programme truly is rolling back the boundaries of the State, it is curiously under-powered. There is a marked contrast here with the language now being used by the Opposition, who talk of re-branding the sector as the First Sector and looking to open up the delivery of a wide range of services.⁵²

46. Even within the third sector itself there is some scepticism about the idea of a transformation in the scale of activity. Joyce Moseley from Rainer felt that some provision was ‘going the other way actually and getting taken back in house’.⁵³ Lord Adebawale (from the social enterprise Turning Point), who has also been at the forefront of the debate on this agenda, told us:

46 Ev 149

47 Q 347

48 Q 345

49 Q 457

50 Q 113, Q 457

51 Q132

52 Conservative Party, *Voluntary Action in the 21st Century*, June 2008

53 Q 42

I think “hype” might be a good word actually in the sense that I have not noticed any massive shift in the paradigm ...⁵⁴

47. Campbell Robb told us that the mass transfer of services to the third sector was “absolutely not” the Government’s intention:

It is not about identifying areas where the whole of that particular service can be taken out. It is about finding those kinds of examples where they really make a difference and, wherever possible, creating the right environment where commissioners and others can have the tools and the organisations to get that to scale if we want it to happen.⁵⁵

Ed Miliband echoed this distinction, telling us that government would not “automatically transfer services into a particular sector because we simply assume in advance that it will always be superior...this is not the basis on which these judgements should be made”.⁵⁶ Richard Gutch, the Chief Executive of Futurebuilders England which was then managing the Futurebuilders fund, told us that the fund only invested in organisations if there was going to be a clear improvement in delivery for service users:

We are not interested in investing in an organisation just so it can take over something that used to be in the public sector and then run it in exactly the same way. We are looking for a significant improvement.⁵⁷

48. As our witnesses told us, third sector organisations are ill-equipped to provide universality and equity to service users. Whatever transformation of public services is about, it should not be about transferring responsibility for delivering large areas of public service out of the State and into the third sector. It appears that government accepts this. Despite the emphasis given in government publications to involving the third sector, only 2% of public service spending is on third sector delivery. The debate on the transformative capacity of the third sector is a rhetorical storm in a fiscal teacup.

49. It is notable that the Government no longer has a quantitative target for the scale of the third sector’s contribution to public service delivery. In 2002 a PSA target was set to raise the sector’s contribution by 5% by 2005–6 (not, admittedly, a hugely challenging target). By the next spending review in 2004, the numerical target had been removed, and the emphasis subtly changed. The Government’s goal became an increase in the capacity of the sector as well as its overall contribution. More recently, there has been a move away from targets for sectoral involvement in particular services; for example, the Ministry of Justice has recently abandoned its target that 10% of probation services under the National Offender Management Service should be delivered by third sector organisations.

50. The Cabinet Secretary, Sir Gus O’Donnell, explained to us that the Government is no longer actively pursuing an absolute increase in the contribution of third sector organisations to the delivery of services:

54 Q 42

55 Q 119

56 Ev 149

57 Q 121

The emphasis in public policy has evolved away from increasing the absolute size of the third sector's contribution to public service delivery, and towards creating a more supportive environment which enables better commissioning of third sector organisations and more ready adoption of third sector innovation where appropriate. This is reflected in the policy programme set out in the third sector review.

An absolute increase in the contribution of third sector organisations to the delivery of public services is not included in the new CSR 2007 PSA indicator for a thriving third sector. Instead we are measuring the proportion of people volunteering and the number of people employed by the sector.⁵⁸

51. This is a significant evolution of policy. **The Government's position has moved from actively pursuing the transfer of services to allowing a more ready transfer "where appropriate". We support that change of emphasis. However, it immediately prompts a further question: how to judge where it is indeed appropriate for services to be provided by the third sector.** We consider this question, in all its complexity, in the next chapter.

5 Third Sector distinctiveness

“My view is that there is nothing that the voluntary sector can do that the public sector or private sector cannot do just as well.”—Martin Narey, Barnardo’s

52. Every Member of Parliament will have experience of excellent work delivered by third sector organisations working in their constituencies. During the course of this inquiry we have also heard a wide range of examples where third sector providers are delivering highly effective services to users including some of the most deprived and vulnerable people in society. However, it is equally apparent that excellence is found across different sectors. In our Skills for Government inquiry, for example, we noted that in the Civil Service “very many excellent things ... are done by excellent people every day”.⁵⁹ The challenge which the State has taken on is to try to identify the areas where involving the third sector in service delivery will improve outcomes for users—ideally, helping to “transform” the service.

Crime Reduction Initiatives (CRI) is a national charity that provides a range of services to support individuals, families and communities whose lives are adversely affected by crime, substance misuse, homelessness, anti-social behaviour, domestic violence, social deprivation and lack of opportunity.

CRI was commissioned to deliver the Drug Interventions Programme (DIP) in Haringey, North London towards the end of 2006. The service includes a core DIP team, structured day programme, specialist prescribing and aftercare service, that was formerly provided by the NHS and Local Authority.

It can be difficult to assess comparative performance on new contracts in part due to variations in the quality of the data left by outgoing providers. However, despite the relatively short period of time that has elapsed, since CRI took over the contract, performance measured against Home Office KPI compact data had clearly improved in respect of all targets.

53. The key concept in the Government’s vision is distinctiveness. Services will not be transformed by a change of provider unless that provider offers something distinctive. This appears to be the primary rationale for looking to the third sector in particular (rather than simply allowing the third sector to participate as a means of widening competition). The Government, as we have seen, believes that there are a number of characteristics which might make third sector organisations particularly suited to public service provision:

- A strong focus on the needs of service users;
- Knowledge and expertise to meet complex personal needs and tackle difficult social issues;
- An ability to be flexible and offer joined-up service delivery;
- The capacity to build users’ trust; and

- The experience and independence to innovate.⁶⁰

Seemingly supporting this, the Commission for Social Care Inspection (CSCI) found in 2005–06 that in all sectors of social care provision—including residential care, nursing care, older people's services, services for younger adults and children's services—voluntary sector providers were meeting a greater percentage of their published standards than either the private or public sectors.⁶¹ The Government also sees “wider benefits” in involving the third sector more, including the generation of social capital and fostering a spirit of voluntarism.

54. Not everybody, though, is convinced that the third sector has something distinctive to offer. The Local Government Association told us that “there is nothing intrinsic in the organisational structure of TSOs which means that they automatically deliver better public services than any other sector”.⁶² The Audit Commission, who must have spent as much time as anyone considering the effectiveness of third sector service delivery, told us that they were “not aware of any evidence that services transferred to the third sector show distinct improvement in quality after that transfer”.⁶³ Even if such evidence were to be found, its meaningfulness would be shrouded by the tendency of local authorities to outsource services that they saw as failing, where the initial transfer would be likely in any circumstances to produce some level of improvement from a poor baseline. Similarly, they were not aware of any evidence that services transferred to the third sector had improved any more significantly than services transferred to the private sector.⁶⁴

55. The strongest denial of distinctiveness, however, came from within the sector itself, from Martin Narey, the Chief Executive of Barnardo's:

My view is that there is nothing that the voluntary sector can do that the public sector or private sector cannot do just as well. There is nothing special about us...

A lot of people in my sector think there is something important about being in the voluntary sector, as if we have a monopoly of compassion, and it is most unfair, we do not.⁶⁵

Mr Narey has a great deal of relevant experience, not just from Barnardo's but also from working for a long time in the public sector, buying services from both the private and the third sectors. Drawing on his experience as a commissioner in the Prisons Service, he reflected how he saw no conflict between profit—the treatment of which is central to the definition of the third sector—and commitment. He felt private providers of prison services were delivering ‘decent, compassionate, value driven services’.⁶⁶ When he tells us

60 Cabinet Office and HM Treasury, *The future role of the third sector in social and economic regeneration: final report*, Cm 7189, July 2007, para 4.6

61 Commission for Social Care Inspection, *State of Social Care in England 2005–06*, January 2007

62 Ev 250

63 Ev 168

64 As above

65 Q 204

66 Q 259

that he has “tried to bury the word distinctive and remove it from the Barnardo’s lexicon”, we are compelled to listen.⁶⁷

56. The parameters of the debate are clear. The remainder of this chapter is concerned with an attempt to assess—through examples, and through more systematic studies where possible—whether the Government and others are right to assert that the third sector can offer distinctiveness in the provision of public services.

The characteristics of the sector

User focus

57. Perhaps the most commonly cited strength of third sector organisations was a strong focus on the needs of service users. This claim was typified by the evidence we received from Swift Health Promotions that TSOs “tend to be client-focused” because there were “fewer operational and political limitations on the help and support they can provide”. The user focus was also linked to the “passion, enthusiasm, generosity of spirit and entrepreneurialism of their workforce (paid or unpaid) in identifying and meeting changing needs.”⁶⁸ The NCVO suggested three more reasons why third sector organisations might be able to demonstrate such a focus:

- the way a particular organisation is set up—for example, many TSOs are founded by people with direct experience of the issue they are seeking to address;
- the way they operate, such as having users on their board, or amongst their staff; or
- because the organisation is based in the local community.⁶⁹

58. FPA, an organisation funded by the Department of Health to provide information to the public and to professionals, described how daily contact with users through their Sexual Health Direct helpline provides them with an overview of concerns about sexual health issues which they are able to share with professionals and policy makers and which informs the content of the information resources they also produce.⁷⁰ Richard Gutch of Futurebuilders England told us that they had invested in Barnet Voice for Mental Health, a safe house for people with mental health problems, run entirely by people with personal experience of mental health problems themselves. Another organisation in which they had invested was Peacemaker, which was doing community cohesion work, and was run by a group of Asian people who were caught up in the Oldham disturbances in the North West.⁷¹ These are undoubtedly organisations which would start from a different perspective to that of a public sector agency.

67 Q 261

68 Ev 276

69 Ev 157

70 Ev 227

71 Q 125

Specialist knowledge and expertise

59. A second government-cited strength of third sector organisations is the knowledge and expertise to meet complex personal needs and tackle difficult social issues. Again, there are numerous examples of such expertise to be found in the sector, such as the example below from the British Red Cross. We also heard from the medium sized national charity Fairbridge that their specialist expertise in tackling behaviour and different learning styles was how every year they win the trust and commitment of over 3,500 young people that most other organisations have found impossible to engage. These include “difficult to reach” 13–25 year olds with multiple needs who are outside education, training or employment.⁷²

The British Red Cross told us about their Swansea Supported Discharge Scheme, commissioned by the Welsh Assembly Government. The scheme supports people with insecure tenancies on discharge from hospital, providing help not only with tenancy issues but with other concurrent problems which are often not otherwise picked up.

They gave an example where their support worker’s expertise allowed them to identify a client’s alcoholism, find her a suitable home and get her life back on track in a way that the public sector had failed to do.

Flexibility and joined-up service delivery

60. A third facet of third sector distinctiveness is the sector’s ability to offer, in the words of acevo’s Peter Kyle, “much more holistic services across the board”.⁷³ Lord Adebowale described how an organisation like Turning Point is able to ‘bring together different funding streams to create sometimes bespoke services that meet the needs of individuals and their communities’. Turning Point’s own Connected Care service was an example of that bespoke response.⁷⁴ Rainer also gave the example of their care leaving services in Surrey where they manage housing provision for care leavers but also bring in social work, personal care and specialist education provision. In addition to the £2.1 million contract for running the service, Rainer was able to access a further £1.2 million from sources such as European institutions which the local authority would have found difficult to access.⁷⁵

The capacity to build users’ trust

61. Another third sector selling point is a capacity to build users’ trust. Joyce Moseley described how many of the young people Rainer deal with, “because of the difficulties they are getting into, see authority figures in whatever state as something they want to avoid”.⁷⁶ Martin Narey told us that he was fairly consistently told by users that they like coming to Barnardo’s because they are not social services. He cited a service in Middlesborough supporting young girls and young men, getting them off the streets where they are subject

72 Ev 224

73 Q 425

74 Qq2–3

75 Q3

76 Q 4

to abuse and prostitution. A number of the young people there apparently said consistently that they would not come to the service “if it was not the name of a voluntary sector provider above the door”.⁷⁷

62. Together (Working for Wellbeing) supports people with mental health needs and delivers specific services to offenders with mental health needs. They gave us a generic explanation of why trust levels might sometimes be higher for third sector organisations, especially in relation to the public sector:

Service-users who have had contact with both the mental health and criminal justice systems have often experienced a significant degree of social exclusion and disadvantage. These experiences may be as a result of their social circumstances, including traumatic and abusive past events, or may be a direct result of the discrimination that they have encountered at the hands of agents of these two systems.⁷⁸

Innovation

63. The final element of the claim of third sector distinctiveness is one which government has often been particularly keen to stress—that the sector offers the experience and independence to innovate. A cursory consideration of the past is enough to demonstrate that many ideas which are now central to statutory provision were incubated in the third sector. Rainer cited needle exchanges, piloted by third sector organisations in London, and family support centres, which were piloted by Shelter and NCH before being rolled out nationally.⁷⁹

Emmaus UK imported into the UK an internationally successful model of communities enabling people to move on from homelessness by providing work and a home in a supportive, family environment.

Companions, as residents are known, work full time collecting renovating and reselling donated furniture. This work supports the Community financially and enables residents to develop skills and rebuild their self-respect.

There are currently 14 Communities open around the UK and several more in development.

64. Help the Hospices gave us reasons why the hospice movement as a collection of voluntary sector organisations might be able to innovate with greater ease than the NHS:

When ideas emerge the relative flexibility of hospice budgets (they may be able to call on reserves or access one-off grants for new work), the commitment of staff and volunteers, and their place in local communities means that they are able to create and deliver innovative services which could not emerge as easily within the NHS.⁸⁰

77 Q 203

78 Ev 281

79 Ev 109

80 Ev 233

The Hospital Management Trust, which owns three acute surgical hospitals in Sheffield, Grimsby and Swansea and runs four nursing care homes, supported this from their own experience in a hospital they once ran in Suffolk. They had been able to develop innovative rehabilitation delivery, day care services, home care services, night sitting and a range of practices “which would have been quite impossible to deliver through the bureaucratic systems within the public sector”.⁸¹

Assessing the evidence on distinctiveness

65. It is clear, then, that many third sector organisations demonstrate the characteristics identified by government as exemplifying the sector’s distinctiveness, and that these can lead to impressive outcomes. What is less clear is whether other sectors do not, or cannot, reach the same levels. In many cases, the empirical basis on which to judge is simply not there. For one thing, there is always a prospect that if commissioning practice were different, organisations might behave differently. Many of the mechanisms for involving users, for example, such as having users on boards, are easily replicated in the public or private sectors. Our recent report on User Involvement in Public Services showed that there are a range of ways in which the public sector is engaging with and involving its users, even if this involvement is inevitably imperfect.⁸² The assumption that third sector organisations have a particular strength in their focus on users is not as clear-cut as many appear to believe.

66. The National Consumer Council (NCC) have recently attempted to address the evidence gap through examining the experience of service users in social housing, employment services and domiciliary care services to find out whether services provided by third sector organisations were indeed distinctive.⁸³ Alison Hopkins (who conducted the research for the NCC) told us that the research was prompted by a sense that the claims made about the distinctiveness and effectiveness of the third sector as a provider of public services were fundamentally anecdotal:

It was all very convincing and all very inspiring, but when one wants to stand back and try and assess and quantify that evidence it is very difficult to do so. There is very little quantitative, statistical evidence on the third sector.⁸⁴

67. Although by no means giving a complete picture, the NCC’s work is a hugely welcome attempt to give some rigour to a sphere where debate has so far, of necessity, too often consisted of assertion and counter-assertion. The NCC’s findings were published in May 2007 and are summarised below:

81 Ev 237

82 Sixth Report of Session 2007–08, *User Involvement in Public Services*, HC 410, May 2008

83 National Consumer Council, *Delivering public services: service users’ experiences of the third sector*, May 2007

84 Q 195

Table 2: Findings of National Consumer Council research

Service Area	Findings
Social Housing	Little difference between performance of public sector and third sector: generally low levels of user satisfaction.
Employment Services	Third sector out-performed private sector in all core service factors; private sector in turn significantly out-performed public sector in all areas.
Domiciliary Care	Little difference in performance of public and third sectors. Private sector providers seen as most responsive, with staff who are most friendly and helpful, and most likely to treat people with dignity & respect.

Source: adapted from NCC

68. Philip Cullum, the NCC’s Deputy Chief Executive, told us that the NCC’s research had not entirely supported the assumption that third sector organisations were particularly user-focused:

Part of the rhetoric around the third sector is an understanding of users and the ability to get close to them. One of the things that we found was that actually that rhetoric in some instances can be rather overblown, particularly when it is being provided to quite a general population like social housing ...

Where it does stand up, it would seem from our research, is where there are groups of people who have quite particular circumstances. In that case that kind of focus on who are the users and what do they really need comes out more strongly.⁸⁵

69. **One of the most commonly cited characteristics of third sector distinctiveness—almost its unique selling point—is the sector’s focus on service users. Yet user focus is not unique to the third sector, and indeed what little research there is suggests that this user focus can be lost when organisations provide services to a large, general population.** Equally, it is hard to measure whether the third sector has an inbuilt advantage in providing specialist knowledge and expertise. This is not something the National Consumer Council’s research attempted to measure. Nobody, though, claims that the third sector has a monopoly on specialism. **If the test of distinctiveness is that the third sector offers more specialist knowledge and expertise than other sectors, then we have not been provided with sufficient evidence to prove that claim.**

70. The NCC’s research *does* tentatively support the notion that the third sector might have an inbuilt advantage in providing a flexible, joined up service. Across employment services, domiciliary care and social housing, users consistently felt that third sector providers were better than other sectors at “providing a flexible service”—important because people’s needs are not always treated holistically by government agencies. However, on other related measures such as “staff who care about you as a person”, third sector organisations were not rated any higher than their competitors by service users. Indeed, in domiciliary care, both the third and public sectors were significantly outperformed by the private

sector on this measure.⁸⁶ Fairbridge told us that when they were commissioned to provide services in Southwark, they “provided a missing ‘joined up-ness’ within the borough that wasn't there before”; but this was “partly due to Fairbridge's work, and partly due to the commissioning process”.⁸⁷ In other words, the impetus for joined up service delivery can come from the State too. **There is some evidence that third sector providers in certain fields provide more flexible, joined-up services. However, flexibility of services seems very dependent on good commissioning practice.**

71. Even in the area of innovation—the very crux of third sector distinctiveness –there is debate as to whether there is an inherent strength within the sector, or whether in fact commissioning practice was more important than who provided the service. The Local Government Association told us about a study carried out by Stephen Osborne at Edinburgh University in 1994, and repeated in 2006, which suggested that ‘innovation is not an inherent characteristic of voluntary organisations, but arises from the policy context created by central and local government’.⁸⁸ The 2006 study also showed that the number of TSOs who state they are involved in innovative activity has fallen considerably. This chimes with observations from Stuart Etherington that innovation comes from involving service users in service design.⁸⁹ The Audit Commission’s work on innovation in local government also found that innovation “tends to come from those who are closest to the users of a service, and often emerges in partnerships. We found evidence of innovation among providers of all kinds, but no particular evidence of greater innovation in the voluntary sector compared with other service providers.”⁹⁰ **The many fine examples of innovative practice in the third sector do not add up to conclusive evidence that the sector is inherently more innovative.** We discuss the question of whether innovation can be bought in chapter 7.

