



ENTERPRISE SOLUTIONS

PUBLIC SERVICE MUTUALS:
SPINNING OUT OR STANDING STILL?

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Introduction

This is the final report of Capital Ambition's Enterprise Solutions project. Led by the London Borough of Lambeth, four London councils have explored how they might establish some of their services as independent social businesses. In particular, Lambeth, Lewisham, Kensington and Chelsea and Richmond have looked at the potential role of employee-led mutuals.

Reports published alongside this document look in detail at the learning to be drawn from their experiences. One report compiles lessons learned in relation to barriers and solutions to mutualisation. Another examines how commissioning might change to support public service mutuals in promoting social value. A toolkit offers practical support for public service leaders considering the complex and highly demanding challenge of 'spinning out' of public ownership.

The role of the current report is to step back, take stock and look forward. Enterprise Solutions began work in 2011, the same year that the Cabinet Office established its Mutuals Taskforce to accelerate the mutualisation that had begun under the previous administration. Championed variously as a way of encouraging innovation among public service professionals, disrupting inefficient public sector bureaucracies and giving service users a stronger role in governance, public service spin-outs appeared to offer a fresh alternative to big-business marketisation on the one hand, and big-state monopolies on the other. How have they fared? In an age of austerity, are mutual ambitions looking realistic and valuable, or fragile and esoteric? Certainly, even their most ardent supporters would concede that their advance has been slower than predicted. As the Chair of the Mutuals Taskforce recently conceded, 'a complete mutuals revolution is not yet upon us'.¹

In section one, Allison Ogden-Newton, Chair of the Transition Institute, looks at the evolving policy environment within which public service mutuals have been conceived, reconsidered and encouraged. She finds strong continuities between the last Labour government and the Coalition. Though she identifies ongoing concerns about successive governments' failure to ensure access to capital for the new organisations, a maturing business support sector for mutuals gives her grounds to believe that steady growth is nevertheless possible.

In section two, Kelly Hall and Richard Hazenberg from the University of Northampton look at how the evidence base around public service mutuals has evolved, particularly since the Coalition came to power. They find some evidence for greater creativity and commitment in mutualised services, but also find that the skills required for successful business planning may not be found in-house.

The conclusion suggests that, just as the Enterprise Solutions project has itself seen a range of solutions, including but not limited to mutualisation, so the future of spin-outs is likely to take a number of different

1. Le Grand (2013)

forms. Employee-led mutuals may grow, but so too will collaborative models, joint ventures, asset transfers and in-house trading companies.

Paul Buddery

RSA 2020 Public Services

1. The evolution of public service mutuals

Introduction

The architecture of public services in the UK is in transition. Across the NHS, local authorities, schools and libraries, our public institutions are being remodelled.

These changes, the result of three decades of numerous, far-reaching reform, have resulted in less direct provision of public services by local authorities. This shift has been driven top-down by successive governments and bottom-up by commissioning bodies, innovative employees and charities with the aim of creating more cost-efficient services that are also more responsive to service users' needs.

In particular, both governments and commissioners have looked to mutuals, often cross-referenced as co-operative and social enterprises, as a potential new model for service provision. Public service mutuals or 'spin-outs' have been defined as '... organisations which have left the public sector ie spun out, but continue to deliver public services and in which employee control plays a significant role in their operation.'²

Mutuals have been idealised as lean, cost-effective and benefiting from a more dynamic social contract with the communities they serve. Successive governments have championed what they see as the innate benefits of new providers that originate from the public sector. However, they have been less clear about how to support the emergence of these new models, or if they will be cost-effective.

At the same time, recent waves of public sector outsourcing driven by ongoing cuts to departments and local government budgets – including the wholesale purchasing of children's residential homes by private equity firms – are increasing the debate around how to balance cost savings and social impact and access to capital for mutuals. In the context of reductions in public spending, the risk is that the sole consideration becomes cost saving, and the potential of staff-led mutuals to create better outcomes is lost.

In this chapter, we look at how policy around public service mutuals has evolved over recent years, with a particular emphasis on the approach taken since the Coalition government came into power in 2010. We also explore the key changes since the establishment of the first public sector spin-outs, what might be in store for new providers and what might assist agencies challenged with making the greatest infrastructure changes to the state since 1945.

2. Cabinet Office (2012)

1. Mutualisation and public sector reform pre-2010

The history of mutualism could be said to begin with the guilds of medieval Britain. However, for the purposes of this paper, the most helpful starting point to the story of mutual-led public sector service providers is in another period of austerity: the early 1990s.

In 1993, leisure centre manager GLL spun out of Greenwich Council. GLL has since flourished and now employs over 6,000 people and runs over 100 leisure facilities across London. There was no overarching national policy framework for these early spin-outs or another leading social enterprise community, the Hackney Community Transport (HCT). Both developments occurred at a time when local authorities were making cuts in spending.

Within the stark choices of either privatisation or closure that became prevalent within local government in the early 1990s, trailblazing, mutually led enterprises showed that innovation was possible. Working together with a growing number of ethical manufacturers and co-operative agencies, this first wave of spin-outs created what we now refer to as the social enterprise movement. Their success showed that there was an alternative to the binary public/private sector choice model previously contemplated.

The election of the New Labour government in 1997 brought with it a renewed enthusiasm for mixed models of public service delivery, this time with an emphasis on social impact. Appointed to Tony Blair's cabinet as Secretary of State for Trade and Industry in 2001, Patricia Hewitt established the first Social Enterprise Unit (SEnU), which signalled a breakthrough for employee-led public services. The unit marked a step change in government policy in adopting principles of social enterprise, co-operation and mutualism and applying them to public sector reform. In 2005, Hewitt became Secretary of State for Health, and one of the leading exponents of mutualised service delivery.

