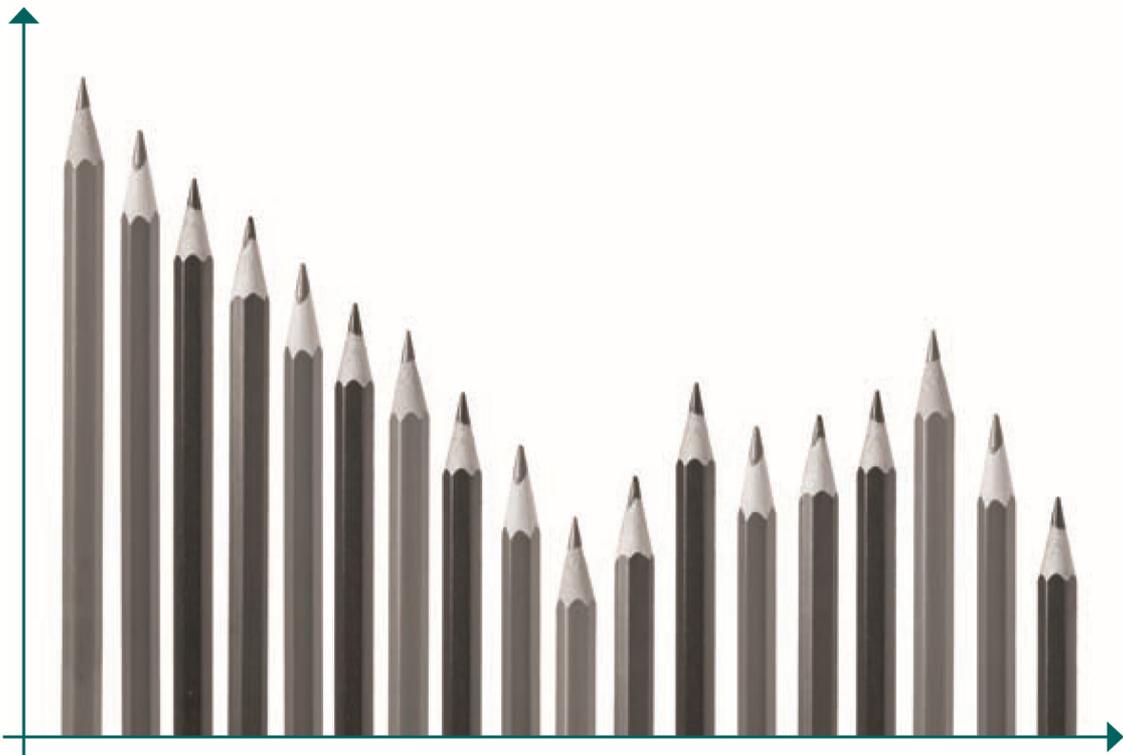


WILL THE WORK PROGRAMME WORK?

Examining the future viability of the Work Programme



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Ian Mulheirn was appointed Director of the Social Market Foundation in October 2008. He joined the Social Market Foundation as the Chief Economist in February 2008, after three years as an economic advisor at HM Treasury. He has worked in a variety of policy areas including child poverty, savings & investment, welfare to work and higher education funding. He has also undertaken research into the drivers of worklessness in London and evaluation of the Working Tax Credit and the National Minimum Wage. Ian led the SMF's influential work on welfare-to-work, and was recently a specialist advisor to the Work and Pensions Committee inquiry into the Work Programme.

SMF ANALYSIS

SMF Analysis papers are occasional papers which form part of SMF's analytical contribution to public debate. SMF has a long track record of work on unemployment and welfare policy. Recent publications in this area include *Vicious Cycles* (sponsored by Remploy), *The Jobs Crisis* (SMF Analysis) and *The Flexible New Deal: Making it work* (sponsored by Remploy).

