

Valuing social impacts:

Should government
pay for results?

Talking Points

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Introduction

In the face of deepening spending cuts and low economic growth all parts of Government are recognising the need to do things differently. Engaging and incentivising voluntary and social enterprises to tackle social issues and improve outcomes for vulnerable groups is one of these approaches, and a key strategy of the Big Society Programme.¹

There are, however, significant barriers to third sector organisations providing services to the public sector. Public sector commissioning focuses too often on activity rather than outcomes and concentrates resources on addressing the consequences of negative social outcomes rather than their prevention. Also, accessing private sector working capital, needed to provide an appropriate level of alternative and preventative service provision, is often difficult for social enterprises.

To address these issues the Government has embarked on a programme of pilot programmes to implement Payment by Results (PbR) across various social service areas. The expectation is that PbR will offer the opportunity to deliver new and enhanced services to address social needs that, in turn, will lead to better outcomes and consequently reduce public exchequer costs which, where ‘cashable’, will provide investors in such services with appropriate financial returns.

In order to understand whether these outcomes are achievable it is important to understand how changes can be measured, monetised and traced to actual reductions in public sector activities and/or expenditure. Consequently the measurement of social impacts is one of the key components to taking such approaches forward.

In the context of reduced public sector spending, the requirement for the public sector to achieve more with less and the transition towards outcome-based procurement, this Talking Points publication provides an approach to measuring social impacts. In addition, we discuss our views on the other practical issues and related steps to achieve wider adoption of PbR by Departments and ensure consistent delivery of better future outcomes.

¹ “I profoundly believe that if we want real social change – if we want to solve our deepest social problems, whether it’s drug abuse, whether it’s problems of poor housing, whether it’s problems of deep entrenched poverty, whether it’s problems of children in care – it’s going to be the voluntary sector, social enterprises ...” (David Cameron, 18 May 2010).

When will Payment by Results work?

Voluntary sector and social enterprises offer significant opportunities to realise, in partnership with Government, better social outcomes and related cost savings. The success of PbR is dependent on being able to make payments to these organisations according to the social

impacts achieved and subsequent cost savings which means that PbR will not be suitable in all situations. As illustrated in **Table One** below, there are various pre-conditions that need to be in place before PbR is likely to be applicable.

Table One: Pre-conditions for PbR

Pre-condition	Description
Social need or opportunity	There is an identified (unmet) social need and significant public sector costs associated with the outcomes of containing or 'fire fighting' social ills ² .
Better outcomes	In addressing this need, other providers, either independently or jointly with the public sector, could deliver better and new social outcomes – e.g. preventing drug taking rather than paying to reduce the consequences of drug abuse.
Cost savings	Such outcomes should have public exchequer benefits in terms of cost efficiencies and/or cashable savings – e.g. reducing the numbers of children going into care may lead to reductions in (consequently unnecessary) child care facilities and related services, which in turn reduces public sector costs.
Value for money	Delivery under PbR gives better value for money than any alternative approach.
Investment interest	There is sufficient interest from providers, either directly or through investors, to raise the necessary levels of working capital in order to provide services, prior to any future payments from the public sector on the delivery of (pre-agreed) outcomes.
Commissioner Payment	If future outcomes are achieved commissioning bodies are in a position to make payments to the provider or their investors (with a level of return over and above the working capital required to provide services).
Contracting routes	There are clear contractual routes to bring together commissioners, providers and investors – e.g. social impact bonds, intermediaries, 'simple' price agreements for the delivery of specified outcomes or other contracting routes.

With these conditions in place Government spending on existing social programmes could be reduced through incentivising the delivery of better future outcomes. Offering financial returns for the successful delivery of these outcomes could be funded by savings to the public purse.

PbR approaches are already being piloted by the Government – including programmes within DWP, DoH, MoJ, DCLG and the Cabinet Office.

In order to further develop such approaches, and ultimately develop the market for PbR, we believe there are several challenges that need to be addressed by Government:

- **Identifying the potential benefits of new forms of service provision** – how should social impacts be measured?
- **Translating these impacts into public exchequer benefits** – do the maths work in terms of ‘cashable’ savings with sufficient returns to attract investors and providers?

- **When to measure and what benchmarks to measure against** – how do we ensure that economic fluidity and market changes that occur during the course of a PbR contract do not leave either party financially penalised?
- **Generating sufficient ‘market’ interest** – how do we bring together Government, providers and funders?