The Labour government wanted to change the way in which healthcare was delivered in England. The initial driver of its strategy came from the 2005 Department of Health papers *Creating a Patient-led NHS: Delivering the NHS improvement plan*³ and *Commissioning a Patient-led NHS*.⁴ The subsequent 2006 white paper, *Our Health, our Care, our Say: A new direction for community services*⁵ outlined the potential for spin-out organisations to deliver healthcare services. This included the provision of more integrated public services by a variety of organisations, including social enterprises and employee-led mutuals. At the time Hewitt said:

‘The social enterprises that are now growing in many other sectors of the economy offer another model of public organisation that is starting to spread, particularly within community health and social care ... I want to see more NHS social enterprises and in the new year, I will be announcing how in health and social care, we can build upon the work of the social enterprise unit that I created at the Department of Trade and Industry.’

3. Department of Health (2005a)

4. Department of Health (2005b)

5. Department of Health (2005c)

From the Conservative government of 1979 to the Coalition government of 2010, more attention has been steadily given to the potential role that social enterprises and mutuals can play in redrawing state-sponsored services

That announcement turned out to be the establishment of the Department of Health's Social Enterprise Pathfinder Programme, which supported and encouraged the development of new social enterprises to deliver health services.⁶

Hewitt also highlighted one of the most celebrated health sector spin-outs of that time – Central Surrey Health – which, while it remains on track as a growing community healthcare provider, has encountered difficulties with public sector commissioning designed to encourage contractors with access to capital rather than social value, in this case community nursing expertise.

In 2008, Labour's strategy manifested itself in the Right to Request Programme, an initiative introduced in Lord Darzi's *High Quality Care for All: NHS next stage final review*⁷, which set out a 10-year vision for the development of the NHS. The Right to Request Programme gave primary care trust (PCT) staff the opportunity to innovate and develop their own organisations to deliver healthcare services. PCTs were obliged to consider and support spin-out requests subject to board approval of the business case. These services would then be contracted out from the NHS with a maximum three-year contract and delivered by the spun-out organisation, remaining free at point of use for the public. These PCT spin-outs formed the first wave of public sector mutuals supported by government policy. At least 38 new social enterprise spin-outs were created, with a total of at least 22,000 NHS staff working within them,⁸ before the scheme was closed in March 2011 and replaced by the Right to Provide Programme introduced by the Coalition government.

From the Conservative government of 1979 to the Coalition government of 2010, more attention has been steadily given to the potential role that social enterprises and mutuals can play in redrawing state-sponsored services. This debate peaked at a time when the government elected in 2010 seemed to place the role of community responsibility at the heart of its philosophy and as it committed itself to an austerity budget that would bring about dramatic change.

2. Mutualisation and public sector reform post-2010

The Coalition government quickly supported the promotion of employee-led public sector spin-outs through the unequivocal commitment to mutualism shown by the Minister for the Cabinet Office, Francis Maude, in 2010. Maude outlined his vision, as part of the more widely known concept of the 'big society':

'It used to be thought that there was a simple binary choice in how public services were delivered. On the one hand, they could be delivered by the state; by staff employed directly by a public sector agency. On the other, they could be privatised. Outsourced. Delivered for profit by commercial suppliers ... There's another model now. One that can transform the way services are delivered. That can release entrepreneurial vigour into the economy. And that can transform the lives not only of the citizens that use

6. Department of Health (2005d)

7. Department of Health (2008)

8. Miller et al (2012)

the services but of the staff who provide them by forming themselves into a mutual, a co-op, spinning themselves out of the public sector, and taking control of their lives and of the services they provide.’⁹

This commitment was backed by the creation of the Mutuals Information Service operating through the Cabinet Office and supported by the Mutual Support Programme to support public sector workers interested in establishing mutuals. In early 2011 Maude said it was conceivable that over a million state workers – a sixth of all public employees – could transfer to mutually run delivery agencies.¹⁰ This was a startling statement that led local authorities in particular to look at bold new initiatives in the face of swingeing cuts. Those initiatives were diverse but all based around the idea that public sector employees could become their own employers.

The financial crash of 2008 ushered in an era of austerity unprecedented in post-war Britain. Although local authorities anticipated cuts, the scale and speed of the subsequent reductions in their funding took many by surprise and it was not until 2010 that the real strategic debate began as local authorities anticipated a 30 percent reduction in their spending by 2015. Faced with this scale of reduction in income, simply ‘salami slicing’ budgets would not create the savings needed.

Services such as libraries, home care, information, advice and guidance have been dramatically reshaped in some areas with lines redrawn around what are considered ‘essential’ services. For those services that remain, cuts were introduced and new approaches quickly considered. Some authorities announced plans to outsource services. For example, Barnet Council in north London adopted One Barnet, a model, based loosely along the lines of budget airlines, where additional services would be charged at the point of use.

This approach appeared to contrast with that taken by councils such as Lambeth, which set up its Cooperative Council Commission to explore the idea of co-operative led services, reiterating ‘big society’ language around enhanced community engagement. As Council Leader, Steve Reed, told the BBC in 2010:

‘The idea is that some things can be managed by the community. For example, imagine you have a piece of waste ground, which you want to tidy up. Instead of the council doing it, you give the community the tools and neighbours do it themselves.’¹¹

Neither model initially placed a heavy emphasis on mutualisation or spin-outs, although both considered them as an option in later strategies.