EXECUTIVE SUMMARY

- The Government’s flagship back to work scheme, the Work Programme (WP), is the most ambitious payment-by-results scheme ever launched in the UK, aiming to help 2.4 million long-term unemployed people find work over the next seven years. In it, private and not-for-profit providers will be paid for each jobseeker they get back into work.
- The design of WP drew heavily on the welfare-to-work model proposed by SMF in its 2009 publication *Vicious Cycles*. Welfare Reform Minister Lord Freud, when in opposition, cited the SMF’s work as a key influence on the policy’s development. Consequently, the SMF feels strongly that this laudable policy should not be derailed by poor implementation.
- Funding for the new programme is tight and dependent upon achieving very demanding minimum performance expectations set by the Department for Work and Pensions (DWP). In addition, DWP has threatened to terminate the contracts of providers who do not meet these challenging benchmarks.
- In this paper, the SMF examines the viability of WP by forecasting the likely performance of the providers during the first three years, based on the actual performance achieved under the Flexible New Deal (FND), Labour’s welfare to work scheme and the forerunner to WP.
- The analysis suggests that WP providers will significantly undershoot the minimum performance expected of them by DWP. This implies widespread contract termination and threatens the viability of the entire scheme.
 - ◆ The performance of FND suggests that WP will get around one in four adult Jobseeker’s Allowance (JSA) clients into work. This implies that providers will fail to meet DWP’s expectations for minimum provider performance.
 - ◆ All providers look likely to underperform the minimum expectations in years one and two of WP. Even by year three, 22 out of 24 FND contractors would have failed to meet the minimum requirements of WP. All providers would therefore have been at risk of having their contracts terminated.
 - ◆ The implied level of WP performance suggests that funding per jobseeker will be significantly less than anticipated, threatening the financial viability of providers.
 - ◆ WP performance is vulnerable to the deteriorating economic outlook since bids were invited, compounding the above problems. Since December 2010, the claimant count has risen by almost 110,000 suggesting that many more jobseekers are likely to move onto the scheme over the coming year.

Table 1: Comparison of DWP’s minimum expectations of Work Programme providers with SMF’s predictions of provider performance

	Year 1	Year 2	Year 3
Minimum WP performance expected by DWP	5.5%	27.5%	33%
Predicted WP performance	4.1%	20.5%	27.8%
No. jobs short of minimum	4,300	17,300	11,600
Predicted WP if FND had a ‘slow start’	4.4%	21.9%	29.7%
No. jobs short of minimum	3,400	13,700	7,200

- These findings raise serious concerns about the viability of WP under current plans. Widespread provider failure or a late bailout would be bad for jobseekers, expensive for the taxpayer and fatal for many subcontractors, especially not-for-profit providers.
- The SMF, credited with writing the blueprint for WP, argues that a rethink is needed to ensure the stability and success of the scheme in getting people back to work. DWP should:
 - ◆ **revise its minimum performance expectations** in the light of the new data from FND, and introduce more credible incentives;
 - ◆ establish greater **transparency about how it derived its estimates of minimum performance**, and clarify how they would vary if economic conditions deteriorate, to create greater certainty and strengthen accountability;
 - ◆ Introduce a **comparative performance target** for providers to clarify the consequences of relative underperformance;
 - ◆ consider **raising outcome payments** for providers to avoid the extensive disruption to jobseekers and major costs to taxpayers that would flow from widespread provider failure;
 - ◆ advance the Government's aim to be the "most transparent government in the world" by **publishing monthly provider performance data, starting immediately**;
 - ◆ investigate and **monitor the distribution of outcome risk between primes and subcontractors** if it wants subcontractors to remain viable in this highly risky environment.

INTRODUCTION

The Government's flagship welfare to work scheme, the Work Programme (WP), was launched in June 2011 and has been described by the Department for Work and Pensions as a "revolution in back to work support" and "the centrepiece of the Government's plans to reform welfare-to-work provision in the UK".¹

WP is one of the principal Government interventions to support the country as the economy emerges from recession. It aims to prevent unemployed people from permanently disengaging from the world of work, which comes at huge on-going costs to taxpayers.²

Aiming to help 2.4 million people to find work over the next seven years, WP is designed to pay providers only when they succeed in getting unemployed people into jobs. Eighteen organisations from the private and not-for-profit sectors have won the DWP contracts to deliver the seven-year programme in England, Scotland and Wales. They will work with adults who have been unemployed for more than twelve months and young people who have been unemployed for more than nine months, as well as sickness benefit claimants capable of working. Providers will be paid for each person they help into a job lasting at least six months.

