



# membership resources

**APSE briefing 12-51**

**October 2012**

To all APSE main contacts in England, Wales, Scotland and Northern Ireland

## **Traded services and client / contractor splits in service delivery**

### **Key Issues**

- APSE conducted a survey amongst its member local authorities to explore the current position with regard to client / contractor splits in service delivery
- This briefing explores the findings of the survey and comments on the issues raised within the survey
- This paper also explores the recent policy moves at a central Government level which appear to tacitly support a return to purchaser / provider splits in service delivery.

### **1. Introduction**

During the summer of 2012 APSE conducted a short survey of member authorities to explore the prevalence or otherwise of remaining client / contractor splits in service delivery, whereby the operational and compliance side of service delivery is separated from the strategic policy, budget and monitoring elements of a service, often referred to as a purchaser / provider type arrangement. This is in respect of 'internal trading' within councils, as opposed to external trading or external contracts, outside of the council's owned directly provided services.

Such arrangements were commonplace particularly in areas of 'traded services', where the direct labour or direct service organisation relied upon 'income' from the client side to deliver specific elements of a service, with costs often broken down into unit prices for specific types of work. The client side role was to raise or authorise work, including any variations to that agreed and to monitor compliance and performance. Many traded services operated under a harsh split between the delivery side (the contractor or provider) and the client side (the purchaser). This briefing summarises the responses and analyses the sustainability of such

arrangements, in the current context of pressure on public services and developing policy. New policy direction such as the Community Right to Challenge and the 'Open Public Services white paper' which are detailed later in this briefing appear to encourage a return to these types of arrangements, despite documented difficulties with this approach to public service delivery.

## **2. Context of client / contractor splits in traded services**

The introduction of compulsory competitive tendering (CCT) of local government services brought with it a plethora of both legislative, and statutory guidance matters, that culminated in the adoption of stark client / contractor splits within local authority frontline services.

The client side has tended to take on responsibilities which would typically include:-

- Identifying the service needs
- Setting service specifications or requirements
- Setting budget and /or prices (unit costs)
- Managing 'contracts' (both internal and external) and
- Monitoring performance and setting policy objectives

Whilst the contractor side would:-

- Deliver the contract or services in accordance with the clients specifications, including service frequency, quality standards , and the management of frontline employees
- Provide management information to the client side for the purposes of performance management and
- Provide the technical expertise to manage and run the operations
- Operated under a 'trading account' arrangement whereby service costs including labour costs, supplies, management costs were recharged to the client side thus creating an internal 'income' stream.

However, with the decline of CCT and introduction of 'Best Value' principles, many authorities reconsidered the client / contractor split and moved towards more integrated methods of service delivery. Integrated services are designed to allow the linkages between both policy and operational requirements into more holistic approaches to service delivery. Integrated delivery removes the false 'purchaser / provider' split in public service delivery with services operating against a pre-agreed budget.

### **3. What about 'trading accounts'**

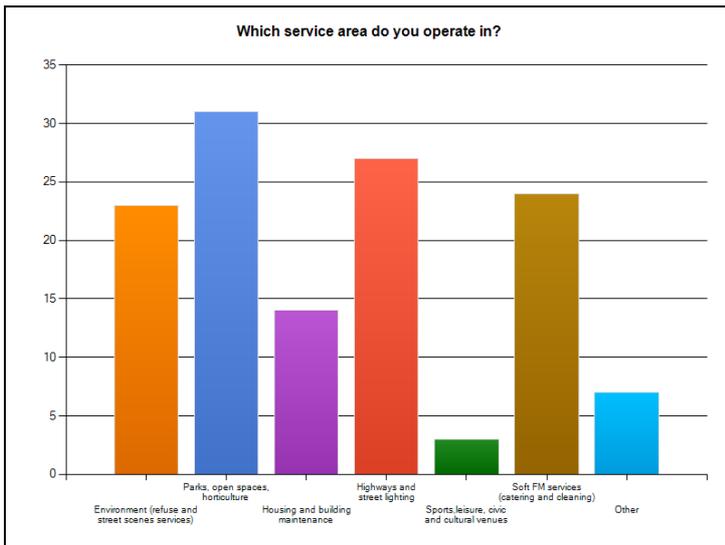
Internal trading (as opposed to external trading) is where 'trading' is between two departments or other parts of the organisational structure of a single body in which one acts as the client and the other as a contractor. During CCT there was strong differentiation on trading accounts keeping the accounts of the DLO or DSO separate.