Meanwhile, from 2010, the Right to Provide Programme allowed for a greater scope of public sector spin-outs to emerge beyond PCTs, to staff working in NHS trusts, mental health trusts, local authority social services and special health authorities. The 2011 Department of Health guide *Making Quality Your Business: A guide to the right to provide*¹² outlined the government’s strategy and was followed in 2012 by £10

9. Maude (2010)

10. Ainsworth (2011)

11. Davey (2010)

12. Department of Health (2011)

million to support the creation of frontline mutual services or social enterprises.

Stepping up a gear, the Community Right to Challenge was included in the Localism Act of 2011.¹³ This requires local authorities to consider an expression of interest submitted by a voluntary or community body, charity, parish council or employees of the authority in relation to providing (or assisting in providing) a public service.

In this way a potentially more mixed market has been encouraged, although reports from the voluntary and social enterprise sector show that progress in the form of increased public sector contracts has been slow. These assertions have been backed by Social Enterprise UK's recent report *The Shadow State*, which says that:

‘While social enterprises are growing and gaining confidence in consumer markets and when trading with businesses, our research shows that those who are working in public service markets are drastically low in confidence. Many are making redundancies and turning away from public service markets in order to survive, just when they are needed most. They cite public sector procurement policy as one of their biggest barriers to sustainability. They often lack the scale, balance sheets or ability to ruthlessly cut costs in order to win out in the current climate.’¹⁴

The Coalition government has expressed its commitment to move to a system that focuses on the price and value of a provider, rather than the costs. In September 2011, the Department for Communities and Local Government published new best value statutory guidance that states that: ‘Authorities should consider overall value, including economic, environmental and social value, when reviewing service provision.’¹⁵ In doing so they have a duty to consult representatives of a wide range of local stakeholders, including council tax payers, service users and those who ‘appear to have an interest in any area within which the authority carries out its functions as well as local small businesses, voluntary and community organisations.’¹⁶

The *Open Public Services* white paper published in July 2011 provides some further definition to the notion of social value within the public sector.¹⁷ It presents a framework for reforming public services that emphasises innovation and community engagement. While not a radical reinvention of public services, it focuses on the importance of social value in new public service contracts during the pre-procurement stage. This approach was enacted as the Public Services (Social Value) Act 2012.

While there is no one agreed definition of social value, NHS North West defined it as relating to the ‘additional benefit to the community [non-financial] from a procurement process over and above the purchasing of goods, services and outcomes’.¹⁸

13. For the full text of the Act, see www.legislation.gov.uk/ukpga/2011/20/contents/enacted

14. Williams (2013)

15. DCLG (2013)

16. DCLG (2013)

17. For the full text of the white paper, see www.openpublicservices.cabinetoffice.gov.uk

18. NAVCA (2013)

Other social and environmental pressures, such as higher rates of unemployment and an ageing population are eating into national budgets

Once more, the European Commission, often a source of anxiety for local authority commissioners, has supported the premise of social value in public services. As stated in the 2011 green paper on modernising EU procurement: ‘Public authorities can make an important contribution to the Europe 2020 strategic goals by using their purchasing power to procure goods and services with higher societal value in terms of fostering innovation.’¹⁹

In a draft resolution responding to the green paper, the European Parliament clarified that the lowest price criterion should no longer be the determining factor in awarding public contracts. Instead, it suggests that contracts should be awarded to the ‘most advantageous tender in terms of economic, social and environmental benefits, taking into account the entire life-cycle costs of the goods, service or work’. This established an open door for commissioners looking for long-term sustainability, social impact as well as value for money.

3. Mutuals and social value

At present local authority councillors are preparing to implement a fourth spending reduction programme and are drawing up plans for more cuts next year. Even those core services that have so far largely escaped substantial cuts – such as care of older people and child protection – are now starting to feel the effects as they face the next round of public sector cuts. Many local authorities have tightened eligibility criteria for some services, and are introducing or increasing charges for others.

In this context, policies that support employees to establish a mutual service delivery agent could be seen to conflict with austerity measures. Other social and environmental pressures, such as higher rates of unemployment and an ageing population are eating into national budgets. For many local authorities, these pressures have created a ‘perfect storm’ and a belief that only economies of scale can achieve the scale of cost reductions needed.

Evidence is now emerging that challenges this idea and instead takes us back to the principle of the strength of a mixed market. Social Enterprise UK’s report states:

‘The pressure for contracts to become larger is due to the conception – often, as we shall see, a misconception – that scaling a process up will always represent a saving. It takes less time to manage; it theoretically has fewer transaction costs; there may be shared infrastructure. But often, the larger a contract becomes, the greater the asymmetry in expertise between the commissioner (that is, the government’s representative) and the supplier. And as many of the services being delivered under these contracts ultimately depend on human relationships, it is difficult to see how much value can be created or real saving made through scaling ever upward. In fact, interest in diseconomies of scale is growing in the social sector.’²⁰

Outsourcing that is driven exclusively by the need to achieve cost reduction with no emphasis placed on social return or value, has shown

19. European Commission (2011)

20. Social Enterprise UK (2012)

us how efficiently the private sector can offer low-cost options that turn out to be expensive as they systematically fail to deliver social impact. Examples of this include: children’s residential care contracts costing the state around £200,000 per child per year in homes now largely owned by equity companies; and the work programme where four companies dominate the list of prime contractors and to date have assisted less than 4 percent of those seen into jobs, while costing the state many millions. These kinds of examples, coupled with austerity, are driving change, with mutualism and social value providing a potential blueprint for progress.