The SMF has long argued for the application of payment-by-results in welfare to work. The 2009 report *Vicious Cycles* was described by one publication as "the blueprint for the Work Programme",³ and Welfare Reform Minister Lord Freud, when in opposition, cited the SMF's work as a key influence on the policy's development. Consequently, the SMF feels strongly that this laudable policy should not be derailed by poor implementation.

¹ Department for Work and Pensions, 'Grayling launches a revolution in back to work support as the Work Programme rolls out nationwide', 10 June 2011, <http://www.dwp.gov.uk/newsroom/press-releases/2011/jun-2011/dwp062-11.shtml>.

² Department for Work and Pensions, "The Work Programme Prospectus" (London: HMSO, 2010).

³ Regeneration and Renewal *The think tanks that shape Tory policy*, 19 October 2009.

Using data and evidence from the Labour Government’s Flexible New Deal (FND) - the forerunner to WP, which ran between 2009 and 2011 - this research explores the viability of this crucial scheme. FND was in many respects similar to the new scheme in that it served one-year-plus JSA claimants (although not the other client groups in WP) and providers were paid, in the main, for the job outcomes they achieved for their clients rather than for simply providing a service. In the light of the performance of FND, this paper asks whether minimum requirements of providers under the new scheme have been set too high and whether the Work Programme is vulnerable to failure as a result.

The paper starts by discussing DWP’s minimum performance expectations of providers under WP and how these criteria were set. It goes on to use newly available evidence on FND to forecast the performance of providers under the new WP. Finally the paper explores the implications of this evidence for this important policy’s viability, and suggests actions that DWP should take to ensure its success.

WORK PROGRAMME MINIMUM PERFORMANCE EXPECTATIONS

DWP’s minimum performance expectations for WP providers vary according to the client group considered. ‘Performance’ is defined as the number of people successfully helped into employment for six months or more, achieved over the past year, as a proportion of the number of jobseekers referred to the provider in that year. Minimum performance levels expected of providers involve securing 10% more jobs than DWP estimates would have occurred without any programme in place (known as the ‘policy off’ performance level). DWP estimates of policy off performance for different client groups across the lifetime of WP contracts are shown in Table 2.

Table 2: DWP-estimated ‘policy off’ performance levels⁴

Jobs / Referrals	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
JSA 18 to 24	5%	30%	40%	40%	40%	30%
JSA 25 and over	5%	25%	30%	30%	30%	25%
ESA Flow	5%	15%	15%	15%	15%	10%

Adults claiming Jobseeker’s Allowance (JSA) comprise the largest single group of clients in WP, making up more than half of referrals in the first year of WP. For this group, the estimated policy off performance implies minimum performance expectations as shown in Table 3. This is policy off plus 10%.

Table 3: DWP minimum performance expectations, JSA 25-plus, Work Programme

Jobs / Referrals	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
JSA 25 and over	5.5%	27.5%	33%	33%	33%	27.5%

DWP expects its providers to do much better than this. Indeed, failure to achieve these minimum performance levels is punishable by contract termination, as the Department made clear in the WP invitation to tender.⁵

“DWP expects that Providers will significantly exceed these minimum levels. However, should Providers fail to reach minimum levels for any of the customer groups; it will lead to contractual action up to and including contract termination if improvements to performance are not made.”

⁴ Department for Work and Pensions, *The Work Programme Invitation to Tender: Specification and Supporting Information*, (London: HMSO, 2010), <http://www.dwp.gov.uk/docs/work-prog-itt.pdf>.

⁵ *ibid.*, 14.

FND, the predecessor programme to WP, was similar to the new scheme in the client group it served and the way in which providers are remunerated. FND ran from October 2009 to May 2011, with the most recent performance data available up to April 2011. For adult JSA claimants therefore, it is possible to assess the expectations of WP against the newly available performance from FND. How realistic are DWP's minimum performance expectations and what are the implications if they cannot be met?

WORK PROGRAMME FUNDING

Under FND, providers were initially expected to receive around 150,000 referrals each year, and the total annual contract value was around £237m. This implied that providers had around £1,600 per jobseeker referred. Each jobseeker remained on the programme for up to one year.