Currently there is no prescribed form for trading accounts although SeRCOP (Service Reporting Code of Practice governed by CIPFA) requires a separate trading account to be kept for each trading organisation showing the full cost of the service and the credits corresponding with changes made to clients ( in accordance with its tenders). However authorities are free to decide what constitutes a separate trading organisation and therefore many 'contracts' may be covered by one trading account, reflecting the different management structures within different local authorities. Within Scotland the Local Government in Scotland Act 2003 (advisory note from the Best Value Task Force) similarly suggests Councils should be supported by robust, business-like accounting which detail income and expenditure in a manner which permits activity-based costing, cost and process benchmarking and other tools of Best Value to be applied. BVACOP defining those activities, which require published trading accounts, includes work carried out by internal trading organisations arising from voluntary competitive tendering exercises. However it is important to note that there is no requirement to operate on the basis of a harsh client / contractor split.

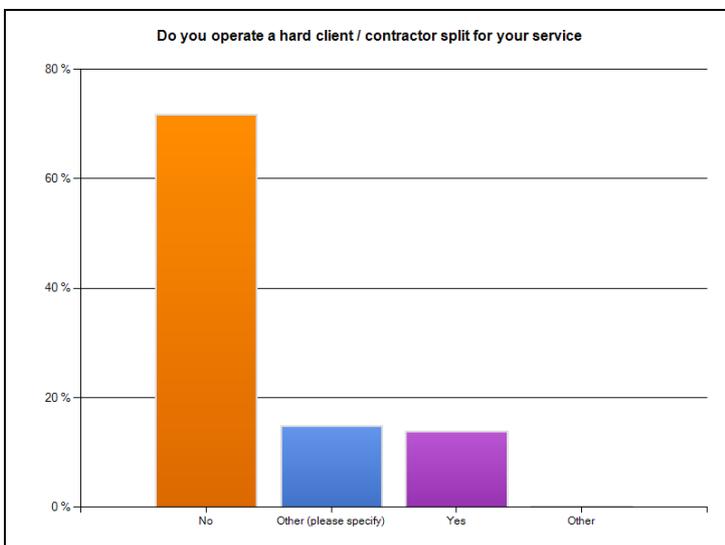
In recent years there is strong evidence to suggest heavy increases in central establishment charges. 'Traded services' often have little or no control over how such charges are set or increased and limited influence on the quality or quantity of services charged for under central establishment charges. This can of course distort 'trading accounts' where performance at an operational level may be high but cost and efficiency appear to show weaker performance as a result of the impact of CEC costs on the service. This is evidenced in detail through APSE's performance networks data on frontline services.

#### 4. Results of the APSE survey

APSE surveyed a range of frontline services with a predominance of respondents working in environment based services such as parks, grounds maintenance, (31%) refuse collection, and recycling (23.5%) and highways and street lighting (27.4%) and in FM services (24%).



APSE asked whether or not services continued to operate on a hard client contractor split. 72% of respondents reported that they no longer operate under a hard client contractor split with just 16% reporting that they continue to operate on this basis with 15% reporting a mix of arrangements with some services operating under some form of separation but not a 'hard split'.



APSE asked respondents **'What do you see saw as the advantages or disadvantages of a hard client / contractor split.** Responses were varied with those maintaining support for a hard client contractor split stating:-

*'Clarity of purpose; robust discipline of debate and challenge'*

*'The service delivery and responsibility for service delivery is clear cut'*

However many respondents cited that they felt that there was no real advantage to a hard client / contractor split and many in fact felt that this route produces unhelpful and inefficient market mechanisms

One commented:-

*'We used to have a client/contractor split and to be honest it was a disaster. The 'contractor' was focused on maximising profit whilst we were focusing on maximising quality. This led to conflict and there is no doubt about it, a drop in standards and also a duplication as officers went out to inspect and agree standards and payments. There seems to be an assumption that it can be done cheaper. Well of course it can but the old adage "You get what you pay for" is as true in service contracting as it is in purchasing goods.'*

Further respondents said:-

*'Advantages of a hard split were mainly transparency in terms of costs and accountability. However the disadvantages include costs of tendering, the uncertainty it can cause within the workforce, difficulties meeting rates of returns, less flexibility with regards reducing costs. Moving away from a hard split allows much more of a partnership approach to be developed'*

*'No advantages, only disadvantages of unnecessary duplication of effort'.*

*'For the contracts with private contractors it enables us to use a procurement strategy to drive value (and savings) for the council and optimise internal service provision. As an example we use private contractors for some recycling collections and selling the recyclables on. There are no advantages to the service provider but perhaps reassurance for the customer. Key disadvantages are inspections/defaults add to the cost of service provision for the customer and inspections/defaults distract frontline staff attention from a focus on customers' needs'*

However many respondents distinguished the need for a hard client contractor split on outsourced services ( by necessity this is the most likely structural outcome of contracted out service) but equally respondents were concerned that this became a focus upon targets, and performance, rather than a focus on continuous improvement in service delivery. Some feared that this false separation actually led to public expectations of service delivery becoming a secondary consideration to *'playing shop'* creating, a false divide between the provider and purchaser. [*'Duplication, additional staff, too much playing shops taking eyes off public expectation'*]

APSE also asked respondents **'Have you made a decision to move away from a hard client / contractor split? If so why?'**

The overwhelming answers on the reasons to move away from a hard client / contractor split related to cost and duplication issues, whereby the separation, of service delivery and policy, gravitated against a holistic approach to service delivery.

