Risk transfer in outcomes-based contracts: Real or illusory?

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Context and Research Question

- SIBs and other forms of outcomes-based contract (OBCs) are typically understood as involving an element of risk transfer from the public sector to the private and/or third sectors.
- Compared to traditional fee-for-service models, OBCs limit the liability of the government payor where the specified outcomes are not fully achieved (Joy & Shields 2020; Edmiston & Nicholls 2017)
- **BUT** given that the public sector remains ultimately responsible for ensuring certain social outcomes such as minimum standards of health, welfare, justice or security, can the risk of failure to deliver these outcomes be meaningfully transferred by contract?
- **Research question: What do responses to the Covid-19 pandemic by parties to public sector OBCs tell us about the degree of risk transfer under these contracts?**

Theory and hypothesis

- OBCs can be seen as part of a broader trend of **quasi-marketisation** in public service delivery (Le Grand 2007, 2011) – but only if users have a choice AND there is some degree of competition amongst providers
- User choice is directly linked to increased financial and performance risks in OBCs, e.g. low take up > failure to meet targets > failure to achieve payback
- If users lack choice and/or there is little or no provider competition, the benefits of quasi-marketisation over direct public provision are questionable
- **UK:** relatively little user choice and provider competition in OBC 'market'
- In order for OBCs to 'make sense' from a theoretical point of view, risk must be transferred to the private investor and/or service provider

Hypothesis: Responses to Covid-19 show that only limited performance and financial risk is taken on by private and third-sector parties to OBCs

Preliminary findings

- Cabinet Office PPN 02/20 *Supplier relief due to Covid-19:* “Where contracts operate ‘payment by result’ or are ‘output / outcome’ based, payments to suppliers should be made on the basis of a calculation of the average of the last three months’ invoices” [even if performance is suspended/disrupted]
- **Example:** Project Apollo (Care Leavers SIB Sheffield) “approximately half our care leavers have (hopefully temporarily) dropped out of the programme as it is simply not at the top of their agenda at this moment in time…our ‘big ticket’ outcomes of entry into education; employment; and sustained employment – are not there, given that educational and training establishments are currently closed…changes to the rate card to reflect this are not currently under discussion – though we are hopeful of exploring some flexibility around length of contract”
- In a society-wide crisis government is expected to underwrite risk…and for some public services **outcome risk can never meaningfully be transferred**, although financial risk of intervention may be

The exception that proves the rule? And broader implications…

- To the extent that responses to Covid-19 are exceptional, they may not allow us to draw general conclusions about risk transfer under OBCs
- **BUT** risk transfer only really matters when things go ‘off-piste’; if everything goes to plan then it doesn’t matter where the risk sits
- If risk transfer is illusory, then parties to OBCs (and other public contracts) could save a lot of time and money (insurance, legal, etc) arguing about it
- Size and diversity of market of potential providers of OBCs may also be reduced by perceived levels of risk attaching to these types of contract
- **User choice:** only government can mandate the use of a particular provider, so it often won’t make sense to transfer take-up risk to private parties
- **Innovation:** some degree of risk may help encourage innovation in public services, but too much has the opposite effect!