Briefing 07/02

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TO: All Chief Executives, Main Contacts and Email Contacts (England)

CC: All Chief Executives, Main Contacts (Wales, Scotland and Northern Ireland)

Briefing on the DCLG Report - *Developing the local government services market to support a long term strategy for local government*

Key issues:

- **The report aims to help bring "much needed and deserved attention to the place of markets in the delivery of both local and central government objectives**
- **The report identifies 12 key points to develop the services market**
- ***There must be a greater understanding that simply turning to alternative suppliers will not necessarily achieve more efficient and effective services, nor will it achieve real transformation of services on its own***

1. Introduction

In addition to the recent Local Government white paper, Strong and prosperous communities, the Department of Communities and Local Government (DCLG) has also published a report, "Developing the local government services market to support a long term strategy for local government". They indicate that understanding and improving the effectiveness of supply markets is critical if local government is to achieve its strategic objectives. The report considers the key challenges and opportunities facing major local government service markets and identifies thematic issues that influence effective competition across the sector. The view from the DCLG is that this report fits well with the aims of the white paper.

This study analysed eight key local government market sectors: asset management and construction services; leisure services; public library services; neighbourhood and streetscene services; regulatory services; technology and transformation services; transport services; and waste management services. A number of these (for example Waste) are also being researched by the Lyons Inquiry into Local Government. Each of these will be the subject of a forthcoming working paper. The report has been produced by Price Waterhouse Coopers (PWC) for the DCLG and can be downloaded from http://www.communities.gov.uk/index.asp?id=1504332

2. The aims of the report and the local government market

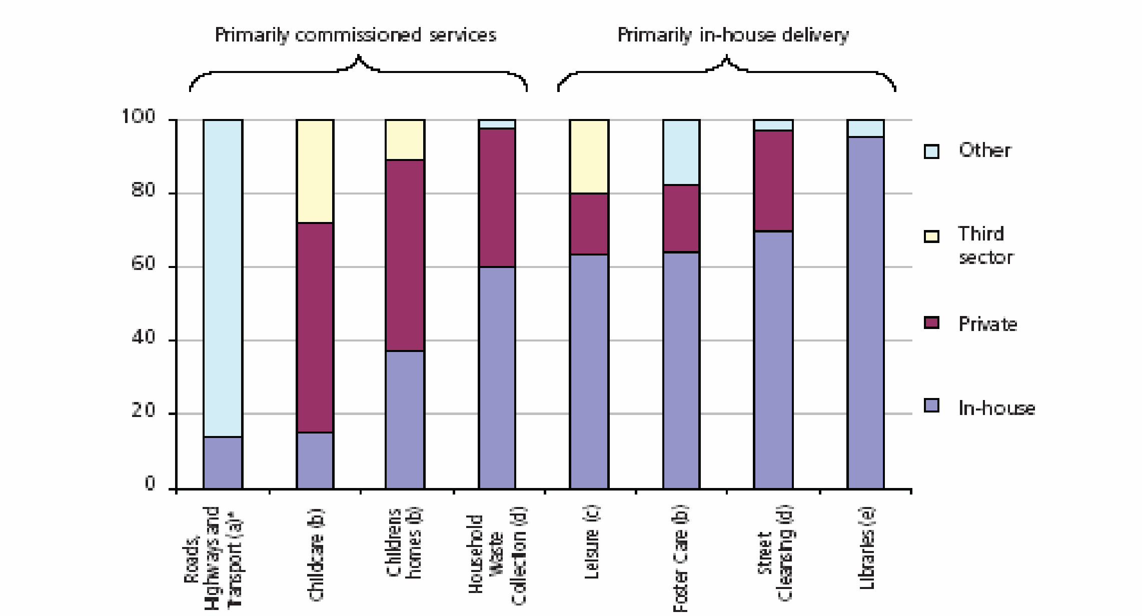
The report begins by expressing surprise that local government spends around half of its revenue with suppliers (including goods, services and third party payments), which equates to £55 billion of spend on an England-wide basis. Its aim is to help bring "much needed and deserved attention to the place of markets in the delivery of both local and central government objectives" and how greater public value can be captured.