72. The one area where we did identify a potential distinctive strength in the third sector was in its capacity to generate user trust. However, while we can see that offenders and users of mental health services may often not trust the State, the same is not necessarily true of other types of service users. Indeed, given that equity is not intrinsic to the third sector, there are reasons why some people might have more trust in the State. This is backed up by the NCC research, which found that levels of trust in third sector providers were only higher in the field of employment services. In social housing provision, the public sector was just as trusted (or perhaps distrusted), while in domiciliary care the highest levels of trust were once again in private sector providers. There is clearly a need to be cautious with these figures, as the NCC’s sample of service providers is not necessarily entirely representative. Nonetheless, the figures do suggest a pattern, which is that where service users are more likely to have had negative experiences of the State, they are more likely to trust non-public sector providers. **In certain areas, it appears that third sector organisations may indeed be more likely to secure users’ trust than public sector counterparts. It is equally apparent, though, that this is not universal across all forms of**

86 National Consumer Council, *Delivering public services: service users’ experiences of the third sector*, May 2007

87 Ev 225

88 Ev 251

89 See for example Paul Jump, “Sector can't guarantee innovation, says Etherington”, Third Sector Online, 21 June 2007

90 Ev 169

public service provision. Nor is it clear that it is a third sector-specific strength. It may be more accurate to suggest simply that certain types of service users, or would-be service users, may be apprehensive of dealing with the State.

Does size matter?

73. A further strand to the debate on the distinctiveness of the third sector was the issue of whether some third sector organisations are in fact more distinctive than others. In particular, within the voluntary and community sector there was a debate around whether the characteristics of third sector distinctiveness identified by the Government were more likely to be found in small, local organisations than in large national ones. This was certainly the belief of Alex Whinnom of Greater Manchester Centre for Voluntary Organisations, who works on behalf of many such small local organisations. He told us that it was a mistake to conflate the two different types of organisation:

I think the mistake, again, is to think that the big national charities with million pound, multi-million pound turnovers are the same thing in any way as the small local charities ... The philosophy around commissioning public services from the third sector, all the rhetoric, is all about the added value you get from what seems to me to be a description of the small, local charities.⁹¹

74. Mr Whinnom's belief was echoed by one of the Manchester-based local charities he worked with, the Wai Yin Chinese Women's Society. The Wai Yin Chief Executive Sylvia Sham argued that local roots brought distinctive benefits:

Local people, local communities delivering local things, is more valid than people who come from London, from everywhere. They are national organisations. Maybe they do not know what the local situation is. It is not about the skill, the professionalism. I respect them as a national organisation but we think we do the best.⁹²

75. The danger that our witnesses identified was that in pursuing a policy agenda designed to obtain something distinctive, the Government might actually unwittingly damage the existing distinctiveness of the sector by incentivising third sector organisations to grow and become more businesslike in order to win large contracts—thus losing what made them distinctive in the first place. This is not just a hypothetical concern; our visit to New York and Boston showed us that this is a real issue in areas where the third sector becomes a major player in service delivery. We heard complaints from many people in the United States that the sector had been changed by service delivery, becoming too bureaucratic and losing much of what had been special about it. We also heard a similar experience of the United States from Richard Gutch, who had written a report based on the experiences of the United States as long ago as 1990 signalling this experience. He told us that this same thing was happening in certain areas in the UK:

I think we have an example of that, to some extent, with housing associations in this country. They have grown and grown and there has been a need almost to reinvent

91 Q 399

92 Q 399

some of the things that were special about housing associations, in terms of providing for groups of people who are at a real disadvantage in getting access to housing.⁹³

76. Other witnesses, however, cautioned against the view that distinctiveness was in some way a factor of size. Lord Adebowale, who heads one of the largest national third sector organisations, disputed the view that big is necessarily bad:

I would not assume that small charities are any better or any worse than large charities. There are excellent small charities, there are some not very good ones, and vice versa... we would not have got most of the contracts that we have won if we had not evidenced that we understood what was happening locally, that we had developed partnerships or relationships with small local charities and that we were working alongside them.⁹⁴

Acevo's Peter Kyle warned us that it was "very easy to stereotype and to pigeonhole different charities based on size or ethos or background", but that it was not necessarily helpful to service users to do so.⁹⁵

77. Perhaps the most helpful overview we heard came from Stuart Etherington, who told us that while there might be a tendency for different characteristics to be present in organisations of different sizes, this did not equate simply to "small good/large bad":

I think it is easy to oversimplify the argument, in a sense, between large and small. I view this as, sort of, 'horses for courses'. The purpose of public services is to provide good services for citizens in a way that is responsive to their needs ... some organisations are better at providing different sorts of services.

Let me give you an example: if you want local tailored solutions to particular complex problems, then the probability is that you are going to try to work with smaller, locally based organisations which reflect the needs of local citizens. If you are trying to provide a similar type of service from one place or another, then you may go for a large organisation which has the capability of delivering that type of service.

I think it is easy to fall into a trap about saying, 'This is good' and 'This is bad' when actually you need a more sophisticated evidence base about what works and what types of organisations work effectively in different circumstances.⁹⁶

The recurring theme was the cry for a more sophisticated evidence base.

93 Q 132

94 QQ 8–9

95 Q 413

96 Q 413

“Added value”

78. Aside from the five elements of distinctive service delivery, the Government also believes that involving the third sector in public services has “wider benefits” beyond quality of service provision—a concept which is often described as “added value” or sometimes as “collateral value”. Memorably, the 2004 Review of the Voluntary and Community Sector cited an observation from Einstein that “everything that can be counted does not necessarily count; everything that counts cannot necessarily be counted”.⁹⁷ More prosaically, the Government went on to explain what it considered to be the wider benefits of employing the third sector to deliver services:

- involving local people to build community ownership;
- building the skills and experience of volunteers;
- increasing trust within and across communities, thereby building social capital.⁹⁸

79. The British Red Cross gave us an example of collateral value in action:

Research has found that VCS care in the home services, including those provided by the British Red Cross, are effective in reducing the sense of social isolation, which was repeatedly raised by service users as their prime concern on leaving hospital. The quality of attention and time given by volunteers was found to be crucial to this.

The social contact the service provides was valued as much as the practical assistance, and furthermore the relationship service users form with volunteers was seen as qualitatively different to that with professional staff from health and social care services, being more flexible and diverse in where it took place, and being based simply upon kindness.⁹⁹

Leonard Cheshire described to us how they use their voluntary income to supplement directly contracted services and lever in ancillary services, ‘making them of greater value to the individual beneficiary than if they had been provided directly by the commissioning authority’.¹⁰⁰ This is a form of added value different from those listed by the Government. We also heard at our seminar about Bulky Bob’s, based in Liverpool, who deliver recycling services to the public but also deliver the collateral value of employing ex-offenders.

80. The question which we need to answer is whether delivery through the third sector really does deliver added value, and whether delivery through other sectors does not. Here, it is difficult to be definite. Not all service provision by third sector organisations does provide these wider benefits. Many of the larger service delivery contracts won by the third sector are won by large organisations, not necessarily employing volunteers or building

⁹⁷ HM Treasury, *Exploring the role of the third sector in public service delivery and reform: A discussion document*, 2004 para 4.2

⁹⁸ Cabinet Office and HM Treasury, *The future role of the third sector in social and economic regeneration: final report*, Cm 7189, July 2007, para 4.7

⁹⁹ Ev 185

¹⁰⁰ Ev 242–243

social capital. Martin Narey (again) told us that he was “cautious about joining this chorus which says that we have some sort of added value”.¹⁰¹ The Charity Commission were also concerned that there were some misconceptions around the concept:

Added value does not mean the innate ability of charities to lever in additional funding, or to deliver more for less. Its potential is not present in every charity, waiting for a commissioner to come along and unlock it.¹⁰²

81. Conversely, the type of added value provided by Bulky Bob’s could theoretically at least be provided by other types of provider. There is no reason why, if it was in the contract specification, private sector organisations could not do as Bulky Bob’s do and employ a certain proportion of ex-offenders. Nor do we know a reason why the public sector could not deliver some services on this basis itself.

82. Added value has many facets, from generating social capital and voluntarism to levering in additional income or providing other unexpected but tangible benefits. Third sector organisations are often likely to be best placed to provide some of these benefits; but this may say less about the capability of other sectors than it does about the weakness of commissioning processes. Unless commissioners ask for added value, we cannot really know if it is a distinctive third sector strength. We will look at this in more detail in chapter 7.

Conclusions

83. We started this chapter with Martin Narey’s provocative statement that he did not believe there was anything the voluntary sector could do that the public and private sector could not do, and that he had therefore tried to remove the word “distinctiveness” from the Barnardo’s lexicon. For him, it was competition that drove improvement in services. Joyce Moseley from Rainer, also with experience of commissioning services from the third sector as a Director of Social Services, cast further doubt that any strong results demonstrated by third sector organisations were solely due to intrinsic qualities or distinctiveness. For her, the contracting out of a service, rather than the distinctiveness of who it was contracted to, made a difference compared to in house delivery:

There is something about the fact that you are running a specific service on a contract that gives you a real focus and that focus can dissipate a bit when it is taken back into the more general youth offending team.¹⁰³

84. Perhaps the most emphatic response to that we heard came from the NCVO Chief Executive Stuart Etherington:

The idea that there is broadly no difference at all between these various groups or organisations that are competing to provide public services is stuff and nonsense actually...

101 Q 261

102 Ev 192

103 Q 5

Historically, the voluntary sector has done things in a different way. It tends to involve users more in describing and developing the type of service that it runs. It tends to be slightly more risk-taking in terms of the sorts of services that it provides. It is often more trusted in terms of provision by excluded groups than the state or, indeed, the market.

There are some characteristics, therefore, which I think generally apply to voluntary organisations that are engaged on this. Where Martin is saying “There is no real difference between us; it is all about the construction of contestability,” I think that is very questionable.¹⁰⁴

85. On close examination, though, it is not clear that these two positions are entirely incompatible. The evidence is clear, at least, that third sector organisations are not intrinsically more capable in any way than other organisations—which is Martin Narey’s point—and yet (as Stuart Etherington says) there may well be a tendency for things to be done differently in different sectors. The challenge for the State is to work out what characteristics it wants in the delivery of particular services, and then try to inculcate those characteristics wherever it can.

86. Our attempt to test the Government’s proposition that the third sector offers distinctive characteristics is no more than a first step. We can offer only tentative conclusions warning against hyperbole. **The evidence is simply not there to judge conclusively whether there are shared characteristics across all third sector organisations, arising from their commonality of origins or ethos, which might make them particularly suited to the provision of public services. Indeed, there is widespread consensus that this evidence base does not yet exist. Will Werry of the Commissioning Joint Committee put it most succinctly when he told us that “it is surprising that a major national exercise is based on ... supposition”.**¹⁰⁵

87. **We have already noted that the Government is not looking to transfer any set proportion of services to the third sector. At most, it has identified certain services which it believes third sector organisations may be particularly well placed to provide. This is a more nuanced approach and more sensible than attempting to claim general merits across the whole third sector. Given the absence of useful evidence, too, it is entirely sensible that the Government should no longer set numerical targets for the sector’s contribution to public service delivery.**

88. The work of the National Consumer Council in assessing user preferences is a helpful step in the direction of an evidence base. There is another important dimension, however, which is overlooked in the work of the NCC. While they tested for the same characteristics across domiciliary care, social housing and employment services, the gap may be a failure to identify which of these characteristics were particularly important to the users of each of these services. The Government identified the need for different characteristics in different services in its cross-cutting review of the sector in 2004. We have reproduced its findings as an appendix to this report. There, the Government tried to communicate the complexity of

104 Q 419

105 Qq 89–90

these questions by setting out what relevant “distinctive” characteristics third sector organisations might bring to the table in different service areas. This is the right idea, but approached from the wrong perspective. **The real question in each service should be what characteristics are needed to get the best outcomes for users and for citizens. This might give commissioners an evidence base when they consider what characteristics they might look for when deciding how to commission a service. It is in this direction that research should focus if the policy of encouraging third sector provision is to be pursued.**

6 Levelling the playing field

“If the sector is so good, why are they not winning now?”¹⁰⁶

Will Werry, Commissioning Joint Committee

89. An underlying theme in all of our discussions around the characteristics of the third sector’s supposed distinctiveness was the importance of the commissioning process in determining whether those characteristics came out in practice when services were delivered. Indeed, inconsistency in commissioning practice proved to be one of the primary difficulties in assessing whether certain organisations had inherent strengths in their make-up. If a third sector organisation is not performing distinctively in providing a certain service, it is not always clear whether this is because there is nothing distinctive about the organisation, or because a poorly designed commissioning process stopped that organisation from playing to its distinctive strengths. Equally, where third sector organisations are providing a seemingly distinctive service, it is often unclear as to whether organisations from other sectors might, if commissioning practice were right, be capable of providing a similar service—possibly at a lower price.

90. The principal mechanism through which public service commissioners engage third sector organisations to deliver public services is competition for contracts. Although there is scope in some circumstances for public service contracts to be allocated without competition, those circumstances are severely limited. This is unlikely to change in practice due to EU regulations designed to ensure openness and fairness in procurement, as the Office of Government Commerce (OGC) explained to us:

The EU Directives only allow the direct award of a contract without an advert or competition in specific, highly exceptional circumstances, such as where urgency necessitates an immediate award or where there is only one provider of a particular supply or service. In the former, the Accounting Officer of the public authority would have to be able to justify their action. In the latter, the public authority must be clear that the provider is the only provider of a particular supply or service. In most cases, the only way to test this properly is to run a competitive tender.¹⁰⁷

91. Bad commissioning can prevent commissioners from buying the distinctive qualities they are looking for in the provision of a particular service. Many of the factors preventing the best outcomes for third sector providers were not sector-specific problems and did not require sector-specific solutions. Although some of the weaknesses in commissioning practice identified might in practice be particularly damaging to potential third sector providers, addressing these weaknesses would improve the commissioning process for all concerned—including, most importantly, the end user and the taxpayer.

92. Given the inquiry’s focus on the third sector, however, much of our evidence focused on how the Government could use the commissioning process to get the best out of the third sector in particular, with third sector-specific solutions. In particular, we heard more

¹⁰⁶ Q 68

¹⁰⁷ Ev 263

than once that simply improving commissioning practices would not be enough for the State to reap the benefits of third sector participation in service provision. According to this argument, third sector organisations face particular disadvantages, whether born of commissioning practice or of inherent characteristics, which mean that they will need special treatment from the State for their strengths to be brought out in service delivery. Proponents of this view often claim that this treatment would have the effect of ‘levelling the playing field’.

93. The level playing field has become totemic as a goal for the market in public services. The Office of the Third Sector’s action plan is typical when it proclaims that “at the heart of this action plan is the principle that where services are commissioned and procured by government, there must be a level playing field for all providers, regardless of sector”.¹⁰⁸ Ed Miliband told us that “our policies are aimed at helping those third sector organisations that are well placed to deliver public services, to compete on a level playing field when bidding for contracts”.¹⁰⁹ Very few of the organisations we heard from disputed that this was an appropriate goal of government policy.

94. As we inquired deeper into the question, however, things became more complex. It became clear to us that there was no consensus as to what a level playing field entailed. Indeed, the differences between alternative perceptions of what it meant were so great that, on the one hand, the Commissioning Joint Committee believed that most third sector organisations enjoyed a level playing field already,¹¹⁰ while on the other, Campbell Robb believed that fields could never be entirely level.¹¹¹

95. We do not wish to become bogged down in the semantics of what constitutes a level playing field. No metaphor can be expected to summarise a policy adequately; and yet we have seen surprisingly little discussion as to what this government commitment does and should mean in practice. In particular, there appears to be a confusion between the pursuit of equality of outcomes, so that every sector wins its “fair share” of contracts, and the pursuit of fair procurement processes, which do not provide any sector with a guarantee of a role. It is the latter which the Commissioning Joint Committee told us they believed to be already substantially achieved—but they also told us that this was not enough to achieve the Government’s goals for third sector involvement:

We entirely agree that playing fields have to be level. By this we mean that there must be no unnecessary impediment to serious tenders of any sort; and that, if clients can do anything to help any sort of competent tenderer to compete which does not hinder other such tenderers, then they should do that too.

But this will not be enough to help members of the third sector, except perhaps some of its biggest members, to win more work in competition. What the sector needs is

108 Cabinet Office, *Partnership in Public Services: an action plan for third sector involvement*, December 2006, p 3

109 Ev 149

110 Ev 125

111 Q 181

instead for clients to exercise some of their many legitimate client discretions differently from now.¹¹²

96. This chapter considers difficulties with commissioning processes identified in our inquiry, and the steps that the Government is or could be taking to get better outcomes from third sector involvement in public services. In particular, we heard concerns that commissioners were demonstrating perverse practices, including unnecessarily short-term contracting, denial of full cost recovery and misjudging the most effective scale of contracts. We also heard financial reasons why third sector organisations were not reaching their perceived potential, and that there was a wider power imbalance between third sector organisations and the State which required special protection or promotion for those organisations. We take each of these broad critiques in turn.

“First do no harm”: eliminating perverse practices

97. It was clear from our evidence that many third sector organisations struggle to engage with public procurement processes as currently undertaken. A typical analysis came from the Camberwell-based charity Cambridge House, who reported some of the barriers they have come up against in tendering for their Independent Mental Capacity Advocacy work in London:

- i) Very short turn around of release of tender documents (one only gave a week) to submission.
- ii) 80 page legal contracts that are irrevocable on signing just at the tendering stage.
- iii) Said legal contract puts all the liability on the organisation. We are fortunate in that we have pro bono legal advice—most organisations would not have this. Our legal advisors have been horrified by the language and liability being presented for a £40,000 per year contract compared to what is usual in the private sector.
- iv) In one instance having to pay over £800 to a credit checking agency just be able to submit a tender. We have achieved Gold status which means we have a certificate to say this and can get bumper stickers to confirm it as well. We have had to understandably question the use of charitable funds in paying for this credit check.
- v) Having less than a week’s notice of being called to interview.¹¹³

98. The experiences of Cambridge House are merely illustrative, and do not all represent the experiences of every third sector organisation which has attempted to bid for a public service delivery contract. However, it is immediately apparent that a lot of these practices are damaging to the attempt to get the best out of potential providers. They will put some bidders off; they will waste bidders’ resources; and they will prevent bidders from having the opportunity to really consider what they might bring to the table. Some of these perverse practices will militate against getting the best out of any provider, not necessarily just third sector ones. Small businesses for example may equally struggle. However,

112 Ev 124

113 Ev 190

businesses arguably have clearer incentives—i.e. profits—to find ways to jump through bureaucratic hoops in pursuit of contracts. Third sector organisations are not profit driven and rarely resource-rich, and that hoops that a business might jump through readily may appear more like insurmountable barriers.

99. One example of a third sector-specific perverse practice is the clawback of surpluses, where elements of surplus made under procurement arrangements are expected to be returned to the public funder. Barnardo's told us they had been offered contracts with provisions expecting unspent money to be returned to the commissioner.¹¹⁴ The Charity Commission told us that such practices had been mentioned to them at their conference in March 2006. We cannot imagine commissioners expecting private sector providers to behave in this way; it is understood that private providers will seek to maximise profit to shareholders. Of course third sector organisations do not pursue profits for shareholders, but this does not mean they should be denied any incentive to achieve economies and deliver surpluses for reinvestment. **Public bodies should not be attempting to claw back surpluses from third sector organisations in contractual arrangements.**

100. There is little scope here for debates of principle: procurement practice that specifically discriminates against organisations of any one sector ought to be eradicated. Unfortunately, a number of such practices working against third sector organisations were reported regularly though the evidence we heard. Disappointingly, these are practices which government identified as far back as 2002, when it undertook to work towards addressing them. The avoidance of these practices are also central to the Compact Code on Funding and Procurement to which central and local government funders are expected to have signed up. On the other hand, the issues around these practices are not necessarily as clear-cut as they seem. We concentrate here on two areas which were raised with us repeatedly—multi-year funding, and full cost recovery.