Funding for WP is substantially more complicated. Under reasonable assumptions, providers who meet the minimum performance expectations in the third year (when WP will be in full swing) could expect an average of (at most) £1,200 in respect of each jobseeker referred over the first three years.⁶ This funding level drops to a maximum of around £900 per referral from year four onwards. So if they achieve the minimum performance levels, WP providers would be operating with at least 25% less money than their predecessors under FND.⁷ Crucially, jobseekers remain on WP for up to twice as long as they did on FND (two years instead of one), hence the smaller amount of money per head must fund both years' interventions.

The actual level of funding per head would be higher than calculated above if providers out-performed the minimum expectations, but lower still if they fail to achieve the minimum. The latter scenario would threaten the viability of the entire Programme. So what does the performance of FND tell us about how likely it is that WP providers will achieve the minimum expected of them?

FORECASTING WORK PROGRAMME PERFORMANCE FROM FLEXIBLE NEW DEAL RESULTS

As DWP has pointed out, drawing conclusions about the likely performance of WP providers based on past FND performance is not straightforward for a range of reasons.⁸ The main reasons are as follows.

- The WP client group is much more diverse, therefore we need to compare FND performance only with WP expectations for adult jobseekers. FND performance figures included a proportion of under-25 JSA claimants, which cannot be directly compared to the adult JSA group under WP. However, the proportion of these younger clients in the FND figures is relatively small, hence they should not substantially affect the comparison. To the extent that they do, however, they would tend to flatter predicted WP performance (see Box 2).
- WP clients stay with providers for two years, rather than just one under FND, giving providers longer to achieve a job outcome. This suggests that any given level of performance (outcomes/referrals) under FND will be higher under WP.
- The definition of a 'job outcome' under WP is broader than under FND. Now providers can add together multiple short employment spells to reach the six months' employment target for which they are paid. Under FND, jobseekers were required to achieve one almost unbroken employment spell to qualify.

⁶ It has been assumed that two-thirds of six-month job outcomes attract the full 13 sustainability payments, and one-third attract nothing. This calculation includes all the revenue that will accrue from jobseekers referred in the first three years. At least some of this revenue may not be received by providers until years four and five.

⁷ In reality, funding per jobseeker will be lower still since providers were asked to offer a discount on the DWP maximum payments as part of their bids for WP.

⁸ House of Commons, "Work Programme: providers and contracting arrangements: Government Response to the Committee's Fourth Report of Session" (London: HMSO, 2011) 9.

Despite these differences between programmes, it is possible to carry out analysis for the major client group of adult JSA claimants. Indeed, such a comparison is necessary if providers and the public are to be able to determine what are realistic performance levels. Inevitably, such a comparison is subject to assumptions and judgements (see Box 2).

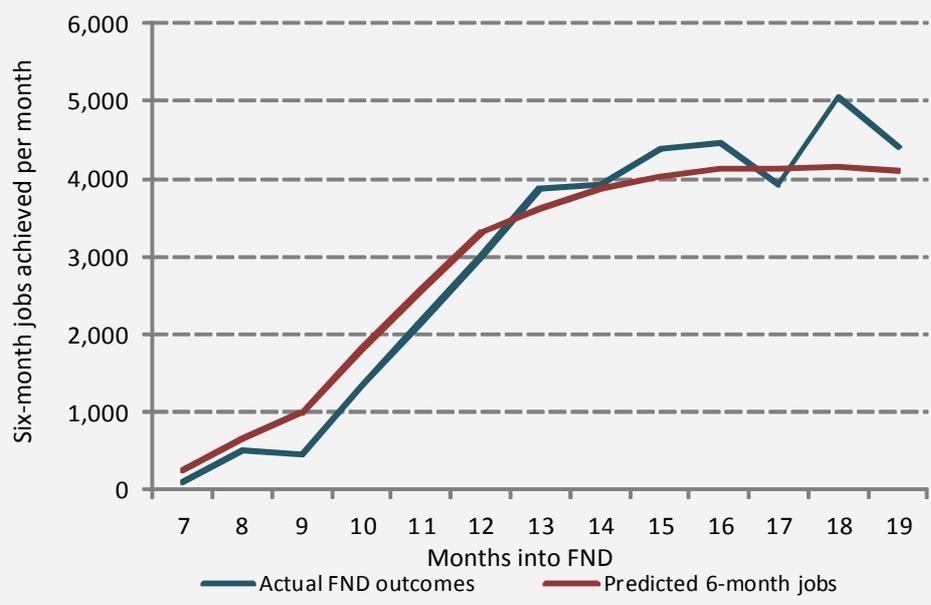
The approach taken in this analysis is to use actual FND performance data to estimate how successful providers were being at getting people into jobs. This performance is then projected forwards, with adjustments to take account of the above programme differences, to predict WP performance. Box 1 sets out the forecasting approach in more detail.