The report identifies a number of dynamics of the markets including:

- ✓ Suppliers and markets are significantly influenced by policy and strategy – both positively and negatively
- ✓ The patterns of supply and demand are highly changeable and differentiated by sector
- ✓ Levels of competition in the supply of sector services vary enormously
- ✓ Competition, and in turn supply chain effectiveness, is a highly contingent factor in the achievement of policy changes and associated national/local objectives
- ✓ The buying power of local government is not leveraged effectively. This is particularly the view from the supply side as identified in the round table discussions
- ✓ The level of attention given to markets in policy development is neither sufficient nor appropriately focused

The report identifies a number of differences between the demand and supply side structures and suggests that this is "to some degree" an opportunity for change. The demand side is structured in two main ways, by function (environment or housing with subsets to the interface such as refuse collection) or by a cross cutting agenda based more on the user needs (children's services). The report claims that the structure of supply does not closely reflect that of demand. Whilst it does not advocate that demand structures should change to meet this it does indicate that procurers should recognise this.

The chart below shows the levels of market share for a range of service areas



These are derived from a number of different sources and relate to periods from 2004 onwards. The large 'other' category for highways and transport is because of the reporting method of non-staff expenditure.

3. Using competition and contestability to deliver greater value

The report considered a range of academic, government and other literature sources to identify a number of evidence-based messages that were considered relevant to the local government supply market. These included:

- ✓ There is a strong theoretical basis and evidence from practice to suggest that effective supply markets lever pressure to improve performance in both in-house delivery of services and external suppliers;
- ✓ Achieving the benefits of competition is highly contingent upon a number of conditions, including high quality commissioning, the development of market capacity (market-creating and shaping) and the orientation of supply towards user choice (for example by instituting choice-based contracting);
- ✓ There are both opportunities and drawbacks to increasing the intensity of competition at different times and in different scenarios. Although greater competition is largely a positive trend in most supplier markets, tactical decisions (such as the involvement of too many suppliers in a competition) can lead to perverse consequences such as high procurement costs, tacit market collusion and bid fatigue from SMEs;
- ✓ Contract aggregation (for example by procuring shared services across local authority boundaries) presents both benefits and also some risks. Management of these risks (such as incumbency advantage, or exclusion of SMEs) may be the difference between a successful long-term aggregation and one which might deliver quick wins – but also longer term problems;
- ✓ Self supply, whilst a credible position in some circumstances, has the major impact of limiting competition, especially when potential suppliers feel some element of bias may be a factor in deciding whether to appoint an in-house team. The report "strongly suggests" competitive neutrality should be a major consideration in procuring goods and services.

In terms of effective competition five main drivers are identified that need to be in place for the goal of better outcomes to be achieved. The absence of any one of the drivers could inhibit the achievement of desired outcomes. These drivers are:

1. Strategic market management
2. Effective commissioning and procurement arrangements
3. Low entry and exit barriers
4. Competitive neutrality
5. Cultural and political issues

4. A new approach to effective commissioning

The report identifies that "operational" commissioning (at a service level) and "*strategic"* commissioning offer the major opportunity for change and improvement. The critical factors in developing strategic commissioning are claimed to be:

- ✓ Building people capacity to lead and manage strategic commissioning;
- ✓ Using a 'whole system' approach to thinking about the relationship between outcomes and services/products;
- ✓ Working across local public service institutions;
- ✓ A willingness to think differently about delivery options.

The report outlines a number of examples to illustrate the possibilities of a wider role for local government as a strategic commissioner in the future and is intended to "reflect discussions about such opportunities at the sector roundtables". The DCLG believe this approach "would be highly congruent with both the future role of local government to be 'place shapers' and community leaders, and the development of Local Strategic Partnerships (LSPs), Sustainable Communities Strategies and Local Area Agreements (LAAs)".