Short-term contracts

101. One potentially perverse aspect of government practice which we heard about throughout the evidence was the short term nature of many contracts commissioners let with third sector organisations. Time and again our witnesses complained that contracts were too short—evidence we heard not just from within the sector, but from public sector bodies like CIPFA¹¹⁵, the Charity Commission, the Commission for the Compact and the Commission for Rural Communities. Nor is this a new phenomenon. The 2002 Treasury Review identified short-term funding as a major problem for third sector organisations and saw renewable one-year contracts as the principal cause for concern. As long ago as June 2005 the NAO was already reporting that progress on achieving longer-term funding was too slow.¹¹⁶

102. Martin Narey—who has experience of long term contracting in the prison service—told us in July 2007 that around 70% of the contracts being delivered by Barnardo's expired the following April:

114 Ev 146

115 The Chartered Institute of Public Finance and Accountability

116 National Audit Office, *Working with the Third Sector*, HC (2005–06) 75, p 45

As things stand in the northwest—and I have no reason to believe that this is very much worse in the rest of the UK—at the moment [July] for about 70 % of our work we do not know whether we will be doing it on 1 April, either because contracts are coming to an end, work is being taken back in house or because local authorities have indicated that they want to continue but they are not sure yet whether or not they will have the funding, and they have within the contracts the ability to give notice to quit if they do not find the money. So it is a very unstable environment.

We now know that Barnardo's lost only 5% of its work in that April, and so the great majority of its contracts were renewed. We have no reason to believe the position of Barnardo's in any of these respects is not typical; a recent Charity Commission survey suggested that around two thirds of contracts were still on a one-year basis.¹¹⁷

103. Both trade unions we heard from also told us about the difficulties for staff of working with such a high level of uncertainty. Rachael Maskell of Unite, which has 60,000 members working in the third sector, asked us to imagine the experience of an employee in that scenario, “wondering at the end of that period how you are going to pay your mortgage, feed your family and what about your own career”.¹¹⁸ Barnardo's put their experience into context by telling us that at the end of January 2008 they had issued redundancy notices to over 100 staff across England, and 261 more staff knew that they might also be issued with redundancy notices. They were subsequently able to withdraw notices as contracts got renewed, but all the staff affected must have feared for their jobs.¹¹⁹ This must affect morale, and the perceived desirability of working in the sector.

104. Possibly more important still than the effect on staff, however, is the effect of uncertainty and change on service users. Debra Allcock Tyler of the Directory of Social Change gave us a poignant example of what this could mean for those who were intended to be the ultimate beneficiaries of this whole policy agenda:

Manju, when she was 13, was raped by her uncle and younger brother, and as a result of that got pregnant. Her family booted her out and she ended up in various psychiatric wards and foster homes and several times tried to commit suicide. She ended up at this particular counselling charity, and had not attempted suicide for about five years as a result of that.

As a result of this contract tendering process that was introduced by the local authority, the particular charity serving Manju did not win it—because the argument became about it not being fair for other charities not to be able to compete for this service. The net effect of that is that [the counsellor] had to go to Manju and say, “I am really sorry, Manju, I can no longer help you” even though the nature of hugely vulnerable people is that they engage in those very special relationships with people.¹²⁰

117 Ev 192

118 Q 61

119 Ev 148

120 Q 428

105. Some contracts are for schemes which are themselves short-term, but too many service delivery contracts still appear to be unnecessarily short. **Nobody seems to be claiming that one-year contracts are generally sensible. Although there are disadvantages of overlong contracts too, in that it is harder to secure accountability to commissioners, there are clear practical problems with the length of many contracts currently. Repeated changes of provider are bad for staff; more importantly, they are bad for service users, who often need to build up relationships with service providers. Nor is it to anyone's advantage if service delivery organisations are unattractive places to work.**

106. Government has talked for some time of a three-year norm for contracts, and longer where appropriate. It is time that this was translated into changed practice. However, we understand that this is not easy. The National Audit Office reported in 2005 that good intentions here were being lost as funding flowed through the delivery chain. The decisions on contract length are made by individual commissioners and not by central government. The priority for the Office of the Third Sector, therefore, must be getting the message through to commissioners on the ground.

Full cost recovery

107. Another area where the State is often accused of not acting in its own best interests is in the enabling of full cost recovery—the principle that payments to third sector organisations should cover the full costs of the services they deliver. Government committed to the principle in 2002 when it asserted a target that by April 2006, all departments would ensure “that the price for contracts reflects the full cost of the service, including the legitimate portion of overhead costs”.¹²¹ However, few third sector organisations report experiencing a consistent commitment to this principle in practice. The evidence of the British Red Cross was typical:

It is important that third sector providers identify and charge for the full cost of providing a service, and essential too that they are able to recover this cost from contractors. Whilst this principle is accepted by government, in practice this has not always been the case, and many government funders remain reluctant to pay proportionate overhead costs within a contract, which presents a long-term challenge to the sustainability of those voluntary sector services.¹²²

108. A recent National Audit Office report on full cost recovery outlined the value for money risks posed to government by failure to meet full costs—both short term risks to the quality and effectiveness of underfunded services, and longer term risks to the sustainability of the service and the market of suppliers willing to provide it. The report found no dispute from commissioners on the fairness of the financial principles underpinning full cost recovery, but did find concerns about what these principles meant in practice. The NAO reported that this was particularly problematic in procurement-type relationships where bidding organisations are not necessarily required to spell out their

121 <http://www.homeoffice.gov.uk/documents/>

122 Ev 187

costs to commissioners, and where third sector organisations may not seek full cost recovery for a number of legitimate reasons.

109. Third sector organisations might for example want to deliver a service beyond the contract specification, and supplement the contractual income with their own money raised by other means. Or they might want to improve their chances of delivering a service for their beneficiaries under contract by bidding at a price that would incur a financial loss and subsidising from charitable funds. The complexity for commissioners therefore is that while they have a responsibility to not put up barriers which may prevent bidders from recovering all of their costs, they also have a responsibility to not discriminate against third sector organisations by requiring they recover their costs if they do not wish to do so. The New Economics Foundation provided us with an example of double-discrimination on this issue, where a commissioning body was demanding third sector bidders priced on a full cost recovery basis while exempting private bidders from this requirement and therefore allowing them to undercut the third sector. Additionally, third sector bidders were told their overheads should not exceed 10 per cent of the price, thus rendering the cost recovery process arbitrary and not based on a realistic assessment of costs at all.¹²³

110. Richard Gutch suggested much of this kind of poor practice was a cultural hangover from relationships that used to be based on grants:

Our overwhelming experience is that commissioners still view the third sector through grant spectacles—they do not treat them in a business-like way—and the kind of contracts that a commercial provider will expect to get—take refuse collection or something, which will be long-term contracts, fully reflecting the costs of the provider in providing the service—are miles away from most of the funding relationships that third sector organisations experience at the moment.¹²⁴

111. This concept of “grant spectacles” may go a long way towards explaining why a sector-specific idea like full cost recovery is often misunderstood in contracting relationships. A similar mentality may be responsible for the practice of clawback (discussed at paragraph 99), which is another hangover from grant funding arrangements. Neither approach represents a professional approach to commissioning. It is interesting too that while the NCVO and acevo continue to call for full cost recovery in their submissions to this inquiry, both organisations have also noted that bidders have a responsibility of their own to understand and reflect their own costs when they put in bids.¹²⁵ This is an important recognition for professionalism around costing and pricing on the part of the sector too. **Commissioners need to lose the habits of grant funding when dealing with third sector organisations in competitive procurement processes. The onus should always be on the bidding organisation to decide how much they want to charge. The responsibility of the commissioner is to ensure that there are neither arbitrary barriers preventing them from doing this, nor discriminatory requirements to compel them to charge their full costs where they may not wish to do so.**

123 Ev 262

124 Q 182

125 Ev 157; Ev 154

112. It is important to recognise that full cost recovery is not a right—it has to exist in a competitive context. While bidding organisations should not be prevented from pricing their full costs into a bid to provide a particular service, commissioners will always retain the right to reject that bid in favour of a cheaper competitor. Government’s commitment to full cost recovery does not, and should not, immunise the third sector from the pressures of efficiency and competition.

113. In a competitive contracting environment, commissioners retain a residual duty to consider and manage the risks that aggressively low bidding might pose to the quality or sustainability of a service or a market, and act accordingly when selecting a preferred provider. However, responsibilities towards organisational sustainability remain the prime responsibility of third sector organisations themselves. This reinforces the importance that bidding organisations understand their full costs before entering the procurement process.

Judging the scale of contracts

114. We began this chapter with Will Werry’s question of why, if the sector had so many qualities, it was not winning now. For Mr Werry, there was a ready answer to his own question: too many things in the procurement process were geared up to bigger contracts for bigger operators.¹²⁶ Again, as on contract length, this argument was put to us by an enormous range of bodies and individuals as a key flaw in commissioning practice which was having a significant deleterious effect on the Government’s intention to get the best out of the third sector. In particular, contracts were seen as being too big for most third sector organisations even when they acted in partnerships—sometimes even when government appeared to have specifically believed that the service was one which third sector providers would be particularly suited to providing.

115. We have cited at paragraph 97 the negative experiences listed by Cambridge House in the procurement processes they had undergone. Despite these difficulties, Cambridge House told us they had been able to equip themselves for tendering processes. However, they were a “large local provider”, and they did not believe others would be in the same position:

We have a huge concern as an organisation that houses and supports a number of other voluntary and community organisations as to how they will participate in such processes.¹²⁷

From his experience of supporting smaller organisations, Alex Whinnom felt the chances of successful engagement with such processes to be ‘hopeless’.¹²⁸

116. Stuart Etherington told us that the drive for scale and efficiency in public procurement represented in some respects a counter-pressure to government’s desire to work more with the third sector:

126 Q 68

127 Ev 190

128 Q 379

Most people in public procurement and commissioning are given, if you like, quite contradictory messages in terms of public policy. On the one hand, it is being argued that we need more efficiency and that efficiency can be created by contestability and therefore we need to do more for less. On the other hand, they are saying, “We quite like the third sector and we think this is quite an interesting way of providing services, so we want you to think about that.”¹²⁹

During the course of our inquiry the Department for Work and Pensions (DWP) conducted a controversial procurement process which illustrated the tension well. Pathways to Work is a DWP programme aimed at getting people on incapacity benefits into work. It is a scheme which was designed to be administered by external contractors, with one contractor charged with administering the scheme in each of the country’s 31 Jobcentre Plus districts. Employment services is an area where the third sector has a history of successful involvement and one where, according to the NCC’s research, the third sector appeared to have distinctive qualities perceived by service users. Indeed, in the pilot of the Pathways programme there had been heavy third sector involvement on which the Government had reported favourably.

117. Nevertheless the sector was, in the words of acevo Chief Executive Stephen Bubb, ‘comprehensively stuffed’ in the first stage of the DWP procurement process, winning just 2 out of the 15 contracts given out at that stage—both to the Shaw Trust. Acevo’s response was to commission an inquiry, chaired by Dame Mavis MacDonald. That inquiry made a number of recommendations including clearer consideration of desired long-term outcomes, the wider use of social clauses and clarity on the extent to which European law allowed government to specifically target third sector providers.¹³⁰ We will come onto each of these later in the report. The subtext, though, is clear—that government operated this particular procurement exercise around contracts too large for many third sector organisations to consider.

118. Invited to comment on the result of this exercise, Ed Miliband told us that there was a tension which government needed to acknowledge between the pressures of efficiency and the need for smaller organisations with local knowledge to be involved.¹³¹ This is a welcome acknowledgement from government that efficiency is not all, and must be balanced against other objectives; but equally, as Dame Mavis MacDonald acknowledged, the third sector needs to recognise that efficiency is a legitimate objective too. **In designing each procurement exercise, the challenge of the commissioning body is to try and determine the trade-off between affordability and service quality to the best possible extent.**

119. In the case of Pathways to Work, the Government was also able to point to a much larger involvement of third sector organisations at a sub-contracting level. We now know that around half of the sub-contractors to the successful primary contractors were third

129 Q 419

130 Acevo and Third Sector leaders, *Independent Inquiry into DWP Pathways to Work Contracting*, November 2007

131 Q 319

sector organisations.¹³² Stuart Etherington intimated that he believed this would be the shape of things to come for third sector involvement in public service delivery:

Where voluntary organisations are increasingly becoming involved is subcontracting: offering to private-sector intermediaries, who are running the contracts. That has been a very significant development over the last couple of years. My own view is that that will continue.¹³³

Moreover he was optimistic that on a commercial and operational level this might not necessarily be a bad thing for third sector organisations, describing one example of a third sector organisation subcontracting with a private provider to DWP:

Interestingly, when I asked the voluntary organisation what was their experience of sub-contracting from a private-sector contractor to the DWP, I expected a sort of torrent of abuse but I was quite surprised: they said, “Oh, no, it’s much better than contracting with the DWP.”

I asked them why and they said, “There are two principal reasons: they do understand that if you are working with the most disadvantaged groups the price should be slightly higher; and they have grasped, unlike the public sector, the notion of cash-flow... You will often find complaints with public sector purchasers, that, because the cash comes in the public sector, they do not understand that organisations can go out of business if they do not get the cash on time¹³⁴

120. Third sector organisations may indeed be treated in a more business-like way in sub-contracting arrangements. However, there are other concerns which need to be considered here, such as the possible removal of the protections embodied in the Compact from a growing proportion of service providing third sector organisations. Sub-contracting also of necessity adds a layer of management, with the potential to increase costs and blur accountability. Meanwhile, another solution for involving smaller or more local organisations is wider use of consortia. Phil Hope told us that consortia “can be a very powerful way that third sector organisations can play a part in these larger contracts”.¹³⁵ He cited the example of Cross-Herts Community Counselling, where six youth and children organisations that provide counselling and advice to young people had got together to bid to deliver services such as sexual health advice to children and young people, aided by an investment from Futurebuilders.¹³⁶ Sylvia Sham told us that Wai Yin had also had a positive experience of forming a consortium:

By working with another ethnic minority group from another partnership ... we put our tender ... more strongly, not only from one ethnic group. We put the tender together for the Learning and Skills Council to get the funding to deliver for about 2,000, as you call them, “hard to reach groups”, to get them from no English to the level of English which is very simple: to go the bank to say, “I want to open an

132 Ev 149

133 Q 419

134 Qq 429, 431

135 Q 321

136 As above

account" or to go to the post office to have a stamp-the simple things they want to learn-and then to progress them into work.

121. **The growth of consortia is encouraging. We do not believe, however, that it is yet at a scale that is going to affect significantly the overall shape of the public services market. It is also costly and time consuming for organisations to come together into consortia.** Alex Whinnom told us that he was involved in a learning consortium in Greater Manchester with around 28 voluntary learning providers in it, including some very small ones which are reaching very hard to reach groups, looking to win contracts from the Learning and Skills Council. Even with 28 providers involved, so that they "could easily handle a contract worth £1 million between us", all the contracts had been on such a large scale that they could not bid for any of them, aside from one about delivering grants to third sector organisations.¹³⁷

122. **It is evident to us that even where there is some evidence that distinctive potential to transform public services does exist, such as in employment services, it risks not being captured due to the nature and scale of the procurement processes in place. Sub-contracts, which third sector organisations are having more success at winning, carry their own risks, and may still be too large for some of the most distinctive organisations; consortia of a sufficient size are hard to establish and maintain. If government wants to involve the smallest organisations who sometimes offer the most distinctive services, it may have to look at doing a number of things:**

- **radically simplifying its tendering processes;**
- **helping organisations to bid, and in particular helping them to form consortia and allowing sufficient time in the commissioning process to do so;**
- **incentivising prime contractors to work with third sector sub-contractors and build their capacity to participate in the commissioning process; or**
- **identifying opportunities to advertise contracts at a significantly smaller level.**

Financial disparities

Access to capital

123. Even beyond simple differences in the size and financial stability of third sector organisations and counterparts particularly in the private sector, there are particular difficulties which third sector organisations will face in the pursuit of large-scale contracts. One commonly mentioned inequality was that in the third sector it was more difficult to access capital. Phil Hope cited this in answer to our question of whether the third sector had any inherent weaknesses:

Access to finance is one area where we have been keen to see if we can improve services and support for third sector organisations. I think that is one of the weaknesses.¹³⁸

124. It does not require much explanation to realise that smaller financial reserves will disadvantage organisations, in that money buys the capacity to bring in new staff and new skills. We heard from Barnardo's that most of their work is won against other third sector organisations. Stuart Etherington told us that it was "simply a fact" that most contracts for service provision were being won by the private sector.¹³⁹ Sylvia Sham spoke eloquently of the challenge for small third sector organisations trying to take on private sector competitors:

It is not like the private sector, where they can employ a group of four people, just sat there all week to write the tender. I cannot do it. I have no money to employ that special consultant to do it, so I lose the tender. All my investment for the staff, training them, all this capacity, what that means is that I put it in the middle of the ocean and I start again.¹⁴⁰

125. Money also helps mitigate any risks associated with service delivery, from the overarching risk that providing a service turns out to be hugely more expensive than originally forecast to the more mundane risk that money will be wasted on bids for contracts that are ultimately not won. On this latter question, it is worth noting that even a large, established and well respected charity like Barnardo's was unsuccessful in 33% of its contract bids in 2006 (91 out of 275). They estimated that the approximate cost to Barnardo's in 2006 of unsuccessful bids was £182,000, or just under 0.1% of their turnover. They also calculated that Barnardo's spends about 1.8% of the total value of a contract in preparing for that bid.¹⁴¹

126. To an extent the problems recounted here are not dissimilar to those that small businesses might face on trying to enter such markets. The Government, though, has been convinced by the case that there are specific difficulties for third sector organisations here, as well as wider public policy reasons for building the capacity of the sector in that it provides benefit to the public in a number of ways (as has long been implicitly recognised through grant funding). Capacity building is therefore about more than just equipping third sector organisations to deliver public services. The Government is committed to improving the capacity of the third sector across all of its identified roles, from campaigning to strengthening communities. Its particular vehicle for investing in the infrastructure of the sector is the ChangeUp fund, which has been delivered since April 2006 by an organisation called Capacitybuilders.

127. The ChangeUp fund was backed by £150 million up to 2008, and a further £83 million has now been allocated over the years covered by the 2007 Comprehensive Spending Review (CSR). The Third Sector Review promised that over the 2007 CSR years

138 Q 358

139 Q 419

140 Q 395

141 Ev 148

Capacitybuilders will have an increased focus on ensuring that infrastructure organisations are equipped to reach down to the smallest third sector organisations, building capacity at a community level.¹⁴² This programme sits alongside work by Regional Development Agencies to support social enterprises and expectations on local authorities to maintain thriving third sectors in their areas. It is a laudable enterprise in its own right. On the other hand, it is unlikely in practice to reach the types of third sector organisations who are doing most of the sector's bidding for service delivery work.

128. The limits of existing capacity building funds were recognised when the Government instituted the Futurebuilders fund following the 2002 cross-cutting review of the sector. Futurebuilders was explicitly set up to improve public service delivery through long-term investment in the third sector, and by the time of the Third Sector Review in 2007 Futurebuilders had made 239 investments totalling £101.9 million to 225 schemes.¹⁴³ Although originally focused on particular services, as of April 2008 the fund is now open to all third sector organisations working to deliver public services. The fund was administered for its first few years by an independent non-profit company called Futurebuilders England Ltd, set up by Charity Bank, the NCVO, Northern Rock Foundation and Unity Trust Bank. However, the organisation lost its bid to deliver the second phase of the scheme, and as of April 2008 the fund is being administered by community lender the Adventure Capital Fund (ACF).

