



National Audit Office

## **PROTECTING STAFF IN PPP/PFI DEALS**

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## Summary

**1** The Government has contracted out approximately nine per cent of its service delivery to the private sector through outsourcing, Public Private Partnerships (PPP) and the Private Finance Initiative (PFI).<sup>1</sup> The contracting out of service provision will often lead to public sector staff becoming employees of the private sector contractor. The National Audit Office has examined the impact on the terms and conditions of staff who transferred to a private sector contractor, in PFI deals which commenced service delivery between 1992 and 2004, through a survey. This paper presents the results of the survey and also explains recent government initiatives to help protect staff delivering public services in the private sector.

**2** When a new employer takes over the delivery of a service, the staff delivering that service are protected by Transfer of Undertaking (Protection of Employment) legislation (TUPE). This ensures any changes to their terms and conditions must be made in a negotiated fashion. Staff who are subsequently hired to work on the contract can, however, be paid at the prevailing market rates. We conducted a survey in October 2004 of a range of PFI deals to determine the extent to which staff hired following the commencement of the contract received different terms and conditions.

**3** The survey covered 13 per cent of PFI deals, 67 per cent by capital value, as at October 2004 and over 15,400 staff transferring from the public to the private sector. All the deals in the final sample had applied TUPE although none were signed following more recent policy changes. It collected information on the number of staff employed, rates of pay and the number of staff in employer pension schemes. The survey collected data at the time the transfer took place and at the survey date to allow a comparison over time. This report is intended to provide a summary of the survey findings. It is not possible to determine the statistical significance of the survey due to the absence of aggregate data on the total number of staff transferred from the public to the private sector under PPP/PFI. Given the timing of the survey, and any impact stemming from more recent policy developments, the survey cannot be used to draw conclusions on the current market.

**4** The survey revealed that total employment levels in the sample of deals increased by 20 per cent between the time the PFI contracts were signed and late 2004 although the number of staff who originally transferred had fallen by an average of 8 per cent a year; voluntary resignation was the most common reason given for the turnover of these staff. In the majority of cases differences in rates of pay had narrowed over time and were less pronounced at the time of the survey.

**5** Since the deals in the survey were signed the Government has extended the protection offered to staff delivering public services in a range of ways. In 2001 the Department of Health introduced a policy to protect soft facilities management staff in PFI deals, such as cleaners. This ensures that the majority will remain employed by the NHS trust and be seconded to the private sector for the duration of the contract. The Office of the Deputy Prime Minister introduced a code of practice in March 2003 to ensure all staff hired to work on outsourced Local Authority contracts receive terms and condition on the whole 'no less favourable' than their public sector counterparts. The principles of this code were extended to the wider public sector by the Cabinet Office in March 2005.

## PART ONE

# In the past staff transferring to PPP/PFI deals could have received different terms and conditions from other staff

### Private sector involvement in public services often involves staff transferring

**1.1** The public sector has contracted out approximately 9 per cent of its service delivery commitments to the private sector.<sup>1</sup> This includes activities such as facilities management and the provision of support services and represents expenditure of £49 billion in 2005-06 (expected to grow to £64 billion by 2008-09). When these contracts are awarded the winning bidder is frequently obliged to take over the existing workforce upon commencement of the contract. This has resulted in significant numbers of employees transferring from the public to private sector, and within the private sector when contracts are re-tendered to different service providers.

**1.2** The total investment in Public Private Partnerships (PPP) and the Private Finance Initiative (PFI) in 2005-06 was approximately £6 billion,<sup>2</sup> representing 12 per cent of the total private sector involvement in public services. These deals cover a wide-range of services, from the construction and maintenance of buildings such as hospitals and schools to national infrastructure projects such as the management of toll roads and the maintenance of the London Underground. From 1995 to November 2004 it is estimated that 35,000 staff transferred from the public to the private sector as a result of PPP/PFI.<sup>3</sup>

### Transferring staff are protected by TUPE legislation

**1.3** When the business in which an employee works transfers from one employer to another, the employees are protected by the Transfer of Undertakings (Protection of Employment) regulations (TUPE), which implement the European Union acquired rights directive. This legislation protects employees' terms and conditions at the point of the transfer. Subsequent changes to employees' terms and conditions must be made in a negotiated fashion with employee representatives, which can include compensation for any loss of rights.

**1.4** For TUPE to apply, a 'transfer of undertaking' must be deemed to have occurred. This may not always be the case and it can sometimes be argued that the nature of the work undertaken by the new employer will be different to that undertaken by the old employer. Where this is the case TUPE legislation will not apply. In January 2000 the Cabinet Office released the *Statement of Practice on Staff Transfers in the public sector* which set out that TUPE should always apply to public sector transfers even where there was no legal case for it. Therefore within the public sector TUPE applies to all situations where a service or function is contracted out, retendered, brought back into the public sector, transferred within the public sector, or restructured and organised in a new way in a different part of the public sector.