The evidence from roundtable discussions with commissioners, suppliers and policy makers, during compilation of the report (PWC claim over 300 were involved) suggest that whilst purchasers and the supply community welcomed experimentation and flexibility with new strategic commissioning arrangements, they were sceptical a 'volunteer' approach would create the step-change needed.

The report identifies that the differing aims of neighbourhood devolution and the efficiency agendas can cause problems for service deliverers. However, it also identifies that in some circumstances both agendas can work well together. An example is given of 'unbundling services' and identifying which require more tailored delivery, and which are more suited to a high degree of standardisation and have a relatively 'generic' demand profile. It also recommends the taking of a longer term view of the need to realise efficiency gains in terms of investing-to-save and higher value outputs such as liveability or healthier communities. The report also claims that the evidence found that "economies of scale are often assumed and on the other hand, local differences sometimes have little material impact".

The report goes on to identify that in driving effective competition a number of general themes should be followed, which are differentiated by market when necessary. The following sets out the key drivers identified for increased competition in various sectors and the potential wider role of local authorities in strategic commissioning.

Waste management – local government could take on a broader role as recognised by DEFRA's waste strategy consultation paper. For example this could be for dealing with other than municipal waste or through establishing trading arrangements with other public bodies (such as NHS), or providing more support in the commercial sector (particularly for SMEs) and in pooling existing and new treatment and disposal facilities with other waste streams. Here working with others could improve the operational efficiency of the service by exploiting scale economies across different waste streams. Increased competition and capacity could be achieved by attracting new domestic and overseas suppliers into the UK market and by local government taking on a more strategic role.

Neighbourhood & streetscene services – provision of a more coherent approach and development of "fence-to-fence" solutions directed at liveability outcomes, through a sensible balance between economies of scale in contracting and locally tailored services, and encouraging a more diverse supply base. The report identifies Streetscene services as an area where local authorities and their service providers (invariably in-house) have developed good practice procedures.

Sports and leisure – Local government taking on a more strategic role and therefore exploiting the full capacity of the wider leisure market by focusing upon capacity planning and facilitation and focusing resources on the needs of, and increasing access for, target groups – for example, within the context of the healthier communities' agenda. Both the Carter Review and Game Plan suggest the need to focus on boosting participation and health outcomes through new models of commissioning and delivery from a more diverse supply base, for example based upon developing mixed use facilities providing community, education, health, and leisure services.

Asset management & construction – local authorities, as community leaders, take on a more strategic planning role in mapping the demand, rationalising and making better use of local public assets and potentially assisting central government in its relocation objectives. Local authorities might in future become the 'hub' front-office for networks of public services across localities.

Corporate services & IT – Development of shared services by local government could be expanded in future, potentially through trading arrangements with other public sector organisations, to support central government relocation and pan-public sector efficiency goals. These should bring about a sensible balance between efficiency and service transformation outcomes.