129. Futurebuilders mainly lends money rather than giving grants. Nonetheless, the former Commissioner for the Compact, John Stoker, referred to the scheme as “money put where the Government's mouth is”.¹⁴⁴ Even the CBI, who might be considered to represent the rivals to third sector providers, considered that “if the Government takes the view that the voluntary sector can help with a policy objective and needs to encourage them by pump-priming the market then yes, they should”.¹⁴⁵

130. However, we did not hear universal praise for the Government's steps to build third sector capacity. The Audit Commission told us that the ChangeUp programme had “proved administratively complex” and resources had not filtered through to front line voluntary sector organisations delivering services. The Futurebuilders fund, meanwhile, had “proved unable to help many smaller organisations, who are often unwilling to take on debt obligations”.¹⁴⁶ It may also have been telling that when Selwyn Image of Emmaus pressed us to call for a new attitude towards capital grant funding, in which the State saw itself as a venture capitalist, he made no mention of Futurebuilders, the Government's existing venture capital fund (albeit one directed at organisations bidding for contracts rather than grants).¹⁴⁷

131. Lord Adebawale, whose organisation had made use of Futurebuilders funding, told us that it was a long way short of the funding available to private sector competitors. He called

142 Cabinet Office, *The future role of the third sector in social and economic regeneration: final report*, July 2007, p 93

143 As above, p 66

144 Q 177

145 Q 108

146 Ev 167

147 Qq 375, 409

for a Voluntary Finance Initiative (VFI), equivalent or comparable to the PFI but for third sector organisations:

We have got Futurebuilders which is to be noted as a good thing, but it is by no means anywhere near the financing that the private sector enjoys ... it is venture capital, but it is dwarfed by several orders when it comes to the VFI and PFI; there just is not a comparison.¹⁴⁸

We heard no clamour for a VFI in our inquiry, however. Ultimately, it is not as easy as a third sector organisation as for a private sector counterpart to take financial risks on such a large scale. Local Compact Voice told us that third sector organisations would rarely be in a position to take such risks in practice:

Contractual relationships for delivery of public services usually do not result in Third Sector organisations building a financial reserve over time that is commensurate with the financial penalty accompanying failure to deliver the service, whatever the reason.¹⁴⁹

132. The Charity Commission told us they would be concerned if charity trustees were involved in activities where they did not recognise the degree of financial risk they were running.¹⁵⁰ The Mental Health Provider Forum told us that “the third sector cannot play venture capitalist or take the same financial risk on investment which can make sense for a commercial player.”¹⁵¹ These observations contained a dose of realism, as did those from Cambridge House:

The ‘level playing field approach’ ... is only level if you are a large organisation or have the capacity to become large. This therefore does not include the majority of the third sector.¹⁵²

133. If a level playing field is taken to mean that third sector organisations are able to compete as financial equals with potential providers in other services, then it will never be achieved. Most third sector organisations, including many who have the characteristics government is looking for in service delivery, are too small to compete for most contracts. Capacity-building is important in itself for reasons beyond service delivery, and it has a role in pump-priming particular would-be service providers, but it will not in itself achieve a level playing field in service delivery.

Other disparities

134. Beyond access to capital, we heard other difficulties in attempts by third sector organisations hoping to compete financially with other sectors. The Charity Finance Directors' Group (CFDG), for example, raised the questions of VAT recovery and pensions:

148 Qq 43–44

149 Ev 248

150 Oral evidence taken before the Public Administration Select Committee on 12 July 2007, HC (2006-07) 904-I, Q 3

151 Ev 257

152 Ev 190

The voluntary sector is uniquely disadvantaged because it operates in an environment where there is no level playing field on issues such as pensions and VAT. Voluntary organisations find themselves competing against private sector and other government bodies for the same contracts but without the same terms and conditions.¹⁵³

The CFDG explained to us that a lot of the services provided by charities are either exempt from VAT (ie they cannot charge it, and so cannot recover the VAT that they pay on their purchases), or they are non-business supplies (because the charity does not charge for the service or heavily subsidises it) and are outside the scope of VAT. In either case, the charity ends up with a substantial irrecoverable VAT bill. Commercial organisations providing services do not have this problem as they almost exclusively provide taxable services, while local authorities receive an automatic refund of the VAT that they pay on providing services, many of which are identical to those provided by charities. The Charities' Tax Reform Group (CTRG) estimates that irrecoverable VAT costs charities in excess of £400 million a year.¹⁵⁴ **The suggestion that charities are “almost uniquely penalised” by the VAT regime appears to have some force (although of course charities have their own tax advantages as well).**

135. Pensions, meanwhile, are part of a wider difficulty that third sector organisations might have with requirements under the Transfer of Undertakings (Protection of Employment) Regulations 2006—known as TUPE—to take on staff when services transfer, and maintain their existing levels of salary and benefits.¹⁵⁵ Will Werry told us that TUPE was particularly problematic for third sector organisations because it was “designed to make it not a factor in tender evaluation”, and because the British Government had exercised its right to apply it to pension rights as well.¹⁵⁶ The CBI’s Neil Bentley told us that he was not sure there was the capacity available in the sector with transfers of staff.¹⁵⁷ **TUPE appears likely to cause practical difficulties when services are moved into the third sector. Many organisations will not have the capacity to take on staff at existing levels of salaries and benefits. If the Government is committed to pump-priming the third sector to improve service provision, it will need to invest in supporting third sector organisations who are effectively prevented from delivering services by the requirements of TUPE.**

136. Another problem that third sector organisations sometimes face is the requirement that bidding organisations should be over certain thresholds to enter into competitions. Such thresholds can be set in such a way as to effectively exclude third sector organisations. Peter Kyle gave us one example:

The Olympics, for example, had as one of the rules for entering the commissioning process that you must have a turnover of £5 million for community transport, even as a sub-contractor. There is only one third sector organisation which has a turnover

153 Ev 197

154 Ev 200

155 Transfer of Undertakings (Protection of Employment) Regulations 2006

156 Q 73

157 Q 77

of that size and is in the business of community transport, so lots of other people could not enter the bidding process because of that one rule.

I think that was there for good intentions, and was probably just standard practice, but there is no need to have that qualification in there.¹⁵⁸

Interestingly, the contract to provide the bus service for workers in the Olympics was subsequently awarded to a new social enterprise formed by Ealing Community Transport and Hackney Community Transport. Hugh Sumner, Director of Transport at the Olympic Delivery Authority, was quoted as explaining that the enterprise won the contract “because of its commitment to making a difference to the areas in which it operates, primarily targeting the unemployed locally, who it then recruits and trains to drive its vehicles”.¹⁵⁹ This seem to be an example of intelligent commissioning, taking added value into account, although we do not know if the £5 million turnover requirement had to be dropped in order to achieve this outcome.

137. Several of our witnesses told us that the problem with contractual specifications was particularly prevalent in insurance requirements. Alex Whinnom told us that he had recently filled in an application to deliver city strategy work on learning and skills for a district of Greater Manchester where they required £10 million worth of public liability insurance to qualify.¹⁶⁰ Sylvia Sham told us the cost of this:

To the medium or small organisation, for £10 million insurance it costs us about £5,000. £5,000 to us is quite a lot of money to get the insurance.¹⁶¹

138. Local Compact Voice mentioned to us the suggestion that there could be a Third Sector Insurance Fund.¹⁶² However, such a fund would not be necessary if bidders factored in insurance costs when making their bids. Private sector bidders certainly will do so. The insurer Zurich explained why this is so important:

When community and voluntary sector organisations take on the running of public services they also take on significant amounts of extra risk. This ranges from the day to day operational risks to the macro strategic risks inherent in running such services. An operational risk in a contracted out meals on wheels service could be an increased likelihood of injury to volunteers due to lifting; a strategic risk could include volunteers not arriving at the allotted time and the service being unable to function on a particular day.

Whatever services third sector groups take on they will find that they incur increased risk management cost, whether through increased insurance premiums or in administration time to manage uninsurable strategic risks. Zurich is concerned that this fact is not being understood during the letting of contracts, which is exposing the community and voluntary sector to greatly increased risks with no financial

158 Q 460

159 Helen Warrell, “Social enterprises win London 2012 transport contract”, *Third Sector Online*, 10 April 2008

160 Q 379

161 Q 380

162 Ev 248

recompense. In effect, local and central government could be tempted to outsource the risk, as well as the service, with no commensurate reimbursement.¹⁶³

139. There is a legitimate question of whether government, ultimately responsible for ensuring public services are delivered, can ever really outsource risk. This question is often debated in the context of PFI deals, and boils down ultimately to whether government can ever tolerate a public service failing. This question goes well beyond the scope of this inquiry, although it is clearly of central importance. In the context of this inquiry, the central observation which comes out of Zurich's evidence is that government could, by transferring too many risks onto providers, cause those providers to fail. That would be an undesirable outcome not only for the service provider, but for the commissioning body (who presumably wants the service to be delivered) and for the service user. In practice, therefore, the commissioning authority is always likely to step in rather than allow the provider to fail—but often only after significant turbulence and at considerable extra cost. **There is clearly an onus on government not to outsource undue risk to third sector providers, or any other providers, without fair recompense—but the fair sharing of risk is in everybody's interest, if services are not to be allowed to fail.**

The role of the Compact

140. The reason why it is possible for too much risk to be outsourced is because there is an imbalance of power in the commissioning process—possibly particularly likely to manifest itself in relation to third sector organisations. Commissioners have, in general terms, much more experience of the tendering and contracting process than most bidder organisations, particularly when the Government looks to involve the smaller, more niche organisations. A common complaint from smaller organisations was that contracts are long, technical, difficult to understand, and vary greatly from one area to the next. This was a complaint we heard particularly forcibly from Alex Whinnom.¹⁶⁴ It would be all too easy for unscrupulous commissioners to insist on contractual stipulations which transferred unreasonable levels of risk to small providers. This is the logic behind the commitments to the sector embodied in the Compact.

141. The Compact is the agreement between government and the voluntary and community sector to improve their relationship for mutual advantage and community gain. As we have seen, it was established in 1998 as a result of a recommendation from the Commission on the Future of the Voluntary Sector in England.¹⁶⁵ Campbell Robb explained that the Compact was designed to address specifically the imbalance of power between government and the sector:

I think as regards the imbalance of power ... part of the reason for having a Compact in the first place is to say that we recognise that and the public sector recognises that and here are some of the ways that you can try to redress that balance of power by

163 Ev 290

164 Q 379

165 NCVO, *Meeting the Challenge of Change: voluntary action into the 21st century*, July 1996

thinking about how you commission, by thinking about how you consult, how you really work with organisations.¹⁶⁶

142. The terms of the Compact go beyond the commissioning relationship to look at all aspects of the relationship between the public and third sectors. We consider some of its principles in chapter 8. However, the interaction between the Compact and the pursuit of a level playing field in commissioning is particularly important to this inquiry. After all, other sectors do not have a Compact, so it could be interpreted as un-levelling a playing field by giving preferential treatment to the third sector. John Stoker, the former Commissioner for the Compact, conceded as much:

If the Compact was delivered, they [third sector organisations] would be treated in some ways differently. That is partly because there are commitments to consultation which are in there: commitments to a voice at the table when needs are being defined and programmes are being put together to meet them; special consideration for black and minority ethnic groups and community groups. These are all there. They do not exist in the same way for other sectors.¹⁶⁷

143. The difficulty with this special consideration is that it is not easy to reconcile with rules guaranteeing fair treatment for all potential providers—as set out in the EU Procurement Directives, and implemented in England, Wales and Northern Ireland by the Public Contracts Regulations 2006. In their submission to us, the Office of Government Commerce explained how limited commissioners' capacity was to discriminate in favour of third sector providers. Only issuing tender documents to third sector organisations would be discriminatory and lack transparency. Direct awards of a contract without an advert or competition would only be permitted in specific, highly exceptional circumstances. Even advertising predominantly in the third sector press could be discriminatory in European law.¹⁶⁸

144. These restrictions exist, as the OGC reminded us, to guarantee the principles underlying the EU Treaty: non-discrimination, equal treatment, transparency, mutual recognition and proportionality.¹⁶⁹ It is for these reasons that commissioners have little choice but to opt for the best provider without any ideological predisposition. The larger third sector organisations we heard from were also strongly supportive of this sector-blind approach as practical as well as principled, encapsulated by Lord Adebawale's observation that Turning Point had no right to exist or to be given work, but should be judged in each bid on its merits.¹⁷⁰ Competitive neutrality is also totemic to the CBI.¹⁷¹ The gist of all this evidence was that the market in public services is a place where the organisations have a choice if they want to get involved, and do so at their own risk—an idea that might be summarised as “seller beware”.

166 Q 177

167 Q 124

168 Ev 263

169 As above

170 Q 30

171 Q 58

145. How, then, can commissioners reconcile the EU principles and “seller beware” with the power imbalance leading to the commitments in the Compact? John Stoker told us that the Compact Code on funding and procurement explicitly states that they are consistent with the requirements of Government Accounting and EU procurement law, and that they apply in contract relationships as well as grants.¹⁷² He did concede, though, that this posed difficulties for commissioners:

On a ‘level playing field’, it may not be straightforward for commissioners to deliver consistently and fully the Compact financial undertakings to third sector partners unless these have been built into the terms of the programme concerned at the outset, and thus apply to bidders from other sectors as well.¹⁷³

146. **There are limits to the differential treatment which commissioners can give to third sector organisations in a procurement process. If Compact financial undertakings are to be built in to tender exercises, they must apply to all sectors equally. Therefore, while the Compact may have value in a contracting environment in redressing imbalances between buyer and seller, it does not level the playing field between bidders from different sectors.**

Conclusions—careful contours

147. **With less access to capital and less capacity to take risks, there will always be practical limits to the third sector’s ability to compete for certain contracts, especially the largest ones. The Government accepted this when Campbell Robb assented to our proposition of a “carefully contoured playing field” as the realistic goal.¹⁷⁴ It is legitimate for the Government to pump-prime the sector and invest in building its capacity, both in general terms and specifically to aid public service provision, as long as it does not unfairly advantage third sector organisations over rivals for service delivery bids. At the moment this seems some way off happening, and so we see Futurebuilders and Capacitybuilders as laudable schemes.**

148. **There is a limit, though, to what can be done by attempts to eliminate inherent disadvantages of third sector organisations when those disadvantages can arise out of the same characteristics that might make them distinctive. If government wants more third sector organisations to deliver services, then the most effective way will be to ensure that commissioners set out requirements when they commission services that play to these organisations’ distinctive qualities. Where there are any barriers, these should be eliminated, and capacity building will play an important part; but the key to improving outcomes will be ensuring that there are the right people in the job, with the right skills and knowledge to use their legitimate client discretions more wisely. The key is intelligent commissioning. We explore this in more depth in the next chapter.**

172 Ev 132

173 As above

174 Q 182

7 Intelligent commissioning

149. We have seen that there are a number of improvements that could be made to procurement processes which would enable third sector organisations to take part more effectively in the delivery of public services. These range from longer time periods for submitting tenders, as requested by Cambridge House, to the elimination of difficult jargon, which Sylvia Sham told us could have a particularly off-putting effect on BME organisations.¹⁷⁵ These are practical problems which could be and ought to be ironed out. The major complaints we heard, however—including those we have just discussed around the length and scale of contracts—speak of a more fundamental problem before the procurement exercises begin, in the earlier processes of commissioning. Whether contract specifications are too big to draw in desired providers, too short-term to get the best out of those providers or otherwise too prescriptive to provide necessary flexibility of action, there is a general failing behind all of these complaints—a failure in designing the service specification.

Commissioning for distinctiveness

150. We have seen that the Government acknowledges there are competing pressures on commissioners, to utilise third sector strengths and at the same time to achieve efficiencies. Although one of the problems this can cause is a drive towards contracts on too large a scale for third sector organisations to get involved, this is not the only danger caused by the pressures of efficiency. Even if the scale of a contract is judged sensibly, there is a danger in competitive processes that a decision will be based too simply on price. Martin Narey told us that the scope for commissioners to choose anything but the cheapest provider was very limited:

When on one occasion I did not give a contract for a private prison to the lowest bidder I had quite a hard time in front of the Public Accounts Committee because that had to be disclosed, so there is relatively limited scope to give contracts from the public sector to other than the bidder who is meeting all the requirements of the tender and at the lowest possible price.¹⁷⁶

151. Dave Prentis of Unison told us that competition militates against consideration of service quality, noting his experience that “the whole emphasis on markets and competition is it is a bidding process, and usually under that process the lowest tender wins.”¹⁷⁷ He told us that the experience of compulsory competitive tendering (CCT) was a warning from history that cost trumped all.¹⁷⁸ Perhaps surprisingly, Neil Bentley of the CBI agreed, telling us that “we may have said at the time that that was the right thing to do but

175 Q 374

176 Q 219

177 Q 66

178 Q 73

we have learned and we are no longer saying that CCT was good”.¹⁷⁹ The CBI’s new emphasis was on quality of services, with a particular stress that quality needs to be funded:

[In CCT] there was a huge drive from public authorities and local authorities to drive down costs, and that affected quality of services and the quality of services that alternative private sector providers were able to deliver. That is what we do not want to see happening in the voluntary sector or for other providers, which is why we keep talking about quality of public service provision, and that needs to be properly funded by the public sector.¹⁸⁰

152. If in practice commissioners are likely to remain under considerable pressure to select the bidder meeting the tender requirements at the lowest price, and yet quality of services is to be a factor, this must be guaranteed in the tender requirements. This makes the key to successful commissioning ensuring that the service specification itself is right. Fairbridge explained in their submission to us that services can go wrong at this very early stage of the process:

Too often programmes targeting our client group fail because providers are chasing formal qualifications inappropriate to the real needs of young people. This means that those commissioning services need an informed understanding of user needs in order to set appropriate outcomes.