BOX 1: FORECASTING METHOD

This paper uses the six-month employment performance of FND providers - dictated by the number of jobseekers on the programme who achieve six months' employment in any seven month period - to forecast the likely performance of their successors under WP. This is done in the following way.

- The profile of off-flow from JSA to employment among adults claiming for over one year is established from benefit data.
- A job outcome *success rate* (proportion of claimants that get a job while on the programme) is combined with the observed outcome profile to give a predicted number of outcomes for each month of the FND programme.
- The job outcome success rate is then adjusted to make the predicted outcome profile most closely match the actual outcomes seen in FND.
- The success rate can be adjusted again to make the predicted outcome profile over the *two year* engagement period under WP most closely match the observed outcome profile under FND. This is done by drawing on evidence of the likely proportion of outcomes that will be secured in the second year of a jobseeker's engagement with WP providers. Chart 1, below, shows a graphical representation of the prediction model fitting the FND outcome data from month seven of FND under a success rate of 24.6% (the central case).

Chart 1: Actual FND versus predicted 2-year WP outcomes, central case success rates



- The appropriate *success rate* is then combined with DWP's referral projections for adult JSA customers to establish implied *performance levels* in years one, two and three.

In order to make the necessary adjustments to allow comparability of FND and WP, it was necessary to make a number of assumptions. Some assumptions, such as the future state of the labour market are obviously unknowable. Others are knowable but there is insufficient publicly available data to be certain about the right assumption. Nevertheless, where possible the assumptions made are conservative (i.e. they tend to flatter predicted WP performance). Box 2 sets out the nature of the assumptions in more detail.

BOX 2: DETERMINANTS AND ASSUMPTIONS

Cumulative spell outcomes in year one. Under FND a six month job outcome was defined as six months' employment within a seven month period. Under WP the six month employment period can be achieved by adding together multiple short employment spells over the provider's entire period of engagement with the jobseeker. This means that success rates should be higher under WP than FND. In the first year of engagement, however, cumulative (rather than single spell) outcomes are unlikely to make a big difference to the number of six-month jobs achieved. This is for three reasons. First, FND evidence on three and six-month outcomes shows that 'survival rates' for those entering employment quickly after referral are higher than for those entering later.⁹ Second, FND allowed for one month out of employment, accounting for many of the jobseekers who fall out of employment briefly. Third, we would not even begin to see any additional effect of cumulative spells on outcomes until month eight at the earliest. For all these reasons, the vast majority of cumulative spell outcomes will fall in year two. In the absence of any public data on this, the year one effect is assumed to be negligible.

Outcomes in year two. In light of the effect of cumulative spell outcomes it is assumed that 30% of six month job payments are secured in the second year of providers' engagement with clients.¹⁰ Nomis data suggests that only 11% of JSA off-flow between 12 and 36 months of a claim occurs in the second half of that period. Taking this assumption would further reduce the predicted success rate. However, since WP outcomes are cumulative it is reasonable to expect that the proportion of outcomes in year two will be higher.

Employment growth. The success rate is predicted on the performance of FND over the 19 months of the programme from October 2009. During that time UK employment grew by 358,000.¹¹ Unemployment also fell marginally. It seems reasonable to assume that the slowly improving labour market conditions facing FND will be similar to those facing WP over its first three years. A further sustained rise in unemployment would, however, make the outlook for WP even more precarious.