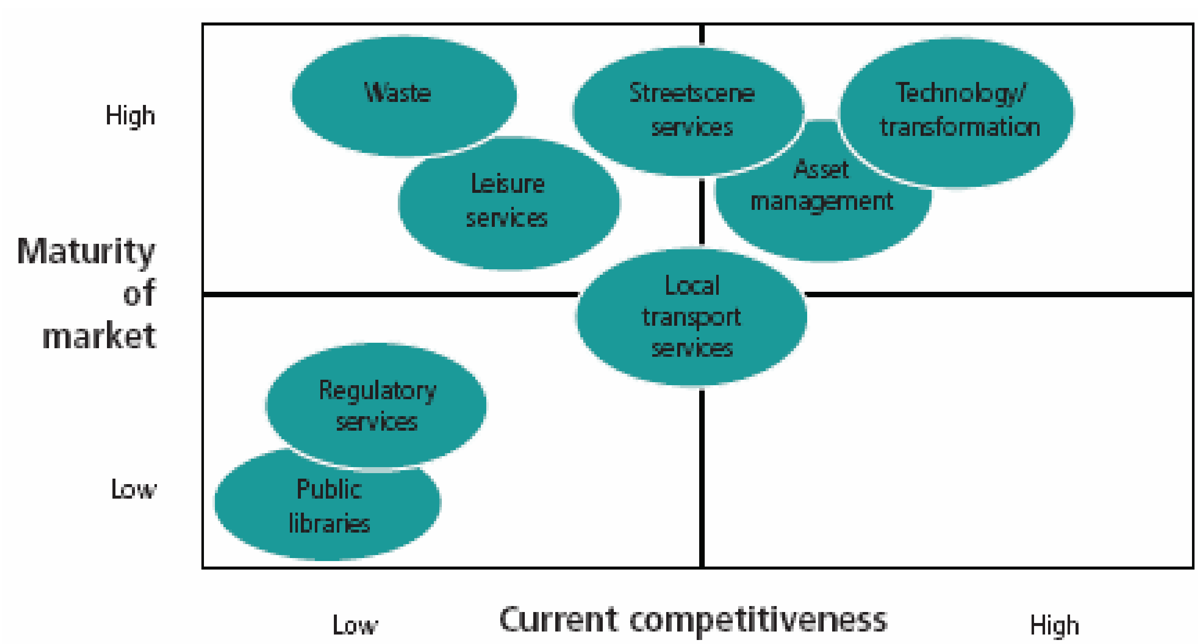
Regulatory services – opportunity to challenge the current pattern of service delivery through the introduction of greater contestability and deregulation to allow the growth of alternative supply and greater choice.

5. Driving improvement in competition

The study is clear that there are substantial variations in the level of competition across the market sectors that fall within the following characterisations:

- ✓ Mature markets with relatively weak competition and restricted capacity, which need to tackle stagnation and reducing entry and exit barriers to bring in new players (for example waste management).
- ✓ Markets that are not currently offering optimum solutions for the local government setting, which need to challenge current solutions and incentivise (e.g. asset management).
- ✓ Services that have had little or no exposure to alternative sources of supply to date, and therefore more limited external challenge to performance than other sectors where design and concept-testing of new delivery models will be required (e.g. regulatory services and public libraries).

The following graph illustrates the points raised in the above bullets by service area:



The argument is also made that buying power is not leveraged consistently and purposively to be effective in stimulating and managing the market as a whole.

6. The view of market of commissioning within local government

The roundtables held with suppliers brought forward a number of criticisms (described as less than good practice) of the current commissioning arrangements which led to the view that the public sector does not leverage its buying power well. These include:

- ✓ A perceived lack of leadership for commissioning and procurement
- ✓ A lack of connection between commissioning, and procurement in particular, and the strategic objectives of local authorities
- ✓ A lack of rigour in working through user needs to supplier engagement
- ✓ Uneven progress towards clear, output-based specifications related to outcomes
- ✓ Entry barriers in the form of high bid costs and overlong process
- ✓ A lack of standardisation in contracting
- ✓ (Some) weak contract management skills

The private sector view is that they have built up a level of expertise that does not exist in local government.

7. Market development and shaping

Market development and shaping takes commissioners beyond the procurement of contracted services to an active dialogue with the marketplace. This is described as "absolutely central to strategic commissioning". Three main elements are identified:

- ✓ *Market intelligence* which refers to the accessibility at local, regional and national level of market data covering areas such as market activity, current and potential suppliers, and future opportunities, to inform strategic planning on both the supply and demand sides. The study found that the quality of market intelligence available to commissioners is mixed at best and further, commissioners are not always considering the cumulative impact of buying decisions on the structure of the market and the leverage they can command;
- ✓ *Market dialogue* which refers specifically to the quality and frequency of interactions between stakeholders on the supply and demand sides;
- ✓ *Market shaping* which refers to collaborative action by public sector organisations and the supply market as a whole to develop markets in ways that support the delivery of key policy objectives at both local and national level.

The report stresses the importance of market intelligence by stating that "the long term competitiveness of key sectors is at stake unless the issue of market intelligence is addressed". It highlights that:

- ✓ Better information for suppliers about future trends in demand to enable capacity planning and investment decisions;
- ✓ A more structured, regular and accessible flow of information for commissioners about the quantity and quality of suppliers in key sectors;
- ✓ A more active approach to developing and shaping the market.