The Third Sector has an extremely good grasp of the needs of its clients and should therefore be consulted in the design of the prospectus for services to be tendered, particularly regarding the setting of appropriate outcomes.¹⁸¹

153. Rainer refer to this process as “intelligent commissioning”.¹⁸² It might equally be referred to as service design. The Wales Council for Voluntary Action told us that the Office of Government Commerce (OGC) had issued guidance which highlights the need for engagement with third sector organisations when policy is first being formulated, when outcomes and outputs are being shaped, and to ensure appropriate procurement strategies.¹⁸³ The Local Government Association also endorse this approach stating ‘the best local authorities involve the third sector in identifying service need and service specification.’¹⁸⁴

154. The extent to which this is translating into practice remains unclear, however. Martin Narey from Barnardo’s told us:

There is some evidence of commissioners coming out to talk to us and say what sort of things work and what sort of things should we include in the tender documents but I have to say that that is very patchy. For very many occasions tenders arrive in

179 Q 92

180 As above

181 Ev 225–226

182 Q 31

183 Ev 287

184 Ev 249

our offices with two weeks to fill them in, with a huge amount of work to do and with little or no scope to say we think it can be done in a different way.¹⁸⁵

Lord Adebawale suggested that there was still some confusion among commissioners over what they were and were not allowed to do under EU procurement rules:

I could give examples of commissioners who have refused to talk to us because they consider it to be commercially sensitive and you think, “well, actually we are the very people you should be talking to”.¹⁸⁶

155. Joyce Moseley, though, felt there was nothing in EU rules which precluded this kind of intelligent commissioning, referring to complaints of such problems as a ‘smokescreen’.¹⁸⁷ Fairbridge also believed it was possible to involve third sector organisations in the design of service outcomes without conflict of interest.¹⁸⁸ The OGC backed this up when they told us that “while this must not give any provider a competitive advantage, third sector organisations may have specialist knowledge and links to the community that are useful in helping to understand how best to meet the needs of certain user groups”.¹⁸⁹ **Commissioners need external input when designing service specifications, and this is recognised in EU procurement rules. If some commissioners still believe that the rules prevent them engaging with organisations who are potential bidders, the onus is on the Government to disseminate the real position.**

156. The New Economics Foundation believed that commissioners’ behaviours often ran in contradiction to the Government’s intention for public service reform:

Whilst the Government’s model of public service reform emphasises the role of users shaping services ‘from below’, the commissioner/provider segregation required by the contestability model can run counter to this co-production approach by excluding the vital input of users’ voice, skills and experience from the equation.¹⁹⁰

Philip Cullum of the NCC agreed that this was a lost opportunity:

I suppose the thing we would most point out is rather than being about the third sector, it is more about consumers’ involvement in shaping policy ... lots of organisations who commission do not involve consumers either in assessing or in the shaping stage at the beginning.¹⁹¹

157. Mindful of the potential of third sector-designed services to deliver better outcomes to users, we asked Martin Narey whether Barnardo’s would consider being involved in service design even if it did preclude them from delivering the resulting service. He told us that though they would probably instinctively prefer delivery because they wanted to work with

185 Q 285

186 Q 32

187 Q 32

188 Ev 225

189 Ev 264

190 Ev 258

191 Q 216

children directly, he would consider working with commissioners in designing service specifications even if it subsequently meant that Barnardo's could not bid for that work:

I would not be averse to an approachable local authority which said, "You could not bid for this work, it would have to go to another organisation but we will pay you to help us design contracts and commissioning arrangements, which would provide good public services".¹⁹²

158. If contracts are almost always going to go to the bidder meeting the tender requirements at the lowest price, it becomes absolutely essential that the service specification is designed to the highest possible standard. If commissioners want services to be provided in a distinctive way, they will need to specify that in their tender requirements, because otherwise there will be little scope for bidding organisations to emphasise their distinctiveness during the procurement process.

159. It follows from this that commissioning bodies will need an extensive knowledge of the services they are looking to buy before they advertise for bidders. If they are to require bidders to provide a service in a particular way, the commissioners need to find out what distinctive ways of providing services are out there. The onus is on commissioners to look at the different potential providers and not be shy to talk to them in designing service specifications.

160. Third sector organisations can play a particularly valuable role in service design, because they can often act as a conduit to service users, and particularly the hardest to reach. Commissioners should talk to potential providers, but their interaction with the third sector should not be limited there. Above all, commissioners need to understand what service users value in a particular service.

Commissioning for added value

161. We established in Chapter 5 that the "added value" often associated with third sector delivery was actually a term covering a range of different outcomes which might be generated by service delivery but which were external to the "core" outcomes of the contract. We noted there that such outcomes are not achieved automatically by employing third sector organisations to deliver services, and that there was no theoretical reason why these outcomes could not be generated by organisations from other sectors. Our tentative suggestion was that achievement of these outcomes might be more a function of the commissioning process than of the identity of the provider.

162. The New Economics Foundation argue strongly and persuasively that "added value" is in fact not only central to the third sector offer, but more importantly central to what government should be looking to achieve in society:

There is evidence to suggest that third sector organisations deliver multiple services and multiple outcomes in excess of those 'contracted' for in their agreements with the public sector ... Any consideration of cost should therefore be a benefit-cost assessment across all outcomes achieved rather than restricting it to the outputs

described in the contract. If this is taken into consideration then there are greater grounds to argue that their unit cost across the full outcome framework is ‘cheaper’.

The commissioning process itself should be revised to enable providers to describe, and then capture the economic, social and environmental outcomes that their delivery approach brings to the sector. That is, to express the full value their organisation can bring to a service and to the wider community.

163. The critique made by the New Economics Foundation raises broader issues than just good commissioning practice. It calls into question the entire direction of public service reform, with an emphasis on easily measurable financial efficiency over harder-to-measure indicators of effectiveness—particularly those of wider social and environmental benefits. Their suggestion of a new model for measuring the effectiveness of services goes well beyond the scope of this inquiry, but certainly warrants consideration at the centre of government and beyond. We may return to it in future inquiries.

164. In the context of third sector delivery, the important issue is that commissioners need to weigh up the relative importance of core contractual outcomes and wider social benefits, and they need to do it at the design stage of commissioning. It is a value judgement whether the benefits offered by pursuing wider social goals will outweigh financial efficiency or service quality in any given situation. There is also a particular difficulty here in that commissioners who are not democratically accountable—for example, commissioners in the National Health Service—may be held responsible for the core contractual outcomes without having any clear organisational incentive to generate wider social benefits. **Government’s task, at a central and local level, is to specify what it wants to gain from the delivery of a particular service. It should certainly take into account wider benefits; but it may need to do more than that, and actually ask for those benefits to be delivered when commissioning services.**

165. The principal mechanism for achieving this is the use of what is known as social clauses. These clauses can be used to ask potential service providers to supply outcomes which might previously have been considered added extras rather than core elements of the contract. Ed Miliband explained the thinking behind the Government’s belief in social clauses:

Social clauses are about saying, “We make the value for money and efficiency tests but we can also look at wider benefits that there might be to the community.”

To take an example, if you are an organisation engaged in furniture recycling but you are also employing local people, or employing people with learning disabilities, a narrow contract would not take that into account, but a contract (and this is allowed under EU procurement rules) that took into account the wider social benefits would take that into account.¹⁹³

166. This approach appears to contribute to third sector involvement in public service delivery in two key ways. Firstly, it is likely to strengthen the competitive advantage of third sector organisations which are experienced in providing “added value” in this way.

Secondly, the move from externality to core contractual requirement also means that these outcomes would have to be paid for. Private and public sector organisations might still be able to out-perform third sector bidders on price, but they would have to factor into their price things which might not come naturally to them, like involving volunteers or aiding access to other providers' services. In some circumstances, insisting on particular types of added value could be a legitimate way of making it likelier in practice that services are run by third sector organisations. Nobody, though, is excluded in principle by social clauses; as Campbell Robb reminded us, there are hundreds of thousands of volunteers in the public sector too.¹⁹⁴

167. Richard Gutch told us that clever approaches to specification ought to be able at least on some occasions to resolve tensions between the size of contracts and the types of organisation the Government would like to see involved in delivery:

I think the trick lies in the commissioner specifying the service appropriately. If they specify about needing to involve local people to work with local organisations that is going to point in the direction of organisations that are not multinational charities but have found ways of retaining that local route which I think is often so important.¹⁹⁵

The Office of the Third Sector's action plan in 2006 included a commitment that it would tackle barriers to the use of social clauses, in part by creating template social clauses for use in appropriate contracts.¹⁹⁶ One year on, several local authorities, including Medway, Braintree, Leeds and Bury, were preparing to use social clauses in live procurement exercises for waste and recycling services. The Government's intention is to learn from these experiments and think about producing guidance on best practice.¹⁹⁷

168. We see merit in the targeted development of template social clauses. But this will not be enough. Commissioners should be expected to think about possible added value at the design stage of commissioning, and then to ensure it is taken into account in the procurement stage. For many commissioners, this will be a significant cultural change. A commissioning authority like the National Offender Management Service is not judged on the generation of social capital or of a spirit of voluntarism—it is judged on core outcomes like providing the right standards of prison accommodation, or prevention of re-offending. It is also judged on how much it spends. The challenge for government is to foster a culture where added value is routinely taken into account in addition to costs and core outcomes, and find the right incentives for commissioners to think about specifying wider benefits where these are appropriate.

194 Q 155

195 Q 132

196 Cabinet Office, *Partnership in Public Services: an action plan for third sector involvement*, December 2006, p 4

197 Cabinet Office, *Partnership in Public Services: the public services action plan—one year on*, December 2007, p 3

Commissioning for independence and innovation

169. Social clauses and user-focused design of service specifications have their merits; but they also have their limits. One final frustration we heard from third sector organisations actually pulls in an opposite direction—the extent to which rigid service specifications left little room for innovation and experiment in methods of service delivery. Innovation is of course one of the supposed distinctive characteristics of third sector organisations which the Government wants to harness to service delivery; but we have also seen that it is hard to provide for it through contractual stipulations. Leonard Cheshire typified the thoughts of third sector organisations who commented to us on this subject:

The third sector has always been known and valued for innovation; to some extent this is constrained in public service contracting by the rigid approach of commissioners, including a predominance of input rather than outcome measurement in contract performance assessment, a more flexible and open approach by commissioners would therefore be needed to take advantage of the real scope for innovation that the third sector can clearly bring.¹⁹⁸

170. The homelessness charity federation Emmaus UK provided us with an example of how such lack of flexibility in reality can discourage some third sector organisations from becoming involved in delivering services on behalf of the public sector at all. Selwyn Image, Vice President of Emmaus UK, explained how some of their member organisations had had to refuse Supporting People money because commissioners put stipulations on their funding that nobody should stay in an Emmaus community for more than a given amount of time, even though this was sometimes wholly inappropriate to the individual concerned.¹⁹⁹

171. Clearly, if it is independence and innovation you want from an organisation, you do not tell them how to go about running their business. Debra Allcock Tyler told us that social clauses primarily benefited the private sector, “because we [the third sector] don’t need social clauses, we are social clauses”.²⁰⁰ Her view on how the Government’s position is seen on the ground suggested a fierce cynicism about the sincerity of government’s desire to get the best out of the sector:

This transformation is “Wouldn’t it be fab if these wonderful, gorgeous, voluntary-sector organisations, full of really terribly nice people, came round delivering public services, because that would be great for us, but only if they do it in this way and to this timescale, for this money, under these conditions and with these terms”.²⁰¹

Alex Whinnom gave evidence in a similar vein on attempting to contract for innovation:

Voluntary action is not about organisations, in the end, or systems or models at all; it is about passionate people getting up and doing something about something, and it is often very dependent on individuals having the skills and the connections and the

198 Ev 243

199 Q 369

200 Q 451

201 Q 451

relationships to do that. As soon as you start to try to bottle it and package it, you have a risk of losing it.²⁰²

172. Campbell Robb seemed to acknowledge the force of these points when he talked about the importance of innovation and flexibility, and the “big trick” being to ensure that government “does not squeeze it out in the big bear hug that you have with the State”.²⁰³ In fact, though, the Office of the Third Sector’s Action Plan is extremely slight on how government can encourage or enable innovation, with much of its two pages on the subject instead concerned with spreading knowledge of existing innovative practice. Campbell Robb explained why this was important:

I recently visited a great project in Coventry. You say, "This is fantastic. Where else are they doing that?" and they say, "In Cornwall". You say, "How is it in Coventry and Cornwall?" and they say, "Because the person who set the project up here moved to Cornwall". That is how good practice is shared, by people changing jobs. It is obviously not a good way to do it.²⁰⁴

173. We did hear, though, from some witnesses who felt there was a way of allowing innovation in a contractual relationship. The means of achieving this can be characterised most simply as outcome-based commissioning. A distinction is drawn here between outputs, which are measurements of end products, and outcomes, which are measurements of end states. If outputs are less defined, providers have more freedom to find new ways of achieving desired outcomes. The Audit Commission struck a positive note when they told us they had found that “contractual arrangements do not necessarily stifle flexibility and innovative practice”.²⁰⁵ Yet the Baring Foundation told us they knew of only one notable example of innovative practice in a contractual arrangement,²⁰⁶ and it is notable that none of the examples of innovation we have cited in this report were borne of contracted services. Far more typical is the story we heard from the Children’s Trust, who told us that they “find that it is possible for us to use charitable funds to ‘pump prime’ new services that can then be commissioned once they have proved that they work”.²⁰⁷

174. Age Concern England noted that outcome-based commissioning was ‘the intention, if not yet the reality of government policy’.²⁰⁸ Martin Narey, though, having experienced both sides of the commissioning relationship, agreed there was room for improvement, but also sounded a note of caution. He noted, in the context of children’s services, that commissioners who had a contract that was “very light in terms of child protection” were “likely to face severe criticism when something went wrong”.²⁰⁹ This is a salutary example that there can be valid reasons for making contracts prescriptive on processes to be used.

202 Q 411

203 Q 132

204 Q 125

205 Ev 169

206 Ev 177

207 Ev 202

208 Ev 166

209 Q 268

175. **Contracts and innovation are uneasy bedfellows. Although it is not impossible to innovate within the parameters of a contract if it is designed to allow it, it requires something of a leap of faith for commissioners to give the necessary levels of freedom to providers. To do so requires a willingness to fall short of desired outcomes in a certain proportion of cases. It seems inevitable that most innovation will continue to take place outside of contracted services.**

176. **The challenge is to create enough flexibility of process within contracts to allow providers to pick up on proven innovative practice elsewhere. As the Government has identified, the spreading of innovative practice is the key to improvement on a national scale. The Government should support outcome-based commissioning where possible, in the interests of flexibility and responsiveness; but where providers have truly innovative ideas for public service delivery, these need to be tested on commissioners at the design stage. It is largely unrealistic to expect commissioners to specify outcomes in a contract without an understanding as to how they will be reached.**

Intelligent commissioners

177. Ultimately, the way to guarantee intelligent commissioning will be to ensure that commissioners themselves understand their roles fully. Embedding practices such as multi-year contracting, user involvement in service design and consideration of wider benefits requires a class of people who instinctively understand the advantages of such ways of working. The Government has acknowledged this as an area needing work, and the 2006 Action Plan announced plans to establish a two-year National Programme for Third Sector Commissioning that would invest in the skills of the 2,000 commissioners from across the public sector who they considered would have the biggest impact on the third sector. This would include staff in Jobcentre Plus, Primary Care Trusts, the National Offender Management Service and in local councils. The programme was designed to work in conjunction with existing training and support for commissioners.²¹⁰

178. Phil Hope told us that training went hand in hand with guidance. He cited the Department for Communities and Local Government's guidance to local authorities on Local Strategic Partnerships and Local Area Agreements, both of which include specific references to the third sector and the importance of factors such as stability of funding and proper consultation in service design.²¹¹ He also told us that he saw himself as a "champion" for the third sector within government, talking to ministerial colleagues on a case by case basis about ways that they could improve their practice.²¹² Beyond these positive incentives, too, there would be assessment of whether local authorities had maintained a "thriving third sector" in their areas, as part of the Audit Commission's new Comprehensive Area Agreements.²¹³

179. None of our witnesses disagreed with the analysis that commissioners on the ground were not yet putting into practice the ideals espoused by the Government. Joyce Moseley

210 Cabinet Office, *Partnership in Public Services: an action plan for third sector involvement*, December 2006, pp 18–19

211 Q 338

212 Q 322

213 Q 338

spoke of the gap between central government's discussions about opening up social markets and local government's actions on the ground.²¹⁴ Particular support for the training programme came from acevo's Peter Kyle, who saw it as the major "blockage" preventing the potential of the third sector from having a transformative effect:

At the moment, the full potential of the third sector is not recognised in the commissioning process. Not all commissioners understand the third sector ... Once the commissioning process recognises there are social outcomes as well as economic ones which the Government want to achieve, then I think there will be much greater potential to have a real step-change in the way that the third sector engages in delivering public services of all sizes.²¹⁵

180. Training 2000 people, however, only goes so far. Martin Narey told us that a more fundamental problem was the calibre of people who were recruited into commissioning roles:

The commissioning talent pool is spread very thinly. Commissioning has taken off so much in health service and local authorities, and indeed where I was, and my regional and national managers would say that they sometimes meet commissioners who are not terribly good customers, they are not very expert in what they are buying.

They are very good about the contractual terms of a contract but they may not know very much about what quality outcomes for children are and they do very cautious things like prescribe the inputs, prescribe how many staff will be on duty rather than prescribing the outcomes for children.

If I was giving advice to any public body on improving public services I would say put your most talented people into commissioning because if they are good commissioners who will talk to potential providers and know the good in creative contracts you could really improve public services. That would really help us.²¹⁶

Asked why this was not happening now, Mr Narey told us that his experience was that it was difficult to tempt the best public servants to work as commissioners, for reasons he did not know:

I know that when I was recruiting commissioners it was very hard to get very good people to move from the delivery side of an operation to wanting to commission work; I find that difficult to explain.

Eventually, in running private prisons, I did manage to persuade arguably one of the single most talented people working in prisons to come and do that job and he had a transformational impact in a few years on remoulding private sector contracts and

214 Q 42

215 Q 459

216 Q 235

improving private sector prisons without putting an additional penny into the contracts.²¹⁷

181. Intelligent commissioning depends on able, knowledgeable commissioners. Training is an essential part of developing skills, and the Government's steps to train key commissioners are positive and will benefit more than just third sector providers. Guidance, championing of the sector and external assessment will all play their part in changing organisational behaviour too; but there are no processes which adequately substitute for skills and ability. If commissioning is one of the keys to transforming public services, government needs to work at every level to attract its most talented people into working as commissioners, because commissioners are the people who will shape the services the public receives. At the very least, this will involve key posts being properly advertised and properly rewarded.

8 The risks of third sector provision

182. So far in this report we have looked at the means by which the Government can get the best out of third sector organisations as potential deliverers of public services. However, any discussion of the extent to which the sector should be involved in service delivery must also consider the risks inherent in delivering through third sector organisations. There are a significant number of risks, to the extent that some people continue to argue that there should be no place for the third sector in public service delivery at all.

183. There is a trap we need to avoid in this discussion, which is to be too focused on the effects of government policy on the sector as an end in itself. Much of the discussion of the risks of the commissioning agenda centres on what it does to the sector, whether in terms of over-regulation, squeezing grant funding or distorting independence. It is taken as axiomatic that such things are bad; it should not be. In practice many of these things may indeed be harmful, but the job of government is to balance different public policy objectives in the interests not of itself or of service providers but of the service user and of the citizen.

184. Research carried out by the Local Government Association made the salutary point that ‘many people often do not know who provides their services and do not care as long as it is of a high quality, meets their needs and is value for money’.²¹⁸ The public has an interest in a healthy and thriving third sector, not as an end in itself, but for what it can offer citizens—whether that is improved public services, advocacy of important causes or stronger communities. We will therefore not be asking directly about the risks of the commissioning agenda to the sector or to government. Instead we will look first at the risks to service users, and then at the wider risks to civil society of perceived threats to the third sector.

Risks to the service user

Standards of service

185. The first obvious risk to service users is that standards of service will slip. In particular, we have discussed in earlier chapters the risk that use of competition can inexorably lead to a situation where contracts are allocated on price rather than quality. This worry is not merely hypothetical; for example, our predecessor Committee found in 2005 that competitive tendering for hospital cleaning seemed to have resulted in a significant deterioration in standards, with disturbing personal consequences for some patients and considerable diversion of NHS resources to care for them.²¹⁹ As that example shows, this is not a worry that is specific to commissioning from the third sector, but if the sector is to have a “transformative” effect on public services then that means a particular emphasis is needed on thinking about factors other than price alone. We considered in the last two chapters some steps that government might take to get the best out of the sector.