Measuring and monetising social impacts

In order to understand whether real social change can be delivered, it is essential to understand how any proposed new or enhanced services can be measured, monetised and traced to actual reductions in public sector expenditure. Without a way of capturing these measures it is unlikely that investors, providers or Government will be able to agree future payments.

What are social impacts?

Social impacts are the effects of an activity or service on the social fabric of a community and the well-being of individuals and families. Such impacts can be measured in terms, for example, of changes in levels of health, crime, sustainability, education, community cohesion and diversity.

By improving social conditions such impacts may also reduce pressures on the public sector. Tackling homelessness, for example, not only has great benefits to individual lives, but also results in lower incidents of hospital and prison admissions, benefit payments and other 'public exchequer' costs.

Valuing social impacts

Understanding the relationships between changes in social impacts from new service provision, and how such changes may or may not affect public sector costs, will be essential to understand where PbR approaches might have the greatest impact on outcomes and costs.

There are 5 key stages to valuing social impacts, as illustrated in **Figure 1** – the 'situation' or social needs being addressed, the inputs or resources required to meet these needs, the range of activities or services that could be adopted, the outputs that might result and the final 'impacts' for society as a whole.

The presumption – both in designing services and evaluating results – is that there is a causal link between activities and the ultimate change in behaviours.

Figure 1: Impact steps



Figure 2: Measuring impact



The way to judge such causality, as shown in **Figure 2**, is to assess what might have happened in the absence of these new activities or services.

Valuing social impacts provides a basis to assess the potential benefits of new (and existing) services. But the real challenge for Government is whether such benefits are 'cashable' – will there be recognisable and measurable changes in current and future public expenditure profiles? PbR introduces a further step to social impact measurement by 'challenging' providers to indicate how, through their services, impacts will be measured, monetised and traced to (actual) reductions in public sector expenditure.

Case in point

Our recent work with the SPARK programme explored a range of questions in relation to the homeless and unemployed people they support. We asked SPARK participants what they would have done in the absence of help, what changes having the support of SPARK has led to and what has been the long term effect on them.

One of the ways to 'monetise' these impacts was to consider the effect upon the public exchequer. For example, over a five year period, we identified that for every £1 invested in the SPARK programme over £6 is likely to be 'saved' by the public sector in terms of reduced housing, unemployment and other benefit payments.

Finally, while it was apparent that the overall effects of the programme were positive – in terms of reduced homelessness and unemployment – some activities were better than others, which informed future planning, delivery and funder decisions.

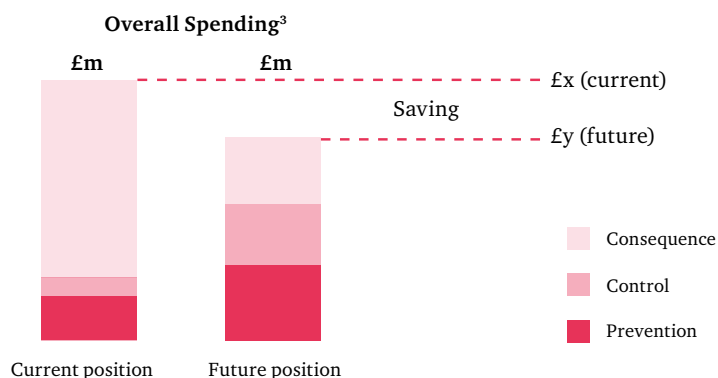
Identifying cashable savings

Our recent work with various local authorities suggests that one of the ways to address this challenge is to consider current levels of public expenditure in terms of three broad categories – the **prevention** (or ‘early intervention’), **control** and **consequences** of dealing with negative social outcomes.

Typically, as illustrated under the ‘current position’ at **Figure 3**, public expenditure is strongly ‘skewed’ towards paying for the consequences of social issues (e.g. in terms of prison places, benefit payments, health and social care). Earlier interventions – under the ‘future position at **Figure 3**’ – can offer the potential to reduce such consequences and in certain cases reduce the overall costs associated with a given social issue.

Bringing together providers who have potential to generate positive social impacts, and considering how such impacts will reduce actual public expenditure, provides the opportunity to radically alter future service provision. Making this happen – under the auspices of PbR – presents various other challenges for Government, not least how to develop the market for such services, how to procure providers and how to measure outcomes.