*'Reduces cost, argument and administration. Allows early 'contractor' involvement using own internal resource'*

*'Reduce financial transactions - make the service same as other Council services i.e. spend budget in best way'*

*'Rationalised management structures and reduced overheads'*

*'Move away from split was to try and provide a more responsive and joined up service to internal users and public in general, also to remove duplication of resources at a time when funding is critical'*

*'Cleaning has been in one area for some years and school catering amalgamated 18mths ago - it was decided that there was too much duplication of duties and it caused a lot of confusion in schools - we consider our service is much more efficiently delivered without the split and schools still have the option for advice if required'.*

*'It is more cost effective to be integrated.'*

*'Move to a soft split allowed the removal of some duplication, particularly around use of technical staff during the "works" phases'*

*'We believe that VFM could not be achieved within a hard client and contractor structure'.*

*'Yes to allow us to work as area based street-scene solving problems and joining up working'*

*'Reduce cost of administering contract arrangements and back office duplication'.*

*'The client / contractor split operated until 12 months ago when it was realised that inspections added to the in-house service costs for the Council. The split is likely to be reintroduced when we become a local authority limited company later in 2012.'*

It is clear from responses however that some authorities still maintain a soft client / contractor split but the majority now favour a more integrated approach to service delivery. This also includes potential benefits from the perspective of managing employment and productivity issues. Rather than the 'carrot and stick' of performance related bonus schemes a shared vision of delivering a quality service with the involvement of the workforce in an amalgamated service. One commentator noted

*"[Our authority] has always carried out the parks, streets and waste services in house. During the CCT era we had a Client, Contractor, and Agent split, with the agent managing the contracts and recharging client departments via service level agreements. At the end of CCT the decision was made very quickly to revert back to a client and operational services setup which lasted to 2003 when all were amalgamated as Environmental Management and were then a combined client and service delivery organisation. One of the key benefits of this was the removal of duplication of effort and to focus on quality rather than Quantity and Bonus schemes which were operated throughout the CCT era and which were then amalgamated into basic pay.*

Time delays were also featured as an issue in responses with one respondent noting that they had managed the '*Removal of unnecessary administration and client costs*' which had resulted in maximising investment in frontline resources. It was also noted that a beneficial impact of this was the removal of time delays in service responses due 'client' processes having to take place before the 'contractor' delivers the service, making the integrated service more effective at response times.

Some operations have acted on external advice with one noting that they had acted on the advice of an Audit Commission report which had noted that the 'hard split added cost to an in house operation'.

**APSE asked 'Have you been able to quantify any savings or quality improvements from more integrated ways of working?'**

Over 37 variable answers were provided to this question but notable savings appeared to have been generated from decreased bureaucracy and slimmer management structures.

*'£800k off management structures across the service.'*

*'Too numerous to account for here, but savings mainly come from integrated teams within a large pool of labour dealing with issues in a single pass and moving with the work needed, thus cutting unproductive time. Overall savings to date are around 12% of original budget.'*

*'Circa £5 million in savings across the whole range of services'*

*'Facilitates smoother communication to customers (mostly schools) and saves a full time salary for a client officer (approx. £27K)'*

*'Reduced staffing numbers (2 x FTE's) removed paper based systems and used IT solutions - integrated software for service area.'*

*'Inspection of the in-house cleaning provision was adding an extra £44k/annum to the service charge (equivalent to 4% of the cleaning value). This £44k of unnecessary expenditure became part of the local authority's efficiency savings. Frontline staff now have a focus on customers' needs rather than on 'pleasing' the inspectors. Frontline staff are now willing to go that 'extra mile' as they feel their work is valued and appreciated by the Council.'*

*'We are saving up to £2.5 m per annum through new ways of working, including abolition of the client/contractor split. Customer satisfaction with the service is also rising.'*

*'Difficult to establish actual figures that are attributable to having no contractor/client split but have achieved upper quartile performance on indicators based on NI195 and 196, have reduced costs per household and head of population and income generation has increased'.*