**1.5** TUPE does not protect all terms and conditions; most notably it does not preserve pension rights. In June 1999 the Treasury introduced guidance relating to the treatment of pensions for public sector staff transferring to the private sector. Under this guidance, staff transferring from the public to the private sector must be offered access to a 'broadly comparable' pension scheme. The Government Actuaries Department is responsible for adjudicating whether the scheme is 'broadly comparable'.

## TUPE has no relevance to staff who subsequently join the contractors' workforce

**1.6** TUPE acts to preserve the terms and conditions of transferred employees. It has no legal relevance to new joiners to an outsourced workforce. Subsequent joiners could therefore have different terms and conditions from the transferring staff. Trade Unions have produced reports<sup>4</sup> which highlight the issue of transferred staff receiving more favourable terms and conditions for performing the same job as new recruits. As this evidence is limited, however, and the position will vary geographically, it is not clear to what extent this occurs. The Office of Government Commerce commissioned some work in this area in 2001 which concluded that new recruits had been offered different terms and conditions from transferring staff and that these were sometimes better and sometimes worse depending on the local labour market.

**1.7** The Government has taken action in order to address this issue; these measures are explored in more detail in section 3 of the report. In June 2001 the Department of Health introduced steps to ensure that, in any PFI deal which involved the provision of soft facilities management, such as cleaning, the majority of affected staff would have the opportunity to remain employed by the NHS Trust if they chose to do so.<sup>5</sup> The Office of the Deputy Prime Minister introduced a Code of Practice in 2003 that seeks to ensure all staff hired to work on outsourced contracts enjoy employment on fair and reasonable terms with conditions which are, overall, no less favourable than those of transferred employees.<sup>6</sup> This Code of Practice was later extended, with some modifications, to the wider public sector by the Cabinet Office.<sup>7</sup> This wider code of practice came into force from March 2005.

## PART TWO

### Differences in pay received by transferring staff and other staff in PPP/PFI deals

**2.1** This is the first substantive survey to measure the extent of any changes to the terms and conditions of employment in PFI contracts. The survey questionnaire was developed with advice from industry, trade unions and our audit clients. Requests for completion were addressed directly to PPP/PFI contractors. The survey has collected data on employment levels, staff turnover, rates of pay and the proportion of staff in employer pension schemes both at the start of the contract and the date of the survey; it can therefore show the movement in terms and conditions for a sample of PPP/PFI deals from their start to the date of the survey (October 2004). Before this survey there was no publicly available data on the aggregate level of any differences in terms and conditions. Due to the impact of policy changes (see Part 3) it is not possible to use the survey results to draw conclusions on PPP/PFI contracts entered into in recent years.

#### The survey covered 58 contractors working on 43 PPP/PFI deals

**2.2** The survey was conducted in two parts. The Part A questionnaire was sent to Special Purpose Vehicles (SPVs), each one responsible for a single PFI contract, to collect data on the SPV and its subcontractors who were performing the services. We contacted 146 SPVs, focussing on higher value projects, from the database held by HM Treasury; only deals in England were considered in order to isolate the impact of

Government initiatives such as the Cabinet Office Statement of Practice on the terms and conditions of staff. Following a 67 per cent response rate from the SPVs we eliminated those projects where no staff transfer had taken place and sent detailed Part B questionnaires to the 170 subcontractors nominated by the respondents. We received a total of 84 detailed returns covering 68 projects, a response rate of 49 per cent. The data submitted by these subcontractors was then critically reviewed so that only those organisations that had submitted fully comparable data were included in the final sample.

**2.3** The final retained sample consists of 58 contractors involved with 43 active projects. As at the survey date these companies employed nearly 12,300 former public sector employees on contracts with a total capital value of £20,151 million and annual payments of £1,629 million. **Figure 1** shows the population coverage of the final sample.

**2.4** The 43 detailed responses covered 13 per cent of relevant deals by number and include the largest deals involving former public sector staff, such as the three London Underground Public Private Partnerships. As a result the sample covered 67 per cent by value of the 341 operational contracts. The statistical significance of the survey is hard to determine in the absence of aggregate data on the total number of public sector staff that have transferred to the private sector under PPP/PFI.

#### 1 Coverage of the sample<sup>1</sup>

	Total population	Total meeting criteria <sup>2</sup>	Total retained sampled	Percentage Coverage
Number of PFI projects	432	341	43	13
Capital value <sup>3</sup> £m	37,670	30,174	20,151	67

Source: National Audit Office analysis

#### NOTES

1 With reference to HMT database of signed PFI deals in England as at December 2004.

2 Those deals that were operational and involved staff transfer.

3 The Public Sector discount rate changed from 6 per cent to 3.5 per cent in 2001; capital values calculated prior to this change have not been re-based.