Figure 3: Generic cost outcomes



Case in point

The Cabinet Office has recently identified that the annual public sector costs of 120,000 families in England with multiple social problems falls within the region of £100,000.

The majority of these costs relate to benefit and care related services. If early intervention approaches could reduce the number of such families that require these services by 10,000 the potential public savings could be as much as £1 billion per annum (i.e. 10,000 x £100,000 = £1 billion). Moreover, if the costs of such intervention approaches were less than such savings – at the type of rate of 1:6 identified for the SPARK programme – then such services could be paid for and rewarded by the Government at a lower overall cost than currently. In simple terms there would be better outcomes at less cost.

³ i.e. if the net cost of new services is less than the net saving obtained – namely £x million - £y million – then a PbR approach may be worth considering.

Stimulating market interest

Markets operate where transactions occur because there are both willing buyers and sellers. Creating such conditions for PbR, in relation to social needs, is being led by Government through a range of steps, including:

- Supporting providers in bidding for public service contracts through such initiatives as Big Society Capital and the Cabinet Office Investment and Contract Readiness programme
- Engaging, through the above and other initiatives, with funders and intermediaries, to generate interest in PbR and investment support
- Considering how best to disseminate information, guidance and ‘best practice’ principles – to commissioners, providers, intermediaries and funders – through such proposed projects as the Early Intervention Foundation
- Developing and implementing, with various commissioners, pilot projects and programmes to test PbR procurement approaches

The Government is endeavouring to generate the conditions for both ‘willing sellers’ – in relation to the first three steps above – and ‘willing buyers’ in relation to the last step.

The approach of these buyers or commissioners to procurement of PbR is informed by their approach to social impact measurement:

1 Based on cost profiles and the implications of reducing future costs.

In this case commissioners are clear what savings they will secure for given outcomes (e.g. the closure of a children’s care home, employment of a given number of NEETs - Not in Education, Employment or Training-, reductions in drug taking etc.). Consequently they may adopt a ‘black box’ approach which (simply) asks providers to ‘bid a price’ for this desired outcome and re-assure commissioners that each provider has access to sufficient funding to deliver this outcome before payment. Under this approach how outcomes are delivered are the primary responsibility of providers – they need to be convinced, as do their investors, that these outcomes can be achieved over a given period and cost. As such the ‘risk’ of delivery is ‘transferred’ to providers and their funders.

2 Based on activities and outcome profiles, leading to positive changes in social impacts.

In this case the commissioner wishes to have insight into the workings of the ‘black box’ – what activities will lead to behavioural change and impact upon costs, how these will manifest over time and when, for example, facilities could be closed down, service mixes altered and other savings be achieved. With this information commissioners can agree not only on ‘the bid price’ for services but also what outcomes are to be expected and when ‘payment triggers’ may apply. Such information is particularly important where the public sector works in partnership in the delivery of services (say between statutory and non-statutory care) – risks may need to be spread across partners and mutual outcomes and dependencies reflected in contractual conditions with providers.

Either of these routes, and combinations of such approaches, are likely to be adopted going forward – their ultimate success, however, will depend post procurement on whether real returns can be delivered and rewarded. In short, planning for change is not necessarily the same as ensuring change occurs. As PbR is implemented there will need to be confidence from any commissioning body on how returns are incentivised and measured.

Driving delivery

The ultimate challenge for Government, in using not-for-profit organisations to drive social change, is assuring that payments for performance lead to desired outcomes.

Payment levels will be based on the savings achieved from delivering net social benefits⁴. This requires consideration of the issue of attribution to the provider or providers in delivering outcomes. In principle, any commissioner will need to be satisfied that “but for” the provider the changes in outcomes would not have been achieved. In practice, as already indicated, it is not possible to directly observe the “counterfactual” (i.e. what would have happened anyway in the absence of a provider). Indirect measures of net social impacts, however, can be used, for example:

- **Control groups** – analysing the outcomes and effects on the public exchequer of the activities of similar groups or individuals that are not in receipt of provider services
- **Intermediate (benchmark) data** – assessing the outcomes either against known norms or target outcomes (e.g. reductions in the average incidence of children being taken into care in similar areas or closure of children’s care homes as a result of lower incidences of admission)

⁴ Another consideration, as implied in the previous section, will be the market price for achieving these social impacts as determined through competition between providers at an initial procurement stage.