The Transition Institute studies the role of social value in public service created through a mixed market of providers. Its research shows what can be achieved when the priority of cost-effective services are shared with the needs of those who rely on those services. The Institute has begun the process of mapping new mutuals and promotes the work of co-operative schools, staff-led community interest youth services and mutual delivery of community care. In defining social value, the institute states:

‘Primarily we mean value in a purely economic sense when we talk about social value: that is, the economic utility that is created as a result of a set of actions and the outcomes of these actions. Value also refers to principles or standards of behaviour and organisations with a social value ethos recognise that their embedded purpose is the cornerstone upon which the rest of the organisation is based.’

4. Success factors for spin-out mutuals

While the number of mutual organisations falls dramatically short of government projections, which need to be revised in the context of extensive public sector job losses – an estimated 350,000 in local authorities alone – employee-led public sector organisations have continued to emerge. Early findings from the Transition Institute’s 2013 survey of the spin-out sector – social enterprises and charities adopting mutual models – indicate that those that have achieved independence are experiencing growth. While further analysis is needed, this suggests that independent service providers will have a growing role to play in the future of public services.

For many this may seem like a new agenda, but in reality mutual delivery agents within the public sector are a maturing section of the market. The institute’s research outlines the increased social impact of growing numbers of public sector mutuals such as NAViGO (North East Lincolnshire’s mental health services) and Empowering People in Communities (EPIC) Community Interest Company (CIC) (formerly Kensington and Chelsea Youth Development Service).

These providers brought together service users with staff to create a business model that could be supported by the ‘parent authority’ at the initial stages of contract negotiation. Their experience, like those of GLL and HCT before them, will depend on the creation of a supportive environment, the nature of the marketplace in which they operate and their ability to grow.

Strong leadership in the context of a supportive environment remains the dominant factor in the establishment of effective spin-outs. Parent authorities that have encouraged leadership and supported the

development of business strategies have played an important role where success has been achieved. As Siobhan Clarke, Managing Director of Your Healthcare CIC, a not-for-profit social enterprise established in 2010 (and formerly within Kingston Healthcare), told the Transition Institute:

‘You definitely need to have strong leadership, a lot of commitment and resolve. However, I don’t think it necessarily has to be a top-down approach. You need to really believe in it, and actually the reason you keep going is because you do believe it. If you believe in the idea, and you explain it to the staff and they see that it is best for the organisation then everyone has input.’

Parent authorities can sometimes struggle to take a more negotiated stance in relation to setting budgets with potential staff-led services. However, those that get the balance right between removing enough obstacles to ‘allow’ mutualisation, and are able to know when to let go of their authority, are rewarded by radical new social-value led service providers. James Miller of Living Well, the HIV and youth support organisation based in Hammersmith, told the institute: ‘In all honesty, the actual separation was surprisingly harmonious and for the most part we were well-supported throughout the journey.’

The initial contract between parent authority and spin-out is perhaps the critical key to success. This contract acts like the dowry of the new organisation: it sets its value and provides the basis for negotiation with subsequent lenders. A contract should support the service, allow for enhanced innovation and be long enough to give the fledgling service time to hone its business model before it has to compete openly.

The strongest benchmark for success comes from the prevailing models of the staff-led mutuals set up in the 1990s. Here we see quick expansion, the ability to borrow capital and invest in assets and the continued strength of their mutual values as the key factors for success. At least one of those criteria jumps out as a serious challenge for a new mutual: access to capital. A great deal depends on the solid and durable nature of their initial contract and the existence of any capital assets against which they might be able to borrow from the open market of suitable social finance intermediaries.

Large specialised social lenders such as Big Society Capital have indicated a willingness to lend to intermediaries interested in working with the new mutualised services. In a statement in early 2013, Big Society Capital Chief Executive, Nick O’Donohoe, said the government’s decision to increase the number of payment-by-results contracts, including an announcement that charities would be able to bid to provide probation services, would require the sector to have the support of social lenders and would be a test of the capacity of the social finance sector. In particular, he stated that ‘... as a result of our establishment, frontline social organisations will begin to notice a real difference in their ability to access capital.’²¹

However, the existence of capital in the outsourcing of public services is very much a ‘chicken and egg’ debate. Where commissioning

21. Ainsworth (2013)

authorities allow newly formed services to establish themselves with a long, healthy contract and even transfer capital assets such as a building formerly owned by the authority, then those new providers stand a much better chance of being able to borrow the necessary capital to achieve further efficiencies.

In the absence of such assets, borrowing becomes almost impossible and the establishment of a sustainable business model that can meet the challenges of competition, unachievable. To bring the added benefit of potentially larger pots of capital from social lenders like Social Investment Business or Big Issue Invest into the equation, parent authorities must ensure assets exist in the first instance.

For some public sector leaders, mutualisation may appear to be a radical step. However, the mutual sector has reached a stage of maturity. This is marked by the development of its associations such as E3M (a new initiative by Social Business International), research bodies like RSA 2020 Public Services and the Transition Institute, and support networks led by the Mutual Support Programme. The world of mutuals is not just a growing and fascinating one: it also has the potential to boost the social value of our public services.

Allison Ogden-Newton

2. Mutuals: An evidential review

Introduction

As discussed by Allison Ogden-Newton in chapter 1, far-reaching reforms over the last three decades have resulted in an increased ‘marketisation’ of the public sector.²²

This chapter will examine the policy motivations for spin-outs, particularly since the Coalition government came to power in 2010. It also looks at the legal implications of spinning out, with a particular focus on the legal forms that these organisations can take. The chapter explores staff motivations for and attitudes towards spinning out, as well as the risks associated with it. Finally, there will be a discussion of the early evidence pertaining to the outcomes of spin-outs, notably those that impact on service users.