218 Ev 250

219 Fourth Report of Session 2004–05, *Choice, Voice and Public Services*, HC 49, March 2005, para 156

186. A particular risk in any contracting relationship is that the State loses the capacity to be an intelligent customer, and is unable to effectively monitor standards of service. By losing its direct contact with service users, the commissioner loses sight of what is happening on the ground, and is in a significantly weakened position when it comes to renegotiating contracts. Will Werry told us that this was exercising him:

One of the things that has slightly bothered me recently is that you get a lot of difficulties with long-term contracts because they have to be re-negotiated, and everybody says how good they are at re-negotiating contracts, never do they say they made a mess of it, but it is very hard to see how well the parties do; it is a very hazardous business.²²⁰

187. The converse of this risk is the possibility that the State will respond with increasingly burdensome monitoring systems. John Stoker told us his impression that loss of state control was less of an issue than damage done by over-tight specifications which proscribe innovation.²²¹ The Audit Commission told us that their studies into competition and contestability had indicated that both of these risks were being realised in different places, although there was good practice evident as well.²²² Community Links noted a problem with identifying baselines against which service providers should be measured.²²³ These are again essentially not sector-specific issues, and lead us into areas we have considered previously in inquiries into choice in public services and government's use of targets.²²⁴ We do not want to go over this ground again, except to note that we have previously warned that crude targets can encourage perverse practices, such as "cream-skimming", where providers concentrate on improving their statistical performance by helping only those users who can be helped relatively easily.²²⁵ This is a potential effect of targets in any sector, but we did hear at our seminar that it could be a particular problem when providers are not committed to equity of service provision.

188. One sector-specific concern we did have to grapple with was the possibility that third sector service providers might be somehow less professional, perhaps because they made use of volunteers (although as we have mentioned the public sector makes use of volunteers too). However, we did not hear this concern from any of our witnesses. Instead, it was emphasised that service delivery was usually provided by paid staff and rarely by volunteers; Rainer and the British Red Cross told us they were unusual among service delivery organisations in making extensive use of volunteers. Peter Kyle told us that people "should not be ashamed of the professionalisation of the sector":

People who have incredibly entrenched, difficult, multiple challenges and problems and difficulties to overcome deserve to be cared for and given support from people who are well trained. In order to have the best people doing that, they have to have

220 Q 107

221 Ev 135

222 Ev 170–171

223 Ev 218

224 Fourth Report of Session 2004–05, *Choice, Voice and Public Services*, HC 49, March 2005

225 As above, para 155

good training, good management, good systems and good pensions, everything that everyone else in every other sector deserves.²²⁶

189. We did not find any evidence that standards of service were intrinsically lower (or higher) in third sector organisations. However, this must be at least in part down to the difficulty of assessing performance levels in public services. If the State moves further along the road of commissioning, it needs to manage the competing risks that it may either lose the ability to assess performance or instead be too onerous in its monitoring requirements. This is not a sector-specific concern, but it will always be one of the central challenges of a commissioning relationship.

Accountability

190. Another set of risks surround the concept of public accountability. There is a basic principle in British democracy that everyone who carries out an executive function must be in some way ultimately accountable, whether to the electorate, to elected representatives, or to some external arbiter of standards. In practice, accountability of the executive is a complex concept and involves a number of different mechanisms, including not just electoral accountability through the ballot box, but regulation, duties to publish information (both proactively and reactively), service user feedback (through mechanisms ranging from consultations to complaints systems), scrutiny and audit.

191. In a contractual relationship, although responsibilities can be determined in a contract, accountability remains within the public sector, usually with the commissioning body. The service provider is accountable to the commissioner through the mechanism of the contract, while the commissioner is then held accountable for getting the contract right or wrong in the first place. Joyce Moseley reflected that when she had worked as a Director of Social Services she had been held to account by her local population and this had made her feel the responsibility to get the best outcome for that population—by outsourcing services.²²⁷ Ed Miliband told us it was very important that accountability remained with the commissioner:

You need the internal procedures in third sector organisations, but ultimate accountability for services lies with the commissioning public authority.²²⁸

192. The risk, though, is that lines of accountability are not clear and not understood by the public. Electoral accountability is not the only facet of accountability, and indeed not all commissioning authorities are electorally accountable—National Health Service commissioners are one obvious example. The issue for this inquiry to consider was not just the impact of contracting out service delivery on accountability for provision, but whether there were specific accountability issues around delivery through the third sector. We heard three particular concerns—around the regulation of service standards, the protection of users' rights, and the provision of complaints mechanisms for service users.

226 Q 437

227 Q 39

228 Q 323

Regulation

193. One facet of accountability is ensuring that services performed by non-governmental organisations, whatever sector they may be in, are effectively regulated. This is an area that exercises the sector a great deal, with the general contention being that the sector is not just adequately regulated, but often over-regulated. Typical was Lord Adebawale's substantiation of his suggestion that Turning Point were "regulated to within an inch of our lives":²²⁹

We are regulated by the Healthcare Commission, the Commission for Social Care Inspection, the Housing Corporation, the Audit Commission and the Charity Commission, which I think is enough to be going along with, but we also have the scrutiny of our contract commissioners in several hundred different locations to contend with ...²³⁰

194. It is clear that charities in particular face a mixture of functional regulation from bodies like CSCI and sectoral regulation from the Charity Commission. There have also been individual instances where public regulators have had overlapping responsibilities, and third sector providers can often prove difficult for functional regulators to deal with as they may provide a range of related services. However, it is difficult to identify too much scope for rationalisation. To take Lord Adebawale's example, one of the bodies he mentioned is an auditor rather than a regulator, while the Charity Commission has a role of looking at all activities carried out by charities and not just service delivery—where, in practice, they will presumably defer to functional regulators for that service. Doubtless, this frustrates a lot of third sector providers, as do the monitoring requirements of commissioners which we have already discussed. Yet short of a general desire to reduce regulatory burdens, we heard no workable proposals for reform. **The levels of regulation required in public services are high. We understand that third sector providers feel over-regulated, but they are hardly unique in this: no-one has ever complained to us that they are under-regulated. Government should always look for ways to remove unnecessary regulatory burdens, and information should wherever possible be shared between commissioners, regulators and auditors; but it may be that high levels of regulation may be something third sector providers have to live with. The cost of complying with necessary regulation ought to be factored in to any bid to provide a service delivery contract.**

Users' rights

195. Another risk that we recognised during our inquiry was that there appear to be some questions about the human rights of users of services which are contracted out of government. Again, this is not third sector specific, although third sector organisations have mentioned this as part of an overall complaint about regulatory burdens. The issue is in some ways clear-cut; nobody's human rights should be reduced by the outsourcing of a service. There is a question, though, of how those rights are safeguarded, and a risk that users do not know where they can turn. In particular, there has been a debate over whether

229 Q 47

230 Q 20

all organisations delivering public services should be considered to be public authorities for the purposes of the Human Rights Act 1998. The judgement in the landmark Leonard Cheshire case in 2002 found that human rights law in care services brought about the deeply unsatisfactory state of affairs that third sector care homes are not considered public authorities and therefore do not have human rights obligations to users of public services. We note that the Joint Committee on Human Rights found this “problematic” as long ago as 2004. Subsequently, what was understood to be the scope of the Human Rights Act has been further narrowed by a series of court cases, culminating in the judgment by the House of Lords in the *YL v. Birmingham City Council and others* case in June 2007. **The human rights of public service users should not be affected by the identity of the service provider. As the Joint Committee on Human Rights has consistently argued, the original scope of the Human Rights Act needs to be restored so that non-public sector organisations can be considered public authorities for the purposes of the Human Rights Act when they are discharging functions on behalf of the State. We acknowledge that this is complex, but it is essential to achieve.**

196. A similar issue needs to be addressed with regard to information rights. Again, bodies outside the public sector have never been considered to be public authorities under the Freedom of Information Act 2000. The test for coverage under the two Acts is different—the Freedom of Information Act lists public authorities, while the Human Rights Act has a generic definition of public authority. **We were pleased to see the recent consultation by the Ministry of Justice on extending the Freedom of Information Act to bodies outside the public sector, including to contractors who provide services that are a function of a public authority. In fact, the Act contained provision that it could be extended to achieve this by Order. We hope that the outcome of the consultation is that all contractors are covered by the regime, in respect of those functions they are carrying out on behalf of the State. Given that there are exemptions around commercial confidentiality, we cannot see any legitimate argument why they should not be. Regulatory burdens on providers should be as light as they can be without reducing the rights of service users and citizens—but no lighter.**

Complaints procedures

197. One final, perhaps more prosaic element of accountability is the direct accountability to service users encapsulated in a complaints procedure. The availability of redress where things go wrong is one of service users’ basic rights. Yet here there appears at least superficially to be not just a risk but a real gap in service provision: a 2006 Charity Commission survey found that 69% of charities reported a lack of complaints procedures, including 40% of those who were delivering public services.²³¹ Campbell Robb acknowledged that this was an area which needed work:

The figure we will be most interested in is the 40 % of organisations that they say are delivering public services that do not have complaints mechanisms. We would want to work with commissioners, the sector and others, through support for the sector, to

²³¹ Charity Commission, *Stand and Deliver; The future for charities providing public services*, February 2007

make sure that the service users feel they have adequate redress through the normal mechanisms that you would have in other sectors.²³²

198. However, he also told us that the need for complaints procedures was and had to be decided by the commissioning authority on a case by case basis, as “you would not want the same redress mechanisms for a small £10,000 contract as you would for a £2 million contract to do something else”.²³³ The Charity Commission’s Independent Complaints Reviewer told us that this was a serious gap that needed filling:

In the delivery of social care, if a user is dissatisfied with a service provided by the Local Authority, ultimately they can refer that matter to the Local Government Ombudsman. If problems occur in the interface with the Health service, the Parliamentary and Health Service Ombudsman can step in to help the citizen. There is no similar arrangement for charities.

She called for the establishment of a Charities Ombudsman.²³⁴

199. Joyce Moseley told us that any commissioner worth their salt would make it part of the contractual terms that provider organisations would provide complaints systems that included provision for redress.²³⁵ Richard Gutch agreed.²³⁶ Phil Hope and Ed Miliband emphasised that they thought it should be possible to complain at source to service providers. But their priority, constitutionally speaking, was ensuring that it was possible for service users who were unhappy about a service to complain to the commissioning authority—whether that was a local authority or part of central government. Ultimately, the Government believed that all service users, whoever provided the service, should and did have the right of recourse to either the Parliamentary and Health Service Ombudsman or a Local Government Ombudsman. We note also that the Local Government Ombudsmen reported in 2007 that they believed they retained responsibility for all services that were for which local authorities had a statutory requirement, regardless of who provided them,²³⁷ and the Parliamentary Ombudsman confirmed with us that she agreed:

My view would be very simply that it is state activity, albeit contracted out, the state cannot contract out the responsibility, even if it contracts out the operation of it.²³⁸

200. We are concerned by the suggestion that 40% of charities providing public services do not have a complaints mechanism, and wonder if a template clause could be devised for service delivery contracts. But we accept the point that it is ultimately the commissioner’s responsibility to make sure that there is an appropriate complaints mechanism, subject to any legal requirements in their area.

232 Q 137

233 Q 138

234 Ev 241

235 Q 48

236 Q 140

237 Local Government Ombudsmen, *Local partnerships and citizen redress*, July 2007

238 Oral evidence taken before the Public Administration Select Committee on 18 October 2007, HC (2006-07) 1086-I, Q 62

201. In terms of the right to complain, however, the most important principle is that the users of services delivered under contract should not lose their ultimate right to complain to an Ombudsman if they do not get satisfaction elsewhere. It appears that this principle is accepted by the Government and applied in practice. With this in mind, we see no need arising from our inquiry for a dedicated Charities Ombudsman. There may, though, be an need to ensure that the users of outsourced public services understand their right to complain to an Ombudsman.

Risks to civil society

202. We have seen that there are some grounds to be optimistic that improved commissioning and procurement processes could see third sector organisations making a more effective contribution to public service improvement. However, we also heard fundamental concerns that procurement—and the competitive approach it requires—damages the ethos and distinctiveness the policy is intended to promote. The primary risk to the citizen is that overemphasis on the commissioning relationship could be to the detriment of the third sector’s other relationships with the State—as innovator, as advocate or as conduit of the views of groups perhaps otherwise unrepresented.

203. John Stoker told us that this was a real concern for him as Commissioner for the Compact:

I have a bit of a concern, as well, about a side effect of the trend in financing relationships away from grant and towards procurement, in so far as it risks inculcating in public-sector people the idea that the commissioning relationship is all they have to concentrate on to the exclusion of the wider relationship between the sectors, which is part of the Compact arrangement and which is not disconnected simply because you go into this new relationship.²³⁹

204. To its credit, there is no doubt that the Government acknowledges that the sector plays a number of other important roles beyond service delivery, and that these must be balanced.²⁴⁰ The question we have had to address is whether that balance is the correct one, and, if so, whether it appears likely to remain so. We heard three main risks asserted:

- A risk that an organisation’s nature and mission can be distorted by the pursuit and delivery of contracts;
- A risk that the nature of the sector more widely was being significantly changed for the worse, particularly through a disappearance of grant funding; and
- A risk that the independence of third sector organisations was being eroded.

These are all related concerns, but we will attempt to take them separately.

239 Q 111

240 Q 110

Distortion of mission

205. We heard from more than one of our witnesses a concern that contracting relationships were effectively incompatible with the nature of third sector organisations. According to this theory, a third sector organisation's distinctive characteristics, including crucially a focus on the needs of users, are threatened by the possibility that focus has to shift to the needs of a contract. Debra Allcock Tyler put this case forcibly:

The nature of contracting changes the nature of your relationship as an organisation with your client. It distorts who the client is and who it is you are existing to serve. There is a lot of evidence that says that organisations which start to engage in contracting relationships begin to satisfy the terms of the contract rather than satisfy the needs of the user.²⁴¹

206. There is also a particular issue for charities, who have to act within their own charitable objectives, and yet may find commissioners have slightly different (or changing) objectives. Tom Levitt, the Member for High Peak, gave an example illustrating this difficulty well:

Picture the scene: a volunteer gets out of a van and takes a piping hot meal to a waiting elderly housebound person. They chat for a few moments and the volunteer, who is perhaps the old person's only visitor of the day, moves on.

The social services department then decrees 'We want you to spend less time delivering meals and more time chatting, helping identify the needs of the most needy clients and identifying what more we can do for them.' If they can cope, the clients are to be given a stack of meals at the start of the week, a freezer to keep them in and a microwave to heat them up, plus training on how to use it.

'No', say the volunteers, 'We volunteered to deliver meals, not chat, we're not social workers!' and off they walk. This is exactly what happened in my county a few years ago. In different circumstances a 'yes' might have brought about a fundamental change in the objects of the charity, mission creep, caused by the influence of the outside body. Neither response is intrinsically right or wrong, but this sort of choice has to be made by voluntary organisation service providers every day.²⁴²

207. The fear of "mission creep" which Tom Levitt identifies was also mentioned to us in the United States, where they have travelled further down the road of commissioning services to the third sector than this country has so far. We heard it too from Selwyn Image of Emmaus, who argued that third sector organisations could lose sight of their missions and become dedicated to keeping themselves going. He gave us an example from his own experience of church-based children's charities:

Children's charities in this country, or church-based ones, were particularly set up to provide a better standard of workhouse or care and adoption and the state took both of those functions and the charities kept on functioning. Essentially, they are now

241 Q 428

242 Ev 284

lobby groups, with huge funds in huge areas and, yes, I think there are some very large questions that should be asked about the function of charity and the efficiency of charity.²⁴³

208. Yet what is not clear is whether this risk of mission distortion or mission creep is peculiar to, or even heightened by, a contracting relationship. The risk is clearly there, and there is something about the nature of the contracting relationship that appears to allow commissioners more ability to direct, or at least negotiate over, the way a third sector organisation goes about its business. Yet such a discussion seems almost to assume that third sector organisations have no choice but to take government contracts, even if they are unhappy with the terms. This is absolutely not the case—as Richard Gutch made clear:

One of the things that voluntary organisations have to be very clear about and their trustees have to be very clear about is "Would getting involved in this particular bit of public service delivery be consistent with our mission, consistent with what this organisation is there to do and the values it brings to it?" That is an assessment every single organisation needs to make for itself.²⁴⁴

209. A contract can, in theory, distort the goals of a third sector organisation. However, the onus is surely on third sector organisations themselves to police their own behaviour. As we have noted already, there is no compulsion for organisations to bid for public service contracts, or to accept them if some of the terms will distort their mission. There may also be a role for the Charity Commission in ensuring that the work of charities in particular goes towards meeting their charitable objectives.

210. Dave Prentis believed that the danger went beyond the distortion of individual organisations' goals, to a distortion of the mission of the entire third sector. He cautioned that there was a danger that the sector would become a mirror image of the private sector as they competed with each other for contracts, and that this in turn would be damaging to the promotion of voluntarism:

I think the whole system of voluntarism in this country which is really based on the community and voluntary sector is under threat by the direction of travel that we could be going down if commissioning in the markets is brought in to that particular sector. Why would volunteers work for multinational companies? Why would volunteers work for organisations making profits? It does not work that way.²⁴⁵

211. The vision of a third sector developing in the image of the private sector is a haunting one. Such a change would indeed be damaging to society, not least in the effect it could have on the spirit of voluntarism which is one of the great values of a healthy third sector to every citizen. However, we are some way off that situation. A small number of third sector organisations may look increasingly similar to private sector counterparts, but there are a huge number who could never be mistaken in method or objective for a profit-making organisation. The Government should bear in

243 Q 397

244 Q 130

245 Q 60

mind the risk of fundamentally changing the sector, but this risk is only really likely to become problematic if contractual funding should come to dominate the sector.

The role of grant funding

212. In our view, an encouragement of third sector organisations to provide more contracted services is unlikely in itself to have a damaging effect on the sector, as long as it is balanced against other ways of involving the sector. We have already cited John Stoker's fear that the government will lose sight of the other elements of the relationship between the two sectors. In particular, his fear was that, as more money poured into service delivery contracts, that would leave less money for grant funding. This posed some special issues for some smaller local bodies that traditionally have been grant financed.²⁴⁶ Alex Whinnom had similar concerns:

If they take all these local contracts and we are then left with very little money on the table either for grants or contracts for locally-rooted organisations, that is something that worries me.²⁴⁷

213. Grant funding is important for a number of reasons. Without it, for one, many organisations would never reach the size where they could begin to bid for contracts. However, the core strength of grant funding is that, as it is less prescriptive than contracted funding, it allows more flexibility to third sector organisations, and more scope to innovate and to campaign independently. The New Economics Foundation told us that it was grants which had given the sector all the characteristics that the Government now prized and wanted to harness in a commissioning relationship:

The reason small to medium third sector organisations are currently able to respond to local need, fill gaps that that the public sector is not geared up for, innovate and take risks is because their funding arrangements allow them greater flexibility.²⁴⁸

214. We entirely accept that grants are a vital part of the funding balance. There does, however, seem to be an element of myth in discussions around this area, based on an assumption that an increase in use of contracts must necessarily lead to a squeeze in grant funding. No such thing has happened. In Table 1 on page 12 we saw that grant funding had not decreased in real terms between 2001 and 2006, even as contractual funding soared. It is clear that Government funding of the third sector has increased hugely over the last decade, and that grant funding, even if slightly tailing off, has been a very significant part of that. The Government does understand that protecting distinctiveness sometimes means different forms of funding, and the commitment to Compact principles—including the welcome step of creating a Commissioner for the Compact—is an example of the Government voluntarily committing itself to ensuring a healthy mix of funding.

215. The other myth in this area is the idea that the pursuit of grants was not also a form of competition. In fact, competition was fierce, as Stuart Etherington recalled:

246 Q 111

247 Q 399

248 Ev 261

People competed for grants as they compete for contracts. Grants were not given by some sort of magical wave of the wand: everybody can have a grant. Voluntary organisations competed for grants—as a different sort of competition, I will grant people that, and it was probably less specific. That is the key point.²⁴⁹

216. The final myth is that all third sector organisations necessarily prefer grants. Our evidence suggests a range of reasons why third sector organisations may prefer contracts to grants. Through its research the Audit Commission identified how ‘many voluntary organisations saw improved stability of funding streams as an advantage of delivering under contract’.²⁵⁰ This was echoed by Doncaster Supporting People Provider Forum, which reported recent experience with local public bodies that organisations receiving grants were seen as easy targets for the withdrawal of funding, whereas organisations with contracts were in a more secure position.²⁵¹ Frontline mental health group Together reported similar concerns.²⁵² Peter Kyle told us about Thames Reach, whose staff had been energised by the validation of winning a contract to deliver a service which they had previously provided through income from grants.