- **Independent beneficiary surveys** – that assess outcomes by evaluating and questioning the “target population” in relation to the effect of provider services on their behaviour and their views on what would have happened in the absence of these services

In many situations, social impacts can be achieved at lower cost with one population group than with others. For example, if a provider is given a target of reducing prisoner re-offending by 5%, they may focus on ‘first offenders’ who are most likely to be responsive to an intervention and, therefore, the least expensive group to target.

This means that opting for a provider who offers the lowest price may not necessarily be the best value for money if they are not incentivised to provide an efficient level of service. The payment mechanism will need to be calibrated to give different incentives as performance tiers are exceeded to ensure efficient investments are made. So, for example, for a given prison population a PbR contract may be cast in terms of reducing reconviction rates across a range of different prisoner categories.

Similarly, where the consequences of failure are significant, the commissioner may wish to consider entering into contracts with providers where poor performance results in penalty clauses. One way of doing this would be to require minimum investment

levels as part of the contract: where social impacts are not being delivered the commissioner could demand compensation equal to the unspent portion of the minimum investment.

Finally, the longer it takes for a given level of social impacts to be achieved the less valuable they are in present value or today’s terms. Similarly, the longer the social investor waits to earn returns the greater the returns they will require. Consequently it is important to decide the timing of performance payments and the performance measures to be used in realising such payments.

For example, where social investments are made in years 0 – 5 and social impacts are achieved in years 5 – 25, it may make sense to make performance payments from 100% of forecast savings to be realised in years 5 – 10 in order to minimise the cost of funds charged by the social investor. In this way, the commissioner will make payments from savings while also minimising the cost of social investor finance.

Again the use of social impact measures, and the projection of how and when impacts will be delivered that have a significant and measurable effect on public exchequer costs, will be essential to designing the payment mechanism and considering when and what to pay as a result of ‘attributable’ outcomes.



Conclusions

Government recognises the opportunities for voluntary organisations and social enterprises to deliver significant social benefits and at the same time reduce the burden of the financial consequences of negative social impacts related to unemployment, crime, drug abuse and other ‘hard’ issues.

PbR approaches are currently being piloted to help these organisations overcome the “barriers” of financing and commissioning and to develop a market for new services. Measuring the impact of these approaches will be critical for Government to assess the cashable savings in terms of the public exchequer and how to reward providers whose activities deliver such savings.

Impact measurement is also critical to providers and investors. Measuring their net social impacts, now and going forward, is essential to understanding the risks and rewards associated with public service contracts based on improvements in social outcomes.

Generating real social change – through PbR approaches – will depend on the willingness of commissioners, providers and investors to engage in the contracting and delivery of services. The future prize will be to reach a degree of market maturity where the confidence to invest is matched with the confidence to deliver at a national and long-term level.

Attribution will be key to establishing such conditions – the “but for” question will need to be addressed in order to incentivise delivery, and, as importantly, release payments. Impact measurement will continue to be key – to evaluate what has changed and why.

Consequently, under PbR, the use of social impact measurement will become central not only to considering new services but also to paying for them. Government will need to demonstrate to all of us that what they are paying for is delivering real social change and benefiting people’s lives.

Recommendations

The market for PbR is relatively under-developed and the barriers to change many and varied. However, if the benefits of PbR approaches to commissioning are to be realised, various steps now need to be considered by Government, including:

- **Developing measurement and procurement guidelines** – key to this is access to cost and impact data which will allow commissioners to gauge the extent and applicability of PbR in relation to any given social issue
- **Implementing protocols for sharing the benefits (and payments) across commissioners** – many of the social issues concerned will have multiple saving implications across a range of Government Departments and single commissioning does not necessarily capture such implications
- **Ensuring ‘scalability’** – to both attract new funders and to deliver a significant scale of effect within the short to medium term – if a pilot programme works it should be applicable on a wider national scale
- **Delivering benefit** – from tax relief or other forms of financial incentive to generate wider interest from the investor community in supporting PbR delivery

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Contacts



Mark Graham

+44 (0)131 260 4054

mark.c.graham@uk.pwc.com



José P Retana

+44 (0)20 7212 6974

jose.retana@uk.pwc.com

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