1. Policy motivations for spin-outs

As discussed in chapter 1, there has been significant policy support for the establishment of public sector mutuals and social enterprises in recent years. The Coalition government is investing in public service mutuals through the £10 million Mutual Support Programme, a comprehensive package of advice and support for potential mutuals, including a web portal and helpline – the ‘Mutuals Information Service’ (MIS) – designed to provide a diagnostic service to assess the readiness of existing public services for spinning out into a public service mutual.²³ As we have also seen in chapter 1, the Localism Act 2011 provided opportunities for community groups to take over and run their local services, notably within the health and care sectors.

Research into the outcomes associated with such health sector spin-outs is ongoing, but early results from Hall et al suggest that spinning out has presented real opportunities to develop services in innovative ways without the burden of public sector bureaucracy.²⁴ However, the same research found that resource dependency on the state through an ongoing reliance on public sector contracts can restrict the amount of economic and political autonomy held by these organisations.

A number of policies have been developed to increase the demand for services provided by mutuals and social enterprises. This includes reforms to the commissioning of public services, as well as the Public

22. Hall et al (2012), Simmons (2008)

23. Cabinet Office (2012b); PA Consulting Group (2013)

24. Hall et al (2013)

Policy has been driven by a desire on the part of local authorities to see concepts such as happiness, well-being and empowerment considered by public sector authorities when commissioning out services

Services (Social Value) Act 2012, discussed in Chapter 1, which requires commissioners of public services to ‘... consider how the services they commission and procure might improve the economic, social and environmental well-being of the area.’²⁵

Policy has been driven by a desire on the part of local authorities to see concepts such as happiness, well-being and empowerment considered by public sector authorities when commissioning out services and is aligned with current EU procurement initiatives, discussed in further detail below.²⁶ Furthermore, the establishment of the Any Qualified Provider policy by the NHS in 2012 sought to encourage a diversity of providers of health and social care services, thereby enabling patients greater choice over the care and treatment they receive and the organisations that they receive it from (including public, private and third sector providers).²⁷

Such policies do not however prioritise social enterprises or mutuals over other providers, and spin-outs must compete with other public, private and third sector organisations for contracts to deliver services. The only exception to this has been in relation to Right to Request Programme, which guaranteed contracts for health spin-outs for between three to five years. However, no such assurances are given under the scheme’s successor, the current Right to Provide Programme.

The focus on social value and political attempts to move procurement processes away from purely financial considerations, has not only occurred at the UK national level. Policy developments within the EU have focused on establishing public procurement processes that are more favourable to social enterprises, public service mutuals and other third sector organisations. Indeed, EU procurement laws, while often regarded as being the reason behind inflexible procurement processes, actually encourage the assessment of ‘social value’.²⁸ A resolution in the European Parliament stated that price should no longer be the main consideration in awarding public service contracts, but that economic, social and environmental factors should also be considered.²⁹ Furthermore, the EU Internal Market and Consumer Protection Committee recommended to the European Commission that they should ‘... reassess the appropriate level of thresholds for supply and service contracts, so as to facilitate access to public procurement by amongst others not-for-profit and social economy operators as well as SMEs, and if necessary raise them.’³⁰

2. The legal implications for spin-outs

The majority of spin-outs establish themselves as social enterprises, the broad definition of which is ‘... business[es] with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners.’³¹ The social enterprise model was seen to give organisations greater flexibility to expand into

25. SEUK (2012)

26. NAVCA (2013)

27. Department of Health (2011b)

28. BWB (2013)

29. The Information Daily (2013)

30. EU-IMC (2011)

31. DTI (2002)

new areas, develop new products and rationalise service delivery.³² The social enterprise model can however encompass a range of organisational forms with different legal structures, and this has led to confusion among policymakers and commissioners as to what a social enterprise should really look like.

Efforts were made to rectify this through the introduction of the Community Interest Company (CIC) in 2004, which offered a specific legal organisational form for social enterprises. Many spin-outs have taken this legal form, especially in the health sector, with approximately 92 percent of Right to Request organisations being established as CICs.³³ The CIC allows a public service mutual to build trust with staff, users and funders through the provision of an ‘asset-lock’, as well as the ‘community interest test’ that requires CICs to only use funds/assets for community benefit.³⁴

However, operating as a CIC is not crucial to ‘spinning-out’ and many other legal forms can and have been adopted, including:

- Companies Limited by Guarantee (CLG)
- Mutuels
- Industrial Provident Societies (IPS)
- Cooperatives
- Companies with Charitable Status (CCS)³⁵

While the health sector has seen the majority of spin-outs adopt CIC legal forms, mutual and industrial provident societies legal forms also offer potential for spin-outs due to their focus on staff/community ownership and community benefit.³⁶ Members have equal voting rights irrespective of shareholding size and benefit from limited liability.³⁷ This provides members the flexibility to pursue policies through democratic decision-making processes that for a spin-out could include service staff and users alike.