Profile of programme starts. The profile of WP referrals (jobseekers moving onto the programme) is a major determinant of the performance measures. DWP's December 2010 referral profile has been assumed.¹² Again this is optimistic in the light of the deteriorating economic outlook over the intervening eight months. There is a significant risk that referrals will not fall as fast as DWP predicts. This eventuality would further reduce provider performance in the early years of WP, as measured by DWP.

Funding per head. It has been assumed that WP providers are able to achieve results at the same rate as FND providers but with substantially less favourable payment terms (both in terms of the funds per referral and in terms of the timing of payments, which are more back-loaded under WP). This cautious assumption may make our projections more optimistic than is warranted.

JSA 16-24 involvement in FND. Under FND, JSA claimants under 25 years old were included in the Programme. Outcomes for this group therefore affect our projection of likely WP performance for the 25-plus group under WP. However, the under-25 group in FND is a small proportion of the total. Moreover, as young people tend to move into work faster than over-25s, their inclusion in the FND figures is likely to bias upwards our estimate of performance under WP. Again, this is a cautious assumption.

⁹ See the following link for data on 3- and 6-month job outcomes for an indication of this effect:
<http://research.dwp.gov.uk/asd/index.php?page=ddfnd>

¹⁰ Proportion based on author's communication with DWP.

¹¹ Office for National Statistics "Labour Market Statistical bulletin", January 2010 and July 2011
<http://www.statistics.gov.uk/statbase/product.asp?vlnk=1944>.

¹² Department for Work and Pensions, *The Work Programme Invitation to Tender: Specification and Supporting Information*, (London: HMSO, 2010), <http://www.dwp.gov.uk/docs/work-prog-itt.pdf>, 24-30.

FLEXIBLE NEW DEAL PERFORMANCE AND IMPLICATIONS FOR WORK PROGRAMME PERFORMANCE

Using the above methodology the available FND data suggests that providers were on course to get around 17% of clients into a job lasting at least six months (the FND ‘success rate’). Under WP the two-year engagement with clients combined with the cumulative definition of a six-month job outcome means that the success rate implied by FND performance is higher.

Taking these things into account, it appears that if WP providers were to perform at the same level as their predecessors, we would see a WP success rate of 24.6%. In other words past performance implies that WP providers will get around one-in-four of their clients six months’ work once the Programme is complete.

It has been argued by some that FND had a ‘slow start’ in which referrals were slow to build. This and other teething problems might mean that the above is an underestimate of the likely success rate. Taking the last six months of FND, when performance was best, implies that we might anticipate WP providers to get 26.3% of clients into six months’ work.

These success rates are one factor in predicting providers’ *performance levels*. However since *performance levels* are defined as job outcomes as a proportion of referrals in the past year, volatile levels of referrals make the *performance level* diverge from the *success rate* (defined as the proportion of people who ultimately get a job while on the scheme).

DWP predicts that referral levels will fall from around 308,000 in year one of WP to 246,000 in year two and 221,000 in year three. Since job outcomes lag referrals by between six and 30 months, the *performance level* is likely to start much lower than the *success rate* figure, and build to be higher than the success rate figure as referral numbers fall away. Using the DWP estimated referral numbers, it is possible to translate the FND-implied success rate into a prediction of performance. Table 4 sets out the predicted WP performance in each of the first three years. Both the central case and the ‘FND slow start’ case are shown.

Table 4: Comparison of DWP’s minimum expectations of Work Programme providers with SMF’s predictions of provider performance

	Year 1	Year 2	Year 3
Minimum WP performance expected by DWP	5.5%	27.5%	33%
Predicted WP performance	4.1%	20.5%	27.8%
No. jobs short of minimum	4,300	17,300	11,600
Predicted WP if FND had a ‘slow start’	4.4%	21.9%	29.7%
No. jobs short of minimum	3,400	13,700	7,200

The result is that on the central case, FND performance suggests that WP providers will substantially underperform DWP’s minimum performance expectations in each of the first three years of the programme. By year three, providers are likely to be operating at a *performance level* of 27.9%, compared to a minimum performance expectation of 33% and even a policy off estimate of 30% (the policy off estimate for JSA 25+ as outlined in Table 2). Even on the more optimistic case (based on the best months of FND), predicted performance remains well down on minimum performance in each year, reaching only the policy off level by year three.

