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# Flexible New Deal: Making it work

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## Aims

The aim of the project is to develop solutions to the potential problems that arise from the new regime:

1. Create financial incentives for providers to **help all jobseekers**;
2. Provide **value-for-money** employment outcomes for the taxpayer through sustainable job placements;
3. Reduce the need for **regulation** and monitoring of providers; and
4. Involve the **third sector** in a way that
  - i. capitalises on and retains their innovative capacity;
  - ii. Does not allow prime providers to exploit their value added for profit; and
  - iii. does not heavily distort their mission





## Context

Flexible New Deal involves two key innovations on the existing system:

1. Shift from process to **outcome focus**
2. **Concentration** of the provider market

This creates two sets of delivery risks:

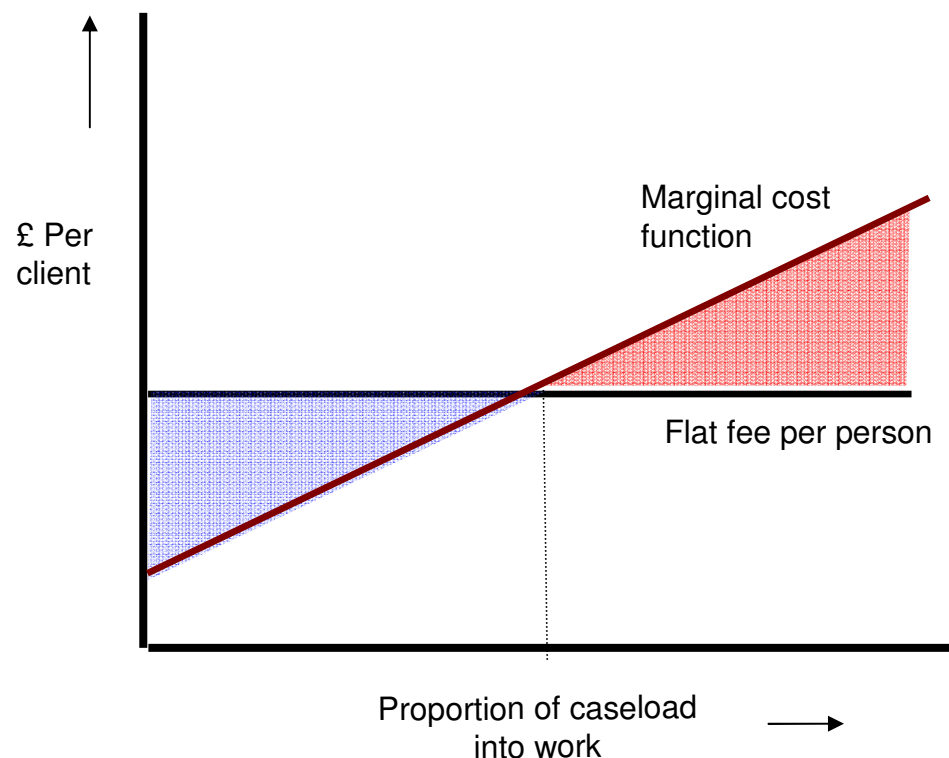
- a) Focus on outcomes can lead to the **parking** of 'harder-to-help' clients
- b) More concentrated market threatens health of the supply market because it:
  - i. Gives substantial market power to prime providers
  - ii. Gives an informational advantage to prime providers



# Outcome focus: parking

Non-aligned interests between the procurer and the service provider lead to:

- ▶ **Parking:** directing minimal resources at harder to help people
- ▶ **Creaming:** helping those closest to the labour market at the expense of others, because they carry the greatest profit
- ▶ There is **no incentive** to transfer the surplus obtained by helping the easiest clients (blue area) to subsidise those harder to help (red area).