Operating as a company limited by guarantee provides a number of benefits, including the relative ease of establishing the legal entity, the transparency offered by the requirement to publish accounts³⁸ and the limited liability that members/owners have.³⁹ However, in relation to spin-outs, such a structure may be problematic as the lack of asset locks could make public bodies and social investors nervous; although recent research has suggested that asset-locks and legal structures are not a ‘deal breaker’ to social investors.⁴⁰ Additionally, the ongoing administrative paperwork required to run as a company limited by guarantee may mean that the structure is too cumbersome for smaller spin-outs.⁴¹

32. Addicott (2011)

33. Miller et al (2012b)

34. TPP Law (2010)

35. LGG (2011)

36. LGG (2011)

37. TPP Law (2010)

38. TPP Law (2010)

39. LGG (2011)

40. Hazenberg et al (2013)

41. TPP Law (2010)

Operating as a charitable entity does offer tax incentives and ensures stakeholders of the future use of funds and assets.⁴² However, this limit on the assets and funds of a charitable organisation would limit the flexibility of a spin-out, which could provide a major hindrance when operating in a competitive marketplace alongside large-scale and established private sector competitors. Establishing a charity is also a complex and often difficult process. Finally, it is more difficult for a charitable organisation to receive investment, as shares cannot be taken in such a model and this could provide complications for a charity that is seeking social investment.

3. Staff motivation and attitudes

Social entrepreneurship literature suggests that motivations for setting up social enterprises can be triggered by either choice ('pull') or necessity ('push').⁴³

Evidence on social enterprises and spin-outs in the health sector indicates that choice or 'pull' spin-outs are those that are opportunity driven and are undertaken to create benefits for the service, its staff or users.⁴⁴ They may arise through staff innovation and desire to improve service provision. Such spin-outs may be 'bottom-up' led, being initiated relatively low down in the hierarchy by public sector employees. On the other hand, motivations to spin-out may be 'push' driven, arising from a reaction to changes in policy and funding, particularly those that threaten services with dissolution or potential privatisation.⁴⁵

Research by Hazenberg and Hall on spins-outs in different sectors identified that the financial crisis and government spending cuts led to local authorities being expected to achieve the same outputs (or sometimes more), with less finance.⁴⁶ Often, spinning out into social enterprises was the only option available for staff to retain control and ownership of their services. Furthermore, the Social Enterprise Coalition (now Social Enterprise UK) states that spinning out enables staff to be '... masters of their own destiny rather than let their future happen "to them"', such as being cut, merged with another public sector body or transferred into the winner of a tender.⁴⁷

Although spinning out is frequently a response to government restructuring policies or spending cuts, Addicott argues that social enterprises may be more successful if they are established through enthusiasm and engagement that comes from the bottom upwards, rather than top-down control mechanisms.⁴⁸ Spinning out to avoid the alternative (eg being put out to tender), may result in a business case that does not stack up and an organisation that will not be able to survive within a competitive marketplace. This can be problematic as Hazenberg and Hall identified: unconvincing business cases/plans were a factor in local authorities rejecting the spin-out of services into social enterprises.⁴⁹

42. LGG (2011)

43. See for instance Thompson (2008), Windrum (2008)

44. Hall et al (2012a), Addicott (2011)

45. Hall et al (2012a), Addicott (2011)

46. Hazenberg and Hall (2013)

47. SEUK (2011)

48. Adicott (2011)

49. Hazenberg and Hall (2013)

Spinning out public services entails significant costs, including planning, setting up and launching the social enterprise

The main cited benefits for public sector staff in spinning out revolve around increased staff involvement in the decision-making processes regarding the design and delivery of services. Evidence suggests that providing staff with ownership of their services increases engagement and commitment, which ultimately contributes to increased productivity and staff morale, as well as lower staff turnover and sickness levels.⁵⁰ Staff ownership can lead to increased creativity, inspiration and innovation, while encouraging and enabling staff to ‘... challenge traditional ways of thinking.’⁵¹

Evidence from social enterprises in the health and social care sector indicates that social enterprises report increased efficiency and less bureaucracy through faster decision-making processes (ie less time is spent on communications with health commissioners).⁵²

4. The risks inherent in spinning out

While the benefits of spinning out are tangible, there are however, a number of risks associated with the process. These include access to finance and business failure. Additionally, spinning out brings with it greater accountability and takes away the ‘safety net’ provided by the public sector.⁵³

Hall et al found that many new social enterprises in the health and social care sector are not yet in a position to be able to compete with other public, private and third sector providers and tender for large public sector contracts.⁵⁴ For spin-outs, this is in part due to the considerable time it takes for them to establish themselves (something usually underestimated), which limits their ability to access funding and secure service delivery contracts.⁵⁵ Although initiatives such as opening contracts to Any Qualified Provider have opened up the public sector for social enterprises, these new organisations have to compete with established and substantial private or voluntary sector organisations. New spin-outs may be superseded by larger and more commercial organisations through their economies of scale and their ability to run loss leaders.⁵⁶

Spinning out public services entails significant costs, including planning, setting up (for example, legal and IT costs) and launching the social enterprise.⁵⁷ While financial and business support has been made available, such as through the Mutual Support Programme or Social Enterprise Investment Fund (SEIF), such funds are only available for limited periods of time and securing funding is a competitive and often lengthy process.⁵⁸

Indeed, significant amounts of fiscal capital are required to underwrite the liabilities that public sector organisations transfer to spin-outs.⁵⁹ The access to such capital is limited to all but the largest organisations and emerging financial markets such as the ‘social investment market’ do

50. Gui (1991), Cabinet Office (2011), SEC (2011)

51. CityCare Partnership, cited in SEC (2011)

52. Addicott, (2011), Hall et al (2012b), Alcock et al (2012)

53. Simmons (2008), Hall et al (2013)

54. Hall et al (2012b)

55. Hall et al (2012b), Tribal (2009), Miller and Millar (2011)

56. House of Commons, 2011, cited in Birchall (2012)

57. SEC (2011)

58. Alcock et al (2012)

59. Burns (2012)

not yet provide the levels of capitalisation required by social enterprises and mutuals.⁶⁰ This lack of available capital is partly due to the limited capacity of the social investment market at the present time, as well as the risk that fund managers perceive in financing organisations that may receive the vast majority of their income from one (or a few) public sector contracts.⁶¹ This is an area that is not helped by the lack of contract guarantees that many new service spin-outs have to deal with, such as those operating within the Right to Provide Programme.