217. Many of the arguments about the risks of distorting missions by pursuing contracts could also be applied to grants. Third sector organisations always acquired grants by satisfying funders that they would provide outcomes which the funder believed were desirable. That is no different in principle from a contracting relationship, and could also distort an organisation’s purposes or discourage an organisation from speaking out—although contracts do allow commissioners the ability to shape processes as well as outcomes.

218. The real risk if grant funding were to disappear or be significantly squeezed would be that some of the most distinctive and innovative organisations would probably lose out. If the Government is looking for these characteristics in a commissioning environment, then it will want to preserve them. In other words, there is logic to the proposition that getting the best out of commissioning means ensuring more grant funding, not less. This appears from the statistical evidence to be what has happened in the last decade. Nonetheless, most witnesses agreed that over that time there has been an increasing bifurcation between the very large and the very small in the third sector.²⁵³ This is a development which the Government needs to monitor and to understand, if it is to ensure the sector continues to receive the right mix of contractual and grant-based funding.

219. Community Links reminded us that grant giving could be seen as a form of commissioning.²⁵⁴ It is certainly one of the levers at the disposal of commissioning authorities. We have already cited at paragraph 77 Stuart Etherington’s call for “horses for courses”. **Horses for courses is right. Where service outcomes are clearly defined and their achievement is paramount, then it is unrealistic to expect government to avoid**

249 Q 428

250 Ev 170

251 Ev 221

252 Ev 282

253 Q 457

254 Ev 213

forming contractual relationships with providers who can guarantee that the outcomes will be delivered. If outcomes are less well defined, though, commissioners may place a higher premium on innovation and flexibility. In those circumstances they retain the option of funding those outcomes through a grant, either for a specific project or more broadly in support of an organisation's overall objectives. The current funding mix does not appear to us to be unsustainable. Ultimately, though, it is up to Government to use the variety of funding mechanisms available to pursue its objectives (on behalf of service users and the public) in what it judges to be the most effective way.

Freedom to campaign

220. Another danger identified to us was that third sector organisations might be more reluctant to campaign against or criticise government on behalf of client groups if they were financially dependent on government funding through commissioning. The campaigning role of the sector is universally recognised to be of enormous importance to the health of civil society, as it achieves important functions like giving a voice to the seldom heard and ensuring a vibrant democracy. Again, the hypothetical risk is plain to see, and the question we sought to address was whether this risk was translating into a problem in practice.

221. Many of our witnesses were keen to downplay this risk. Turning Point and Rainer, for example, told us that they were both routinely involved in campaigning against the Government despite being highly dependent on public sources of funding.²⁵⁵ Lord Adebawale mentioned Turning Point's highly public campaign on the subject of blood-borne viruses in needle exchanges:

I have never in my career withdrawn a campaign that we thought was valid and valuable on the basis of a threat by a minister, MP, councillor or anyone else for that matter, and we would not.

Neither had any experience of their funding being threatened by a public authority. Nor had Barnardo's, who supplied us with a list of the campaigns they had been involved with recently.²⁵⁶

222. On the other hand, while confident of their own circumstances, these larger bodies did express concern for their smaller counterparts. Turning Point told us that some local commissioners had been at the least nervous about funding organisations who might campaign against them.²⁵⁷ The Compact Commission also feared self censorship by smaller organisations. Rotherham Metropolitan Council put it succinctly:

For large third sector organisations it will be possible to manage both service provision and campaigning. For smaller organisations it may require decisions as to the key aim of the organisation and how this may be funded.²⁵⁸

255 Qq 14–17

256 Ev 144

257 Q 17

258 Ev 274

223. Martin Narey told us that there was a particular danger to organisations whose core funding came from a single source; he told us that there was some evidence from the 1990s that Nacro did have core funding removed, partly because they had spoken out against the penal policies of the then government. The key strength here appeared to be in income diversity; Rainer and Turning Point told us they had great numbers of contracts, so were not too worried by the prospect of losing some, while the evidence from Barnardo's suggests that if anything a dependency on grant aid is potentially more risky.²⁵⁹ Commissioning may actually help stability in this regard.

224. The National Consumer Council told us that despite the oft expressed fears, they had encountered no evidence of problems here:

A lot of third sector organisations worry about the potential that there will be some negative knock-on effects, but we do not have any evidence that that is necessarily a problem.²⁶⁰

Meanwhile, the Local Government Association told us that “many local authorities directly fund the third sector precisely so they can lobby local government and give a voice to specific groups in the community”.²⁶¹

225. It is clear that pursuing and delivering public service contracts is not necessarily a barrier to independent campaigning and advocacy. In particular, there may be positive effects of entering into a contracting relationship, as it can deliver stability of income; organisations which rely on grants for core funding are arguably more at risk than large service delivery organisations.

226. Yet the risk is only there if government allows it to be. Perhaps the single most important message government can give to commissioners, and commissioners can give to the third sector, is that third sector organisations must continue to feel free to speak out. It is also important to have an apparatus to protect independence, and the Government deserves credit for establishing one in the form of the Compact—as well as an enforcer in the form of the Commissioner for the Compact. We will follow with interest the discussions between the sector and the Government on whether the Compact and the Commissioner ought to be put onto a statutory footing.

Public disengagement from government

227. One final risk that we identified is that out-sourcing services could mean that the funders of these services did not get the credit for providing them. The danger here for the citizen is that it will increase a public mood that the State does not provide citizens with what they need, and so enhance the already troubling public disengagement with government and politics. **We believe that where services are provided on behalf of the State, it should be made very clear to all service users—perhaps through partner-branding services. The exception to this would be where there is a risk that it might deter vulnerable users.**

259 Q 220 [Narey]

260 Q 220 [Hopkins]

261 Ev 252

9 Conclusions

228. A striking finding of our inquiry has been that, while some of the statements both supporting and opposing the expansion of third sector provision have verged on the hyperbolic, the evidence around the benefits and risks remains for the most part speculative or anecdotal. In part, this is simply because many services have only recently been contracted out to the sector. Nonetheless, there is a clear onus on the Government, as the proponent of greater involvement of the third sector in service delivery, to make the case on a more empirically demonstrable basis. We hope that an inquiry onto this subject a few years from now would be able to draw on a solid base of evidence which might allow firmer conclusions on what works and in what circumstances.

229. **While the scale of third sector involvement in service delivery remains close to its current small-scale level, many of the risks to the sector which were identified in our inquiry appear to us to have been overplayed.** There clearly would be risks if the Government were to go significantly further down the road of procuring services from third sector organisations under contract, especially if that were at the direct expense of grant funding for the sector's other important functions. However, for now at least, grant funding continues to be a very significant element of the funding mix for third sector organisations, and their ability to campaign and speak out does not seem to be obviously affected. Indeed, most risks to the sector appear to have been equally applicable in a grant funding environment. Moreover, there is an apparatus in place to protect the distinctive characteristics of the sector and hence protect the citizen, in the form of the Compact and its enforcer.

230. **The risks to government and to the service user may be more significant. Most of these are also not sector-specific, and are better seen as general risks of contracting out public service delivery. There is a particular issue around accountability, where action needs to be taken regarding the application of users' rights under the Human Rights Act and the Freedom of Information Act; and clarity is also needed around who service users can complain to when they have concerns about the service they have received. Beyond this, all commissioners face a significant challenge in effectively monitoring service provision while preventing unnecessary costs and bureaucracy. It is by no means proven that the benefits of contracting out services to providers from any sector outweigh the costs of effectively monitoring performance. Only the last of these risks, however, is potentially a show-stopper. The risks around accountability, while significant, could be mitigated by changes to the law. If the Government commits to tackling those issues, therefore, we see no reason not to continue cautiously along the path of encouraging third sector provision of public services.**

231. Caution is needed because progress must be on the basis of trialling in certain areas, through better use of commissioners' legitimate discretions, towards the collection of an evidence base. We do not want to see a mass transfer of services without significantly stronger evidence that this would be beneficial, and we are heartened that the Government does not appear to support such a mass transfer. Ultimately, it must be right to judge all prospective service providers on their merits. To do that, we need a vigorous mixed economy of provision, capable of eliciting the various distinctive strengths of different organisations in different sectors.

232. However, the idea that there will ever be a level playing field where providers of every variety compete on an equal basis is unrealistic. There should certainly be no unnecessary barriers to particular providers competing for contracts, but there will always be significant disparities between third sector organisations and counterparts in other sectors, not least in financial terms. While intelligent commissioning might mean more decisions could be made on factors beyond cost of service provision, cost will rightly always remain a factor for commissioners.

233. With all those caveats, though, we believe that intelligent commissioning offers scope to involve the third sector more. The key to getting the best out of the sector will be fostering an understanding of the sector's strengths among commissioners, who are central to determining the shape of public services. A culture change is needed to encourage the best people to become commissioners, with the right training and experience in place to ensure that they get the right mix of skills and specialist knowledge. That culture change should lead to the decline of perverse practices like overly short-term contracting. It should lead to an understanding of the importance of designing service specifications appropriately, engaging with users and possible providers to consider the outcomes which might be delivered for service users. It is at this crucial design stage where commissioners can design the playing field to play to the distinctive strengths of certain organisations, by determining the nature of the outcomes being bought, the scale of the contracts through which they buy them, or any wider social benefits that ought also to be delivered. In short, intelligent commissioners have a great deal of scope to involve third sector organisations more by wise use of their legitimate client discretions. If that happens, and those organisations are given the freedom to be distinctive, we believe there may well be potential in some areas for genuinely improved outcomes for the public.

Appendix: Matching public service requirements with third sector organisations' strengths

Public service Requirement	Third sector Strength	Reason
The quality of service being provided is difficult to specify, measure and monitor	User focus	Private providers may have an incentive to reduce quality to increase profit. The third sector has no such incentive.
The demands of service users are high differentiated	Flexibility, innovation and 'joining up'	Public and private providers are geared to provide services for large numbers of people. The third sector has the flexibility to deal with individual needs.
When services have to be directed at localities or sections of the community that have been excluded from traditional service provision	Knowledge, expertise and experience	Third sector organisations are often established by members of the excluded community in response to a perceived gap or inadequacy in service provision.
Labour-intensive services where the flexibility and commitment of volunteers can be an asset	User focus	Volunteers tend to spend more time providing a higher quality service, especially for disadvantaged people.
Services directed at users that do not trust businesses or the government	Trust and accessibility	Third sector providers have no hidden agendas and higher credibility with disaffected users.
Service users are likely to require a co-ordinated portfolio of services	Flexibility and 'joining up'	Third sector providers spend more time on bringing services together for the user.
Users often have difficulty engaging with service providers (multiple disadvantages)	Flexibility and 'joining up'	Wider stakeholders allow the third sector to focus on overlapping disadvantage.

Source: HM Treasury, "Exploring the role of the third sector in public service delivery and reform", a discussion document accompanying the 2004 Spending Review.

Conclusions and recommendations

Government and the third sector

1. It is clear that the State is commissioning more services from the third sector than ever before, and is increasingly doing so through procurement-type relationships. These commissioning trends, and their impact on the third sector, are at the heart of this report. (Paragraph 24)

The Government vision

2. If there is no common understanding of what commissioning means, that can only be a barrier to effective relationships. Government and the private and third sectors need to come to a commonly accepted definition of commissioning if it is to continue to be the State's preferred method of interacting with the sector. In particular, Government needs to convince the third sector that commissioning is something distinct from procurement. (Paragraph 38)

The scale of third sector involvement

3. As our witnesses told us, third sector organisations are ill-equipped to provide universality and equity to service users. Whatever transformation of public services is about, it should not be about transferring responsibility for delivering large areas of public service out of the State and into the third sector. It appears that government accepts this. Despite the emphasis given in government publications to involving the third sector, only 2% of public service spending is on third sector delivery. The debate on the transformative capacity of the third sector is a rhetorical storm in a fiscal teacup. (Paragraph 48)
4. The Government's position has moved from actively pursuing the transfer of services to allowing a more ready transfer "where appropriate". We support that change of emphasis. However, it immediately prompts a further question: how to judge where it is indeed appropriate for services to be provided by the third sector. (Paragraph 51)

Third Sector distinctiveness

5. One of the most commonly cited characteristics of third sector distinctiveness—almost its unique selling point—is the sector's focus on service users. Yet user focus is not unique to the third sector, and indeed what little research there is suggests that this user focus can be lost when organisations provide services to a large, general population. (Paragraph 69)
6. If the test of distinctiveness is that the third sector offers more specialist knowledge and expertise than other sectors, then we have not been provided with sufficient evidence to prove that claim. (Paragraph 69)

7. There is some evidence that third sector providers in certain fields provide more flexible, joined-up services. However, flexibility of services seems very dependent on good commissioning practice. (Paragraph 70)
8. The many fine examples of innovative practice in the third sector do not add up to conclusive evidence that the sector is inherently more innovative. (Paragraph 71)
9. In certain areas, it appears that third sector organisations may indeed be more likely to secure users' trust than public sector counterparts. It is equally apparent, though, that this is not universal across all forms of public service provision. Nor is it clear that it is a third sector-specific strength. It may be more accurate to suggest simply that certain types of service users, or would-be service users, may be apprehensive of dealing with the State. (Paragraph 72)
10. Added value has many facets, from generating social capital and voluntarism to levering in additional income or providing other unexpected but tangible benefits. Third sector organisations are often likely to be best placed to provide some of these benefits; but this may say less about the capability of other sectors than it does about the weakness of commissioning processes. Unless commissioners ask for added value, we cannot really know if it is a distinctive third sector strength. (Paragraph 82)
11. The evidence is simply not there to judge conclusively whether there are shared characteristics across all third sector organisations, arising from their commonality of origins or ethos, which might make them particularly suited to the provision of public services. Indeed, there is widespread consensus that this evidence base does not yet exist. Will Werry of the Commissioning Joint Committee put it most succinctly when he told us that "it is surprising that a major national exercise is based on ... supposition". (Paragraph 86)
12. We have already noted that the Government is not looking to transfer any set proportion of services to the third sector. At most, it has identified certain services which it believes third sector organisations may be particularly well placed to provide. This is a more nuanced approach and more sensible than attempting to claim general merits across the whole third sector. Given the absence of useful evidence, too, it is entirely sensible that the Government should no longer set numerical targets for the sector's contribution to public service delivery. (Paragraph 87)
13. The real question in each service should be what characteristics are needed to get the best outcomes for users and for citizens. This might give commissioners an evidence base when they consider what characteristics they might look for when deciding how to commission a service. It is in this direction that research should focus if the policy of encouraging third sector provision is to be pursued. (Paragraph 88)

Levelling the playing field

14. Public bodies should not be attempting to claw back surpluses from third sector organisations in contractual arrangements. (Paragraph 99)

15. Too many service delivery contracts still appear to be unnecessarily short. Nobody seems to be claiming that one-year contracts are generally sensible. Although there are disadvantages of overlong contracts too, in that it is harder to secure accountability to commissioners, there are clear practical problems with the length of many contracts currently. Repeated changes of provider are bad for staff; more importantly, they are bad for service users, who often need to build up relationships with service providers. Nor is it to anyone's advantage if service delivery organisations are unattractive places to work. (Paragraph 105)
16. Government has talked for some time of a three-year norm for contracts, and longer where appropriate. It is time that this was translated into changed practice. However, we understand that this is not easy. The National Audit Office reported in 2005 that good intentions here were being lost as funding flowed through the delivery chain. The decisions on contract length are made by individual commissioners and not by central government. The priority for the Office of the Third Sector, therefore, must be getting the message through to commissioners on the ground. (Paragraph 106)
17. Commissioners need to lose the habits of grant funding when dealing with third sector organisations in competitive procurement processes. The onus should always be on the bidding organisation to decide how much they want to charge. The responsibility of the commissioner is to ensure that there are neither arbitrary barriers preventing them from doing this, nor discriminatory requirements to compel them to charge their full costs where they may not wish to do so. (Paragraph 111)
18. It is important to recognise that full cost recovery is not a right—it has to exist in a competitive context. While bidding organisations should not be prevented from pricing their full costs into a bid to provide a particular service, commissioners will always retain the right to reject that bid in favour of a cheaper competitor. Government's commitment to full cost recovery does not, and should not, immunise the third sector from the pressures of efficiency and competition. (Paragraph 112)
19. In a competitive contracting environment, commissioners retain a residual duty to consider and manage the risks that aggressively low bidding might pose to the quality or sustainability of a service or a market, and act accordingly when selecting a preferred provider. However, responsibilities towards organisational sustainability remain the prime responsibility of third sector organisations themselves. This reinforces the importance that bidding organisations understand their full costs before entering the procurement process. (Paragraph 113)
20. In designing each procurement exercise, the challenge of the commissioning body is to try and determine the trade-off between affordability and service quality to the best possible extent. (Paragraph 118)
21. The growth of consortia is encouraging. We do not believe, however, that it is yet at a scale that is going to affect significantly the overall shape of the public services market. It is also costly and time consuming for organisations to come together into consortia. (Paragraph 121)

22. It is evident to us that even where there is some evidence that distinctive potential to transform public services does exist, such as in employment services, it risks not being captured due to the nature and scale of the procurement processes in place. Sub-contracts, which third sector organisations are having more success at winning, carry their own risks, and may still be too large for some of the most distinctive organisations; consortia of a sufficient size are hard to establish and maintain. If government wants to involve the smallest organisations who sometimes offer the most distinctive services, it may have to look at doing a number of things:
- radically simplifying its tendering processes;
 - helping organisations to bid, and in particular helping them to form consortia and allowing sufficient time in the commissioning process to do so;
 - incentivising prime contractors to work with third sector sub-contractors and build their capacity to participate in the commissioning process; or
 - identifying opportunities to advertise contracts at a significantly smaller level. (Paragraph 122)
23. If a level playing field is taken to mean that third sector organisations are able to compete as financial equals with potential providers in other services, then it will never be achieved. Most third sector organisations, including many who have the characteristics government is looking for in service delivery, are too small to compete for most contracts. Capacity-building is important in itself for reasons beyond service delivery, and it has a role in pump-priming particular would-be service providers, but it will not in itself achieve a level playing field in service delivery. (Paragraph 133)
24. The suggestion that charities are “almost uniquely penalised” by the VAT regime appears to have some force (although of course charities have their own tax advantages as well). (Paragraph 134)
25. TUPE appears likely to cause practical difficulties when services are moved into the third sector. Many organisations will not have the capacity to take on staff at existing levels of salaries and benefits. If the Government is committed to pump-priming the third sector to improve service provision, it will need to invest in supporting third sector organisations who are effectively prevented from delivering services by the requirements of TUPE. (Paragraph 135)
26. There is clearly an onus on government not to outsource undue risk to third sector providers, or any other providers, without fair recompense—but the fair sharing of risk is in everybody’s interest, if services are not to be allowed to fail. (Paragraph 139)
27. There are limits to the differential treatment which commissioners can give to third sector organisations in a procurement process. If Compact financial undertakings are to be built in to tender exercises, they must apply to all sectors equally. Therefore, while the Compact may have value in a contracting environment in redressing imbalances between buyer and seller, it does not level the playing field between bidders from different sectors. (Paragraph 146)