8. Conclusions from the report

Based upon the research and stakeholder discussions undertaken in preparing this report, the DCLG and PWC have drawn together 12 key conclusions, which are set out below:

1. Commissioning and procurement should be elevated in importance so that they incorporate a strategic perspective to advance local government's wider role in 'place shaping'.
2. A clear and comprehensive commissioning framework for local government needs to be established, which provides a central focal point for those involved in the development of policy, the commissioning of activities and the procurement and provision of services.

3. Greater investment should be made in the development of commissioning skills and capacity in local government.
4. 'Received wisdom' about the delivery of core services must be challenged.
5. Performance, efficiency and value-for-money can be improved through a diverse and competitive supply community.
6. The supply side of the mixed economy – the public, private and third sectors – must recognise its role in stimulating effective competition and supporting capacity planning,
7. Public service suppliers and those who represent them should engage pragmatically in the future development of the local government services market,
8. The market environment must be neutral between different classes of provider, and care needs to be taken to ensure that artificial entry barriers to local government markets do not discourage new providers.
9. A balance must be sought between aggregation and localism in commissioning services,
10. Central and local government need to take an active approach to developing and shaping the local government services market
11. There should be encouragement of a more strategic dialogue between policy, commissioning and supply communities.
12. There should an investment in an on-going forensic review of local government markets so that actions are taken based upon evidence.

The report concludes by identifying three issues that need to be addressed by the different stakeholder groups if the findings are to be taken forward.

1. ***Policy makers*** will need to be prepared to take a leadership role and to recognise that there is a need and responsibility for the public sector to actively engage in the development and management of the supply markets.
2. ***Commissioning capacity*** will need to be enhanced with models developed, that focus on sound business principles. The procurement and commissioning function will need to be seen at the heart of local government's approach to service delivery and improvement.
3. ***Suppliers*** will need to recognise that the importance of diversity of supply and the need for honest and active engagement in order to develop the viability of market areas.

The importance the DCLG attach to this issue is perhaps best demonstrated by their final statement that ***"the challenges are significant, but the opportunities presented by a more dynamic market, for local government and ultimately the end-users of the services, make this a key priority in the development of local government's strategic role over the medium and longer term"***.

9. APSE comment

This report needs to be given serious consideration by service deliverers and should be viewed with the same level of importance as the more publicised local government white paper. The DCLG view is that it links well in terms of capacity building and the efficiency requirements of the white paper and also the 3% efficiency savings outlined in the Treasury pre Budget report (December 2006).

The report does contain some useful guidelines that local authorities can use to determine the effectiveness of their services. The best providers are (and should be) continually striving to improve their services. The role of Business Process Re-engineering (BPR) will become increasingly important for providers from all sectors in designing service improvements from commissioning through to delivery. The role of Local Area Agreements (LAAs) and Local Strategic Partnerships (LSPs) will grow in importance, especially in the policing framework. Additionally, a duty of community involvement will become integral when signing up to an LAA/LSP.

However, APSE has a number of concerns with some points. In particular there appears to be an over emphasis on the views of the suppliers which appears to contradict a number of the themes of the white paper in that services must be more responsive to citizen needs and circumstances.

The reports conclusion (point 4) includes a statement that 'Received wisdom' about the delivery of core services must be challenged. This includes a follow on statement that ***"there must be a greater understanding that simply turning to alternative suppliers will not necessarily achieve more efficient and effective services, nor will it achieve real transformation of services on its own".*** APSE welcomes this statement and believes it sends a strong message that outsourcing without carrying out a full assessment of service requirement is not the answer. APSE also agrees all providers should be willing to challenge current patterns of service delivery, drawing on the best of the public, private and third sectors in the drive to secure continuous improvement and efficiency gains. APSE through its network promotes the use of best practice examples to share knowledge especially where service managers and staff are undergoing transformation and require all the help and guidance they can get. A further sub point under conclusion point 4 indicates that the approach to commissioning and procurement needs to encourage innovative solutions to service transformation based around the needs of users and local areas. This appears to ignore the vital role that service deliverers bring to the process.