The savings and other improvements in service quality are of course dependent upon the size and nature of the services involved but the consistent theme of savings and improvements from the survey results are:-

- Savings in management structures
- Reduced administrative burdens
- Reduced cost and bureaucracy of inspection / compliance
- Seamless service delivery – right first time approaches with a focus on quality rather than headline compliance with specifications.
- Responsiveness and inbuilt flexibility to changing service needs without the need to renegotiate specifications and costs
- Ability to respond to ad-hoc emergencies such as severe winter weather, public emergencies

The majority of respondents, 58%, operate in-house services but a further 43% operate mainly in-house services with some external contracts. Some respondents were sceptical about the operation of 'thin client' models on outsourced contracts. These arrangements can be typified by a contractor being required to self-monitor contract compliance against set performance expectations and to report to the 'thin client' on contract performance; this would also include incidences of performance failure. Respondents felt that these arrangements with contractors who are encouraged to self-monitor, and report on their own contract performance or performance failure have no incentive to be rigorous or objective in their judgements (particularly on outsourced contracts this was considered to be highly unsuitable).

## **5. APSE comment**

It is clear that many local authorities have rejected a hard split between 'purchaser /provider' or 'client / contractor', in favour of more integrated and flexible approaches to service delivery. The results of the APSE survey would support the view that client / contractor splits in in-house service delivery, more-often-than-not, add to costs and inefficiency, and that these problems equally arise within outsourced service delivery which require stringent monitoring and performance management. The accepted orthodoxy of the CCT era of internal markets has been replaced by integrated services but it is clear that this is based on

the best and most efficient use of resources to service needs. There is still an on-going emphasis on performance management but with the ownership of performance being across the service.

The reported benefits of integrated service delivery provide for a more joined up approach between operational delivery and policy objectives, and avoid duplication and bureaucratic burdens. The lack of a hard client / contractor split supports a view that integration leads to greater employee ownership of the service outcomes. In many cases it is also reported that the managerial structures are de-layered as a result of integrated working. There are also consequential reductions in the costs of failure demand because of the ability to introduce better responses and new systems and processes.

However recent developments in national public policy suggest that a return to the separation of purchaser / provider or client / contractor splits are once again being favoured by Government.

The open public services white paper ( at chapter 3 on commissioning) identifies a commitment which states *'The Government will look at instances in which the separation of purchasers from providers makes sense as a means of encouraging innovation and diversity of provision'* and goes on to say *'The Government has made significant progress with implementing structural reforms to separate purchasers from providers, notably through health and welfare reforms'* and continues that *'Building on this, we are also introducing a far-reaching programme of new payment by results contracts...'*

Such statements are a concern to APSE. There is no evidence that a separation of 'purchaser and provider' in public services will breed greater efficiencies or better outcomes. A recent CBI report claims that through diverse provision an average of 11% efficiency savings can be achieved however, aside from a generic calculation based on the total for public service spending, the CBI does not evidence this 11% figure. It is an assumption. Moreover the report fails to contrast assumed savings with the inbuilt inefficiencies of purchaser / provider splits and costs to the public sector of duplication, contract monitoring, performance and compliance. The CBI report also fails to recognise the innovation in public services that have already delivered huge efficiencies through restructuring and transforming service delivery models, including through integrated service delivery mechanisms. In waste and recycling APSE's own performance data shows productivity improvements, reduced costs compared to improved service delivery on recycling, and reductions in landfill tax payments as a result of

service redesign and integration. Costs have also been reduced through the adoption and use of route optimisation technologies and the integration of policy and delivery, such as public education campaigns on recycling and waste minimisation. The Open Public Services White paper, and the CBI report, in stating that purchaser / provider splits may generate efficiencies does not adequately consider that many of the assumed savings have already been made as part of the internal service redesign and service delivery integration that has already taken place in local authority frontline services. Equally such reports and statements do not consider the inherent additional costs of managing purchaser / provider splits in service delivery nor make any attempts to quantify such costs.

A further concern for APSE is that developments, such as the Community Right to Challenge, could invoke unwarranted competition in public service delivery through the requirement, if an expression of interest is accepted, to hold an open procurement exercise. The involvement of in-house teams in bidding processes could see a tendency to separate out the service delivery providers into 'contractor' style relationships during the conduct of the procurement exercise resulting in additional costs and bureaucracy to local councils. This is a great concern when budgets are limited.

Whilst there is no 'one size fits all' model to service delivery in times of pressured budgets it is important to consider the often hidden or obscure costs associated with hard client / contractor arrangements. It is equally important to avoid succumbing to policy fads that suggest without evidence that purchaser / provider arrangements are some form of panacea to deliver efficiency savings when often this can both frustrate and add costs to frontline services.

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