To achieve the minimum *performance levels* set out in the WP invitation to tender, we estimate that providers would need to have demonstrated a *success rate* of around 29% (compared to the 24.6% implied by FND data). Under FND just two of the 24 providers were performing at this level over the period for which we have data. Under WP, all other 22 would potentially have faced possible contract termination.

IMPLICATIONS FOR THE WORK PROGRAMME

All of this has important implications for WP.

- **Minimum performance expectations look too optimistic.** Most obviously this analysis suggests that WP minimum performance expectations are higher than we have reason to believe is achievable. DWP's expectations – issued in December 2010 - looked very challenging to experts from the start.¹³ But this was before full performance data on FND became available and before recent downgrades of UK growth projections from independent forecasters.
- **It is not credible to threaten contract withdrawal for over 90% of providers.** If these forecasts are correct, a very high proportion of providers will be at risk of contract termination according to DWP literature. Such action would introduce costly uncertainty and upheaval in the system and is therefore not credible. Nevertheless, for investor confidence, more realistic revised expectations are needed.
- **Lower performance will put further downward pressure on resources.** At the levels of performance implied by FND, funding per client under WP will be around at least 30% less. This does not take account of the substantial 'discounts' offered by some providers on DWP's headline payment offers. Below-expectation performance therefore threatens the financial viability of the Programme.
- **Slower than anticipated economic growth will add to the pressure.** With the outlook for economic growth deteriorating in recent months, WP faces a much stronger headwind than was anticipated when the terms were set. Since December 2010, the claimant count has risen by almost 110,000 suggesting that many more jobseekers are likely to move onto the scheme over the coming year. This will add to the substantial financial pressure on providers.

WHAT SHOULD THE GOVERNMENT DO?

DWP should **revise down substantially its minimum performance expectations** in the light of new data from FND and the changing economic outlook. More realistic minimums will be a more credible incentive for providers and remove a significant source of uncertainty in the market about the consequences of real underperformance.

Predicting WP performance is difficult with the available public data, but essential if providers' bids are to be realistic, and to strengthen public accountability. For this reason, as the Work and Pensions Select Committee recently proposed, DWP should **make transparent how its minimum performance expectations are derived.**

More generally, DWP minimum performance expectations are based on estimates of what would happen in the absence of any programme. That policy off performance is likely to vary substantially with the state of the wider economy and labour market, making it hard credibly to set exact minimum performance levels years in advance. To resolve this unavoidable problem with a fixed target, DWP should develop a more transparent *process* for determining minimum performance. This should consist of two parts:

¹³House of Commons, "Work Programme: providers and contracting arrangements: Government Response to the Committee's Fourth Report of Session" (London: HMSO, 2011), 33.

- First, to reduce uncertainty around the programme substantially, DWP should **clarify how policy off performance will change if labour market conditions deteriorate**. Such a step would reassure taxpayers by ensuring that any additional funding to providers in that scenario would only reflect changes in the economic outlook.
- Second, given the challenges that macroeconomic fluctuations and regional variation raise for assessing acceptable performance, DWP should look at introducing **a comparative minimum performance requirement among providers**.

Funding per jobseeker referral is very sensitive to performance levels, which is the nature of an outcome-based system. However, the risk is that the attainable level of outcomes has been substantially overestimated with the effect that outcome payments may well be too low for the programme to be financially viable. DWP should **consider raising outcome payments**, since widespread financial failure in among providers will ultimately be more costly for taxpayers and jobseekers.

The Government has stated its aim to be “the most open and transparent government in the world.” This is a laudable aim. Yet the plans for WP fall short. DWP has said it will release the first performance data on WP in autumn 2012. For the purposes of transparency and accountability, DWP should therefore **commit to publishing monthly performance data starting immediately**.

The prime contractor model of the WP is the right one. However, in this extremely tight funding environment, subcontractors (particularly those in the Voluntary and Community Sector) are highly vulnerable to having financial risk off-loaded onto them by primes operating under extremely tight financial conditions. DWP should **investigate and monitor the distribution of outcome risk between primes and subcontractors** if it wants subcontractors to remain viable.