The APSE Briefing (06-56) on the white paper's Health and Well Being chapter outlined that the public want greater personalisation of services in packages that are coherent, not fragmented and remote. A strong core of directly provided services allows authorities to respond to changes in priorities, both within neighbourhoods and at a national level. One of the other principles underlying the arguments in the white paper for responsive services is that there should be an element of choice and it is not made fully clear within this report how the choice argument would be built into the process.

Conclusion point 5 promotes that performance, efficiency and value-for-money can be improved through a diverse and competitive supply community. A sub point of this envisages that wider development of performance benchmarking data across key services to ensure that in-house or external provision continues to deliver value for money. APSE welcomes the use of benchmarking data but believes this should also incorporate a quality of service factor rather than a value for money judgement only.

In addition to this report, the white paper also states that councils can encourage more providers (particularly the third sector) to enter the market and compete for contracts by improving commissioning and procurement processes. Revised statutory guidance will be issued by DCLG in 2007 which will strengthen the key principles of best value and will cover the commissioning role of councils, community participation and provide that councils should regularly test the competitiveness of their performance in comparison with others.

When services are found to be underperforming (for example high cost and low performing), they should where practicable, be an opportunity for challenge. A code of practice on competition on the core practices expected in all councils and suppliers will also be developed. The APSE view is that whilst a code of practice may be useful in determining when competition becomes necessary it can be viewed as inappropriate. APSE believe if a service is performing well and evidence substantiates this there is no justification for going through a time consuming and resource intensive exercise. At worst, the statutory guidance could be seen as a move back towards CCT.

The report on market development and shaping indicates that local government has a major role to play. APSE believes that local government should concentrate on providing and commissioning services to its public. Using waste management as an example (as local authorities are major commissioners and providers of this service), the report indicates that local government could increase competition and capacity by attracting new suppliers. The evidence from the latest company assessment in the waste industry appear that the number of companies continue to consolidate. The turnover of the leading seven companies, accounts for over two thirds of the sector turnover and this percentage is increasing year on year. Additionally, following a takeover the seven companies will become six (source CIWM November 2006). It is hard to see, in an industry that is becoming increasingly complex, how local government could buck this trend.

The white paper continues to promote the potential benefits of councils and local public bodies delivering more services (both in back office functions and front line services) in collaboration with each other. APSE has strongly promoted the benefits of shared services and how this approach can help support small districts looking to make efficiency gains and improve services.

Chapters 6 & 7 of the report give views from the private sector on commissioning, market development and shaping which are critical of the role of local authorities. Whilst these are given almost two chapters the criticisms of the supply side in failing to engage are given less weight. The issues of risk transfer when commissioning services is not raised as a concern, despite this being a contentious issue when services are being procured. Additionally, the problem of exit from delivery of service is not discussed; this is particularly a problem when the local authority wants to close a school or library but is tied into a long term contract with a supplier. In terms of commissioning a problem affecting the public, private and third sectors is regarding skills. The questions of improving the numbers, age profile and training are major factors that need to be addressed if the upward trend is to continue.

This report highlights the importance attached to the efficiency agenda by the DCLG and it is apparent that the extent of delivering choice will depend on how successful local government is on delivering the required savings. This all needs to be set against a background of increased costs for social care, waste management and in settling equal pay claims. Local authorities are likely to have to make decisions on managing expectations (for example standardising delivery against increasing customer expectations and choice) and to use BPR techniques to shape services effectively.

In determining the market, local authorities need to be in a position where they can make decisions and judgements that will harness the contributions (for example skills and knowledge) of all providers that will benefits and meet the aims of the local authority. This has to be more than a decision to transfer the service.

APSE would welcome feedback and comments on this paper as it will assist with future lobbying meetings APSE is holding with the DCLG. Comments by email to jmarsh@apse.org.uk

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