28. With less access to capital and less capacity to take risks, there will always be practical limits to the third sector's ability to compete for certain contracts, especially the largest ones. The Government accepted this when Campbell Robb assented to our proposition of a "carefully contoured playing field" as the realistic goal. It is legitimate for the Government to pump-prime the sector and invest in building its capacity, both in general terms and specifically to aid public service provision, as long as it does not unfairly advantage third sector organisations over rivals for service delivery bids. At the moment this seems some way off happening, and so we see Futurebuilders and Capacitybuilders as laudable schemes. (Paragraph 147)
29. There is a limit, though, to what can be done by attempts to eliminate inherent disadvantages of third sector organisations when those disadvantages can arise out of the same characteristics that might make them distinctive. If government wants more third sector organisations to deliver services, then the most effective way will be to ensure that commissioners set out requirements when they commission services that play to these organisations' distinctive qualities. Where there are any barriers, these should be eliminated, and capacity building will play an important part; but the key to improving outcomes will be ensuring that there are the right people in the job, with the right skills and knowledge to use their legitimate client discretions more wisely. The key is intelligent commissioning. (Paragraph 148)

Intelligent commissioning

30. Commissioners need external input when designing service specifications, and this is recognised in EU procurement rules. If some commissioners still believe that the rules prevent them engaging with organisations who are potential bidders, the onus is on the Government to disseminate the real position. (Paragraph 155)
31. If contracts are almost always going to go to the bidder meeting the tender requirements at the lowest price, it becomes absolutely essential that the service specification is designed to the highest possible standard. If commissioners want services to be provided in a distinctive way, they will need to specify that in their tender requirements, because otherwise there will be little scope for bidding organisations to emphasise their distinctiveness during the procurement process. (Paragraph 158)
32. It follows from this that commissioning bodies will need an extensive knowledge of the services they are looking to buy before they advertise for bidders. If they are to require bidders to provide a service in a particular way, the commissioners need to find out what distinctive ways of providing services are out there. The onus is on commissioners to look at the different potential providers and not be shy to talk to them in designing service specifications. (Paragraph 159)
33. Third sector organisations can play a particularly valuable role in service design, because they can often act as a conduit to service users, and particularly the hardest to reach. Commissioners should talk to potential providers, but their interaction with the third sector should not be limited there. Above all, commissioners need to understand what service users value in a particular service. (Paragraph 160)

34. Government's task, at a central and local level, is to specify what it wants to gain from the delivery of a particular service. It should certainly take into account wider benefits; but it may need to do more than that, and actually ask for those benefits to be delivered when commissioning services. (Paragraph 164)
35. We see merit in the targeted development of template social clauses. But this will not be enough. Commissioners should be expected to think about possible added value at the design stage of commissioning, and then to ensure it is taken into account in the procurement stage. For many commissioners, this will be a significant cultural change. A commissioning authority like the National Offender Management Service is not judged on the generation of social capital or of a spirit of voluntarism—it is judged on core outcomes like providing the right standards of prison accommodation, or prevention of re-offending. It is also judged on how much it spends. The challenge for government is to foster a culture where added value is routinely taken into account in addition to costs and core outcomes, and find the right incentives for commissioners to think about specifying wider benefits where these are appropriate. (Paragraph 168)
36. Contracts and innovation are uneasy bedfellows. Although it is not impossible to innovate within the parameters of a contract if it is designed to allow it, it requires something of a leap of faith for commissioners to give the necessary levels of freedom to providers. To do so requires a willingness to fall short of desired outcomes in a certain proportion of cases. It seems inevitable that most innovation will continue to take place outside of contracted services. (Paragraph 175)
37. The challenge is to create enough flexibility of process within contracts to allow providers to pick up on proven innovative practice elsewhere. As the Government has identified, the spreading of innovative practice is the key to improvement on a national scale. The Government should support outcome-based commissioning where possible, in the interests of flexibility and responsiveness; but where providers have truly innovative ideas for public service delivery, these need to be tested on commissioners at the design stage. It is largely unrealistic to expect commissioners to specify outcomes in a contract without an understanding as to how they will be reached. (Paragraph 176)
38. Intelligent commissioning depends on able, knowledgeable commissioners. Training is an essential part of developing skills, and the Government's steps to train key commissioners are positive and will benefit more than just third sector providers. Guidance, championing of the sector and external assessment will all play their part in changing organisational behaviour too; but there are no processes which adequately substitute for skills and ability. If commissioning is one of the keys to transforming public services, government needs to work at every level to attract its most talented people into working as commissioners, because commissioners are the people who will shape the services the public receives. At the very least, this will involve key posts being properly advertised and properly rewarded. (Paragraph 181)

The risks of third sector provision

39. We did not find any evidence that standards of service were intrinsically lower (or higher) in third sector organisations. However, this must be at least in part down to the difficulty of assessing performance levels in public services. If the State moves further along the road of commissioning, it needs to manage the competing risks that it may either lose the ability to assess performance or instead be too onerous in its monitoring requirements. This is not a sector-specific concern, but it will always be one of the central challenges of a commissioning relationship. (Paragraph 189)
40. The levels of regulation required in public services are high. We understand that third sector providers feel over-regulated, but they are hardly unique in this: no-one has ever complained to us that they are under-regulated. Government should always look for ways to remove unnecessary regulatory burdens, and information should wherever possible be shared between commissioners, regulators and auditors; but it may be that high levels of regulation may be something third sector providers have to live with. The cost of complying with necessary regulation ought to be factored in to any bid to provide a service delivery contract. (Paragraph 194)
41. The human rights of public service users should not be affected by the identity of the service provider. As the Joint Committee on Human Rights has consistently argued, the original scope of the Human Rights Act needs to be restored so that non-public sector organisations can be considered public authorities for the purposes of the Human Rights Act when they are discharging functions on behalf of the State. We acknowledge that this is complex, but it is essential to achieve. (Paragraph 195)
42. We were pleased to see the recent consultation by the Ministry of Justice on extending the Freedom of Information Act to bodies outside the public sector, including to contractors who provide services that are a function of a public authority. In fact, the Act contained provision that it could be extended to achieve this by Order. We hope that the outcome of the consultation is that all contractors are covered by the regime, in respect of those functions they are carrying out on behalf of the State. Given that there are exemptions around commercial confidentiality, we cannot see any legitimate argument why they should not be. Regulatory burdens on providers should be as light as they can be without reducing the rights of service users and citizens—but no lighter. (Paragraph 196)
43. We are concerned by the suggestion that 40% of charities providing public services do not have a complaints mechanism, and wonder if a template clause could be devised for service delivery contracts. But we accept the point that it is ultimately the commissioner's responsibility to make sure that there is an appropriate complaints mechanism, subject to any legal requirements in their area. (Paragraph 200)
44. In terms of the right to complain, however, the most important principle is that the users of services delivered under contract should not lose their ultimate right to complain to an Ombudsman if they do not get satisfaction elsewhere. It appears that this principle is accepted by the Government and applied in practice. With this in mind, we see no need arising from our inquiry for a dedicated Charities Ombudsman. There may, though, be an need to ensure that the users of outsourced

public services understand their right to complain to an Ombudsman. (Paragraph 201)

45. A contract can, in theory, distort the goals of a third sector organisation. However, the onus is surely on third sector organisations themselves to police their own behaviour. As we have noted already, there is no compulsion for organisations to bid for public service contracts, or to accept them if some of the terms will distort their mission. There may also be a role for the Charity Commission in ensuring that the work of charities in particular goes towards meeting their charitable objectives. (Paragraph 209)
46. The vision of a third sector developing in the image of the private sector is a haunting one. Such a change would indeed be damaging to society, not least in the effect it could have on the spirit of voluntarism which is one of the great values of a healthy third sector to every citizen. However, we are some way off that situation. A small number of third sector organisations may look increasingly similar to private sector counterparts, but there are a huge number who could never be mistaken in method or objective for a profit-making organisation. The Government should bear in mind the risk of fundamentally changing the sector, but this risk is only really likely to become problematic if contractual funding should come to dominate the sector. (Paragraph 211)
47. Horses for courses is right. Where service outcomes are clearly defined and their achievement is paramount, then it is unrealistic to expect government to avoid forming contractual relationships with providers who can guarantee that the outcomes will be delivered. If outcomes are less well defined, though, commissioners may place a higher premium on innovation and flexibility. In those circumstances they retain the option of funding those outcomes through a grant, either for a specific project or more broadly in support of an organisation's overall objectives. The current funding mix does not appear to us to be unsustainable. Ultimately, though, it is up to government to use the variety of funding mechanisms available to pursue its objectives (on behalf of service users and the public) in what it judges to be the most effective way. (Paragraph 219)
48. It is clear that pursuing and delivering public service contracts is not necessarily a barrier to independent campaigning and advocacy. In particular, there may be positive effects of entering into a contracting relationship, as it can deliver stability of income; organisations which rely on grants for core funding are arguably more at risk than large service delivery organisations. (Paragraph 225)
49. Yet the risk is only there if government allows it to be. Perhaps the single most important message government can give to commissioners, and commissioners can give to the third sector, is that third sector organisations must continue to feel free to speak out. It is also important to have an apparatus to protect independence, and the Government deserves credit for establishing one in the form of the Compact—as well as an enforcer in the form of the Commissioner for the Compact. We will follow with interest the discussions between the sector and the Government on whether the Compact and the Commissioner ought to be put onto a statutory footing. (Paragraph 226)

50. We believe that where services are provided on behalf of the State, it should be made very clear to all service users—perhaps through partner-branding services. The exception to this would be where there is a risk that it might deter vulnerable users. (Paragraph 227)

Conclusions

51. While the scale of third sector involvement in service delivery remains close to its current small-scale level, many of the risks to the sector which were identified in our inquiry appear to us to have been overplayed. (Paragraph 229)
52. The risks to government and to the service user may be more significant. Most of these are also not sector-specific, and are better seen as general risks of contracting out public service delivery. There is a particular issue around accountability, where action needs to be taken regarding the application of users' rights under the Human Rights Act and the Freedom of Information Act; and clarity is also needed around who service users can complain to when they have concerns about the service they have received. Beyond this, all commissioners face a significant challenge in effectively monitoring service provision while preventing unnecessary costs and bureaucracy. It is by no means proven that the benefits of contracting out services to providers from any sector outweigh the costs of effectively monitoring performance. Only the last of these risks, however, is potentially a show-stopper. The risks around accountability, while significant, could be mitigated by changes to the law. If the Government commits to tackling those issues, therefore, we see no reason not to continue cautiously along the path of encouraging third sector provision of public services. (Paragraph 230)
53. Caution is needed because progress must be on the basis of trialling in certain areas, through better use of commissioners' legitimate discretions, towards the collection of an evidence base. We do not want to see a mass transfer of services without significantly stronger evidence that this would be beneficial, and we are heartened that the Government does not appear to support such a mass transfer. Ultimately, it must be right to judge all prospective service providers on their merits. To do that, we need a vigorous mixed economy of provision, capable of eliciting the various distinctive strengths of different organisations in different sectors. (Paragraph 231)
54. However, the idea that there will ever be a level playing field where providers of every variety compete on an equal basis is unrealistic. There should certainly be no unnecessary barriers to particular providers competing for contracts, but there will always be significant disparities between third sector organisations and counterparts in other sectors, not least in financial terms. While intelligent commissioning might mean more decisions could be made on factors beyond cost of service provision, cost will rightly always remain a factor for commissioners. (Paragraph 232)
55. With all those caveats, though, we believe that intelligent commissioning offers scope to involve the third sector more. The key to getting the best out of the sector will be fostering an understanding of the sector's strengths among commissioners, who are central to determining the shape of public services. A culture change is needed to encourage the best people to become commissioners, with the right training and

experience in place to ensure that they get the right mix of skills and specialist knowledge. That culture change should lead to the decline of perverse practices like overly short-term contracting. It should lead to an understanding of the importance of designing service specifications appropriately, engaging with users and possible providers to consider the outcomes which might be delivered for service users. It is at this crucial design stage where commissioners can design the playing field to play to the distinctive strengths of certain organisations, by determining the nature of the outcomes being bought, the scale of the contracts through which they buy them, or any wider social benefits that ought also to be delivered. In short, intelligent commissioners have a great deal of scope to involve third sector organisations more by wise use of their legitimate client discretions. If that happens, and those organisations are given the freedom to be distinctive, we believe there may well be potential in some areas for genuinely improved outcomes for the public. (Paragraph 233)

Formal Minutes

Thursday 26 June 2008

Members present:

Dr Tony Wright, in the Chair

Paul Flynn

Kelvin Hopkins

Mr Ian Liddell-Grainger

Julie Morgan

Mr Gordon Prentice

Mr Charles Walker

Draft Report (*Public Services and the Third Sector: Rhetoric and Reality*), proposed by the Chairman, brought up and read.

Ordered, That the Chairman's draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 233 read and agreed to.

Summary agreed to.

A Paper was appended to the Report .

Resolved, That the Report be the Eleventh Report of the Committee to the House.

Ordered, That the Chairman make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Wednesday 2 July at 3.15 pm

Witnesses

	<i>Page</i>
Thursday 7 June 2007	
Lord Adebowale , Chief Executive, Turning Point, and Joyce Moseley , Chief Executive, Rainer	Ev 1
Tuesday 12 June 2007	
Dr Neil Bentley , Director of Public Services Policy, Confederation of British Industry (CBI), Dave Prentis , General Secretary, UNISON, Rachael Maskell , National Officer, Amicus, and Will Werry , Chairman, Commissioning Joint Committee	Ev 17
Thursday 5 July 2007	
John Stoker , Commissioner for the Compact, Campbell Robb , Director-General, Office of the Third Sector, and Richard Gutch , Chief Executive, Futurebuilders England	Ev 32
Tuesday 10 July 2007	
Martin Narey , Chief Executive, Barnardo's, Philip Cullum , Deputy Chief Executive, and Alison Hopkins , Senior Policy Advocate, National Consumer Council (NCC)	Ev 50
Tuesday 20 November 2007	
Rt Hon Ed Miliband MP , Chancellor of the Duchy of Lancaster & Minister for the Cabinet Office, and Phil Hope MP , Minister for the Third Sector	Ev 66
Thursday 17 January 2008	
Selwyn Image CBE , Vice President, Emmaus UK Foundation, Alex Whinnom , Director, Greater Manchester Centre for Voluntary Organisations, and Dr Sylvia Sham , Director, Wai Yin Chinese Women Society	Ev 84
Stuart Etherington , Chief Executive, NCVO, Dr Peter Kyle , Director of Strategy and Enterprise, acevo, and Debra Allcock-Tyler , Chief Executive, Directory of Social Change	Ev 93

List of written evidence

	<i>Page</i>
1 Rainer	Ev 106
2 Turning Point	Ev 112
3 Amicus	Ev 118
4 Commissioning Joint Committee	Ev 124
5 UNISON	Ev 127
6 Commissioner for the Compact	Ev 132
7 Futurebuilders England Ltd	Ev 136
8 Barnardo's	Ev 142
9 Supplementary memorandum from Barnardo's	Ev 148
10 Further memorandum from Barnardo's	Ev 148
11 Rt Hon Ed Miliband MP, Minister for the Cabinet Office	Ev 149
12 Association of Chief Executives of Voluntary Organisations (acevo)	Ev 151
13 National Council for Voluntary Organisations (NCVO)	Ev 155
14 Accenture	Ev 161
15 Age Concern	Ev 165
16 Audit Commission	Ev 166
17 The Baring Foundation	Ev 172
18 Brian Paul Tovey	Ev 180
19 British Red Cross	Ev 183
20 Cambridge House	Ev 188
21 Charity Commission	Ev 190
22 Charity Finance Directors' Group	Ev 196
23 The Children's Trust	Ev 201
24 CIPFA	Ev 204
25 Commission for Rural Communities	Ev 207
26 Community Links	Ev 209
27 Crime Reduction Initiatives	Ev 219
28 Doncaster Supporting People Provider Forum	Ev 220
29 Fairbridge	Ev 224
30 fpa	Ev 226
31 Headway Dorset	Ev 229
32 Supplementary by a Headway client	Ev 229
33 Help the Hospices	Ev 230
34 The Hospital Management Trust	Ev 235
35 Independent Complaints Reviewer	Ev 240
36 In-volve	Ev 241
37 Katherine House Hospice	Ev 241
38 Leonard Cheshire	Ev 242
39 Local Compact Voice	Ev 247
40 Local Government Association	Ev 249
41 Mandy Lawrence	Ev 254

List of written evidence (cont'd)

42	Mental Health Providers Forum	Ev 255
43	New Economics Foundation (nef)	Ev 257
44	Office of Government Commerce	Ev 263
45	Partnership for Young London	Ev 264
46	Remploy	Ev 269
47	Richard Molineux	Ev 271
48	Rotherham Metropolitan Borough Council	Ev 273
49	Swift Health Promotions	Ev 275
50	Together	Ev 280
51	Tom Levitt MP	Ev 283
52	Wales Council for Voluntary Action (WCVA)	Ev 285
53	Women's Health in South Tyneside	Ev 288
54	Zurich	Ev 290

List of Reports from the Committee during the current Parliament

The reference number of the Government's response to each Report is in brackets after the HC printing number.

Session 2007–08

First Report	Machinery of Government Changes: A follow-up Report	HC 160 (<i>HC 514</i>)
Second Report	Propriety and Peerages	HC 153 (<i>Cm 7374</i>)
Third Report	Parliament and public appointments: Pre-appointment hearings by select committees	HC 152 (<i>HC 515</i>)
Fourth Report	Work of the Committee in 2007	HC 236 (<i>HC 458</i>)
Fifth Report	When Citizens Complain	HC 409
Sixth Report	User Involvement in Public Services	HC 410
Seventh Report	Investigating the Conduct of Ministers	HC 381
Eighth Report	Machinery of Government Changes: Further Report	HC 514
Ninth Report	Parliamentary Commissions of Inquiry	HC 473
Tenth Report	Constitutional Renewal: Draft Bill and White Paper	HC 499

Session 2006–07

First Report	The Work of the Committee in 2005–06	HC 258
Second Report	Governing the Future	HC 123 (<i>Cm 7154</i>)
Third Report	Politics and Administration: Ministers and Civil Servants	HC 122
Fourth Report	Ethics and Standards: The Regulation of Conduct in Public Life	HC 121 (<i>HC 88 Session 2007–08</i>)
Fifth Report	Pensions Bill: Government Undertakings relating to the Financial Assistance Scheme	HC 523 (<i>HC 922</i>)
Sixth Report	The Business Appointment Rules	HC 651 (<i>HC 1087</i>)
Seventh Report	Machinery of Government Changes	HC 672 (<i>HC 90 Session 2007–08</i>)
Eighth Report	The Pensions Bill and the FAS: An Update, Including the Government Response to the Fifth Report of Session 2006–07	HC 922 (<i>HC 1048</i>)
Ninth Report	Skills for Government	HC 93 (<i>HC 89</i>)
First Special Report	The Governance of Britain	HC 901

Session 2005–06

First Report	A Debt of Honour	HC 735 (<i>Cm 1020</i>)
Second Report	Tax Credits: putting things right	HC 577 (<i>HC 1076</i>)
Third Report	Legislative and Regulatory Reform Bill	HC 1033 (<i>HC 1205</i>)
Fourth Report	Propriety and Honours: Interim Findings	HC 1119 (<i>Cm 7374</i>)
Fifth Report	Whitehall Confidential? The Publication of Political Memoirs	HC 689 (<i>HC 91, Session 2007–08</i>)

Sixth Report	The Ombudsman in Question: the Ombudsman's report on pensions and its constitutional implications	HC 1081 (<i>Cm 1961</i>)
Seventh Report	The Ministerial Code: the case for Independent Investigation	HC 1457 (<i>HC 1088, Session 2006–07</i>)
First Special Report	The Attendance of the Prime Minister's Strategy Adviser before the Public Administration Select Committee	HC 690