Low awareness remains a problem for the promotion of employee-led public service mutuals as the viability of spinning out as an option is not widely understood within local government, the NHS and, in some cases, Whitehall.⁶² This lack of awareness led TPP Law, one of the leading law firms operating in this area, to state that public sector commissioners should collate information on public service mutuals as part of a demonstration programme designed to inspire other public services to follow suit.⁶³

While the education of commissioners is ongoing in relation to spin-outs, (including links to policy initiatives such as the Public Services (Social Value) Act 2012), this is still an area in which more could be done. The evidence gap around the viability of public sector spin-outs also limits their adoption, particularly when human resources and legal departments have little knowledge of the process, or the main imperative for the restructure is cost-cutting.⁶⁴ Indeed, this is an area that recent research by Hazenberg and Hall identified as limiting spin-outs in local authorities.⁶⁵ Tax issues have also limited the growth of spin-outs, with tax policy and regulation generally favouring debt over equity investment.⁶⁶

There are emerging concerns around the ability of public sector staff to establish and run public sector mutuals. Spin-outs require strong leadership from public sector social entrepreneurs, as well as long-term leadership stability.⁶⁷ Spinning out requires public sector staff to ‘work in a different way’, take on new roles and often demonstrate business and entrepreneurial skills they do not necessarily possess.⁶⁸

Indeed, the survival of traditional business models in a competitive marketplace is often challenging enough, but this is made even more difficult for social enterprises as they have to balance a triple bottom line (financial, social and environmental).⁶⁹ Recent evidence suggests that public sector workers may not have the business and management skills required to set up a social enterprise, survive within a competitive market and balance the social, environmental and economic areas of the organisation.⁷⁰ These various factors may lead senior managers not to pursue the spin-out of services.⁷¹

60. Hazenberg et al (2013)

61. Hazenberg et al (2013)

62. Burns (2012)

63. TPP Law (2010)

64. Burns (2012)

65. Hazenberg and Hall (2013)

66. Burns (2012)

67. SEL (2010), Addicott (2011)

68. Simmons (2008)

69. Campi et al (2006)

70. Hazenberg and Hall (2013), Burns (2012), Hall et al (2012b)

71. Hazenberg and Hall (2013)

There are also ongoing concerns around the employment and pension rights of public sector staff in spin-outs and there has been some resistance from trade unions in this area.⁷² In relation to this last point, the process of spinning out public services is complex, as the transfer of assets (ie buildings) and liabilities (ie pensions), requires extensive legal support that often does not exist within the public sector. This has led to the growth of law firms that specialise in processes such as Transfer of Undertakings (Protection of Employment) regulations (TUPE).⁷³ These firms also provide general legal advice to public sector organisations exploring the option of spinning out services.

The evidence suggests that a successful spin-out requires support internally from staff at all levels of the organisation, and as Hazenberg and Hall found, a lack of ‘buy-in’ by senior management teams can lead to the spin-out not going ahead.⁷⁴ Local politics and support from those ‘at the top’ (ie senior management and elected officials) may therefore play a role in whether the spin-out goes ahead, and securing a local authority ‘champion’ could be extremely beneficial to the process.⁷⁵

5. Users and outcomes

One of the key benefits of spin-outs is their potential for greater engagement of service users in both designing and running services. User engagement may include having service users as board members, or as paid staff or volunteers.⁷⁶ Although users have greater representation within spin-outs than most public services, there is still limited evidence to show that users’ views get fully integrated into organisational aims and objectives.⁷⁷ Further investigation is needed to examine the nature of consultation and degree of co-design and the barriers and challenges that exist.

Research on the impact and outcomes of spin-outs is limited, especially in relation to service user outcomes. Therefore, little is known about how well spins-outs are performing in comparison to their public sector counterparts. This evidence gap arises primarily out of the infancy of most spin-out ventures, which inevitably means that it is too early to establish clear outcomes and impact. The limited research that does exist around user outcomes is largely positive, suggesting that spin-outs are able to provide high quality, responsive services that are inclusive of all groups within society.

An evaluation of the SEIF stated that, although it is too early to obtain data on user health outcomes, social enterprises – including health spin-outs – are particularly good at providing services for vulnerable and disadvantaged groups.⁷⁸ Furthermore, Miller et al revealed that Right to Request spin-outs are committed to tackling inequalities and are able to respond to local needs.⁷⁹ Ongoing research being carried out by the Local Government Association is exploring the performance of eight case study

72. Birchall (2012), TUC (2011)

73. Notably TPP Law (2010) and BWB (2013)

74. Hazenberg and Hall (2013)

75. SEC (2011)

76. Hazenberg and Hall (2013), Hall et al (2012b)

77. Simmons (2008)

78. Alcock et al (2012)

79. Miller et al (2012a)

spin-outs operating across England. The data from such research projects, when complete, should provide a better overview of the outcomes experienced by staff and users of public services that have been spun out.⁸⁰