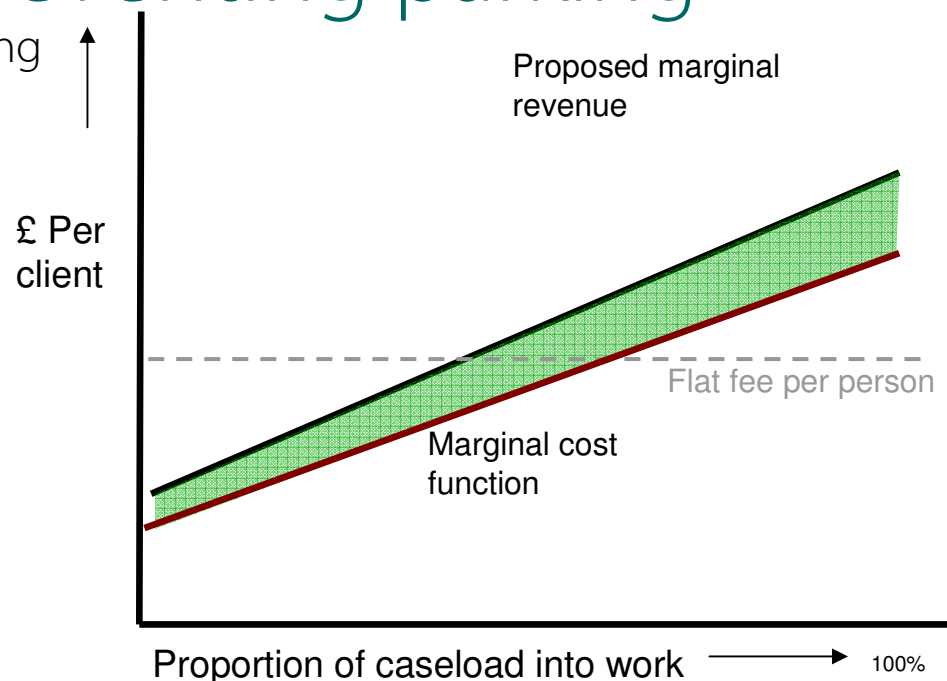


# Outcome focus: preventing parking

Action plans create only minimal parking disincentives

Alternative: to use graduated payment based on

- ▶ proportion of caseload put into employment
- ▶ length of time unemployed
- ▶ statistical profiling



## Solutions

Align the financial incentives of the state and the provider through payment based on *proportion* of clients found work. This avoids the need for complex and blunt regulation.

Penalty fees for providers where clients are jobless at 24 months

## Outcome focus: Success payments

- ▼ Hales et al. (2003) evaluation of employment zones suggested that among those found work through EZs, a higher proportion were
  - **dissatisfied** with their job (17% vs 7%)
  - **lower-paid** (49% vs 38% <£4.60/hr)
  - in **lowest occupational groups** (52% vs 39%)
- ▼ Both EZs and New Deal had little impact on the chances of clients **sustaining** work 7 to 10 months later
- ▼ “..neither of the programmes seemed to have had an appreciable longer-term impact in raising the chances of their participants experiencing sustained periods of paid work.”
- ▼ This means that taxpayer is not getting VFM on these programmes.

### **Solution**

Outcome payments should be weighted more heavily to longer-term success, particularly 12 month outcomes, with extra funding attached



## Maintaining a healthy supply market

- ▼ Small number of prime contractors carries a range of advantages.
  - ▼ Ease of management
  - ▼ Economies of scale
  - ▼ Incentives to invest
  - ▼ Market stability
- ▼ **Monopsonistic power** of primes disadvantages smaller sub-contractors
- ▼ **Informational advantage** of prime contractors. Primes know more about each client's likelihood of job success than do sub-contractors, and can exploit this



## Maintaining a healthy supply market

- ▼ These concerns cannot simply be left to the market to resolve
- ▼ Three kinds of problems result:
  - ▼ Primes expropriate the **surplus** of sub-contracting organisations away from their intended mission (See Grout & Yong (2003))
  - ▼ Imbalance reduces independence of sub-contractors to **innovate**
  - ▼ Threatens the **diversity and effectiveness** of the supply chain
- ▼ In short, this structure threatens the things about the third sector that make it attractive to involve in the first place.



# Market power: solutions?

Can the Code of Conduct prevent this behaviour?

- ▼ Hard to identify 'bad' behaviour
- ▼ Limited credibility for Department to censure or heavily fine those found to be exploiting that market power.
- ▼ Limited scope for sub-contractors to complain

## Solutions

- ▼ Sub-contractors actively encouraged to bid for work as a **consortium**.
- ▼ **Independent regulator** with the power to fine prime providers.
- ▼ FND contract specifications between prime contractors and DWP be **publicly available**.





# Market power: risk-sharing

*Example of a risk-sharing payment structure for sub-contracting*

Provider	Payment structure	Failure			Success		
		Revenue	Cost	Profit	Revenue	Cost	Profit
Prime Provider	£200 service £800 outcome	£200	£300	<b>-£100</b>	£1,000	£800	<b>£200</b>
Sub-contractor	£300 service £500 outcome	£300	£400	<b>-£100</b>	£800	£400	<b>£400</b>

Service payment to sub-contractor is higher than the service payment it receives from DWP.

Risk is shared: the prime has incentive only to send sub-contractors clients they think sub-contractors can help because the Prime retains a stake in job-placement success.

## Solution

Primes obliged to offer a higher service payment to sub-contractors than the one they receive from DWP (where sub-contractors assume job placement responsibility).



## Getting the most out of 3<sup>rd</sup> Sector

- ▼ Third sector organisations can contribute in two main ways
  - ▼ Closer connection to the local community enables effective job placement
  - ▼ Local knowledge and client-specific out-reach work means that some are better at helping people before they encounter the FND gateway
- ▼ FND design takes account of the former but not the latter.
- ▼ A rigid gateway approach will not work for some jobseekers.

### **Solution**

3<sup>rd</sup> sector providers engaged in out-reach work should be allowed to help those clients *directly* and receive outcome payments for doing so, rather than putting potentially vulnerable clients through the JC+ gateway first.