Conclusion

The Coalition government has built on the support provided by the last administration for public sector workers to take control of their services by spinning them out as social enterprises or mutuals. It actively promoted the role of mutuals within the public sector in its programme for government, arguing that such models can be more efficient and responsive.⁸¹

The evidence to date suggests that staff in spin-outs are more engaged and committed than in the public sector, and that this contributes to increased productivity, lower staff turnover and sickness levels.⁸² Some mutuals are doing well in engaging service users in design and delivery, including as board members, paid staff or volunteers.⁸³

However, emerging evidence identifies a number of barriers faced by spin-outs, including access to finance (including start-up funding), as well as competition from other public, private and third sector organisations for public service contracts.⁸⁴ Furthermore, some public sector workers (for example, health clinicians) may not have the management and business skills required to set up and run a social enterprise within a competitive marketplace.⁸⁵

As the appetite for spin-outs increases and new providers move into delivery, important opportunities arise for gathering the body of evidence needed to assess the extent to which social enterprises and mutuals will be able to effectively involve service users and deliver more efficient, responsive and high quality services than the public sector.

Dr Richard Hazenberg and Dr Kelly Hall

80. LGA (2012)

81. Cabinet Office (2010), Cabinet Office (2012a)

82. Cabinet Office (2011), SEC (2011)

83. Hazenberg and Hall (2013), Hall et al, (2012b)

84. Hall et al (2012b), Tribal (2009)

85. Alcock et al (2012), Addicott (2011)

Conclusion

Enterprise Solutions was not a project that aimed to create public service mutuals. It was an action learning project looking at the potential and process of mutualisation. So the fact that only one of the four participating boroughs spun out an employee-led mutual through the course of the project is in no way a judgement of its success. Nevertheless, it is striking that the move towards mutual models in this small project has been similar to the national movement: slower than some had predicted and leading to a wider variety of solutions.

One borough explored the business case for micro-mutuals in its Adult Social Services Department before deciding that the services in question would be more sustainable commissioned out through open tender. Another looked at spinning out its communications and public relations services as a way of creating better networking and development opportunities, and is still considering what interim stages and trading models might be necessary in moving towards this goal. Another explored the partial spin out of its library services, but ultimately retained responsibility for the service itself while transferring library buildings to a local social enterprise, which has developed them as multi-functional community hubs. Only in Kensington and Chelsea has a new spin-out emerged; its Youth Support and Development Service beginning trading as EPIC CIC in April of this year.

For mutualisation sceptics, the slow pace and relatively small scale of the transitions to date confirm that the mutuals agenda is a sideshow. The value of government contracts to the private sector has doubled in four years to £20bn.⁸⁶ Viewed against this scale of transfer, the outsourcing through spin-outs of some specialist health and community services and the occasional high-profile Whitehall unit is underwhelming. Unless and until a larger number of big national and local services spin out as social businesses, the entrepreneurial transformation promised to the supply side by a new wave of social businesses will not materialise. Unsettling the incumbents will require a critical mass.

Government and public service leaders therefore need to be bolder. Where we see public service mutuals operating elsewhere in Europe at scale as mature parts of the public service economy, local and national policymakers have gone further than the UK in promoting the conditions for success, such as highly accessible business support, a focus on value-creation through participative governance and co-production and long-term commissioning strategies.⁸⁷ Yet these are difficult times in which to introduce these kinds of changes. Demand reduction – or, more

86. Plimmer (2013)

87. For a full discussion of international success factors, see Bland (2011)

For a local authority to consider how it can stimulate local entrepreneurship and a dynamic social enterprise economy without considering its own service model would be short-sighted

crudely, cost reduction – is an overarching imperative for public services, and mutuals are often a time-consuming and expensive solution to a service delivery problem that can be addressed more immediately through in-house cuts or competitive tendering. For services of around 100 staff, Social Finance estimates that a spin-out options appraisal is likely to cost approximately £10K (including staff time), with another £60–£120K needed for business planning.⁸⁸ If spin-outs can successfully use this initial public investment to tap a diversity of new funding streams, including social finance and work outside the public sector, services may become more effective and efficient in the long term, but the parent body may not feel that this is a risk they are in a position to take on traditional value-for-money grounds.

One of the reasons that public service mutualisation, or the promotion of social enterprise solutions, requires strong political leadership is that the benefits that can flow from it may be clearest at a whole-area level, rather than simply in terms of service-by-service fiscal savings. The social value of employee-led services, genuinely responsive through their governance mechanisms to their service users, is more complex than the financial cost of those services, and enhancing it will be crucial as local authorities look to demand management and the nurturing of resilient communities as solutions to pressures in the longer term. Within a strategy that emphasises the importance of resourceful communities, networks of social businesses that draw from and develop local skills and retain value locally have distinct advantages over other outsourced or in-house options. For a local authority to consider how it can stimulate local entrepreneurship and a dynamic social enterprise economy without considering its own service model would be short-sighted.

Mutualisation poses many of the right questions, even if it may not ultimately offer the right form. As Lewisham Library service found in considering its future options, partnering with and supporting the local social enterprise sector proved an effective way of generating locally valued outcomes through a locally trusted partner. In other places, the best enterprising solution may be an in-house trading company, partnered with specialist small and medium enterprises.

RSA 2020 Public Services believes that sustainable economic growth and public service reform are two sides of the same coin. Mutualism – and social enterprise approaches more broadly – provide a valuable way of connecting them in practice.

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RSA 2020 Public Services

88. Social Finance (2012)

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