**2.5** At least half of the retained sample reached financial close prior to the announcement of the Cabinet Office Statement of Practice (January 2000); all 43 deals, however, applied the provisions of TUPE. The timing of the survey means that none of the deals were signed under the more recent measures which aim to harmonise the terms and conditions of staff. Further analysis of the sample can be found at Appendix 1.

**2.6** The data has been analysed by the service type of the contract and the grade of staff. Service delivery takes two main forms. The operation and maintenance of buildings and equipment is termed “Hard Facilities Management”. In contrast, the provision of services such as catering and cleaning is known as “Soft Facilities Management”. Where contractors indicated that the contract involved elements of both Hard and Soft FM they have been classified as Mixed FM. The sample broken down by contract type is shown in **Figure 2**.

## The total number of staff in the surveyed deals had risen by 20 per cent

**2.7** The total number of employees in the 43 deals at the time the contracts were signed was 18,518 of whom 15,480 were former public sector staff with terms and conditions protected under TUPE legislation; these staff occupied positions in the broad categories set out in **Figure 3**. As at the survey date in October 2004, the numbers employed had increased to 22,221 (nearly 12,300 of which were former public sector employees) compared to when the contracts were signed; this time span was different for each deal but averaged 3.3 years.

**2.8** Some growth in employment would be expected as many of these PFI deals are extending the services previously provided or launching programmes of significant new investment. The proportion of full time staff moved only slightly from 62 per cent at the time of transfer to 61 per cent at October 2004; the percentage of full time staff at the time of transfer is based solely on the proportion of transferred full time staff. **Figure 4 overleaf** shows where the growth in employment took place in the 43 deals. If the two London Underground PPP deals are excluded from the analysis the overall percentage growth in employment over the period is slightly higher at 21 per cent.

### 2 The majority of contracts in the sample deliver facilities management

Contract Type	Contractors	Percentage
Soft Facilities Management	27	47
Hard Facilities Management	14	24
Mixed Facilities Management	12	21
Administrative	3	5
Professional	2	3
<b>Total</b>	<b>58</b>	<b>100</b>

Source: National Audit Office analysis

### 3 The majority of staff transferring were in the manual grade

Grade of staff	Number of staff	Percentage
Senior Management	220	1
Middle Management	1,132	7
Supervisors	1,197	8
Clerical	1,634	11
Manual/Operative	11,297	73
<b>Total</b>	<b>15,480</b>	<b>100</b>

Source: National Audit Office analysis

#### 4 The greatest growth in employment levels was seen in Soft FM contracts

	Time of transfer			October 2004			Increase	
	Transferred staff	Other staff	Total staff	Transferred staff	Other staff	Total staff	Number	%
Soft FM	5,243	1,616	6,859	3,778	4,882	8,660	1,801	26
Hard FM	7,215	493	7,708	6,203	2,980	9,183	1,475	19
Mixed FM	2,896	611	3,507	2,219	1,611	3,830	323	9
Administrative	114	306	420	58	465	523	103	25
Professional	12	12	24	10	15	25	1	4
<b>Total</b>	<b>15,480</b>	<b>3,038</b>	<b>18,518</b>	<b>12,268</b>	<b>9,953</b>	<b>22,221</b>	<b>3,703</b>	<b>20</b>
<b>Excluding London Underground PPP</b>	<b>9,184</b>	<b>2,787</b>	<b>11,971</b>	<b>6,646</b>	<b>7,845</b>	<b>14,491</b>	<b>2,520</b>	<b>21</b>

Source: National Audit Office analysis

### Turnover of transferred staff in the survey was 21 per cent as at October 2004

**2.9** It is to be expected that the number of transferred staff working on a PPP/PFI contract will decline over time as staff leave through natural wastage. **Figure 5** shows that the turnover of transferred staff in the survey varies by the type of service provision and averages 7 per cent per year. The soft FM contracts experienced the highest annualised rates of transferred staff turnover at 9.6 per cent. This is not unexpected given the nature of the work, principally cleaning and catering, as these professions generally experience relatively higher turnover rates. The total annual staff turnover for the public sector in 2004 was 12.4 per cent.<sup>8</sup> It is not possible to compare the survey results directly with this figure as the survey only shows the turnover of transferred staff.

#### 5 Soft FM contracts experienced the highest turnover of transferred staff

	Absolute change (%)	Annualised change (%)	Absolute numbers
Soft FM	27.9	9.6	1,465
Hard FM	14.0	6.0	1,012
Mixed FM	23.4	7.1	677
Admin support	49.1	8.2	56
Professional	16.7	7.7	2
<b>Overall</b>	<b>20.8</b>	<b>7.6</b>	<b>3,212</b>

Source: National Audit Office analysis

### The majority of transferred staff leaving the contracts did so voluntarily

**2.10** **Figure 6** shows the reasons given by the contractors for the turnover of staff protected by TUPE legislation. About two in every dozen were a result of redundancy or dismissal. The majority of changes in the survey data were of a voluntary nature, although it should be noted that the term 'voluntary redundancy' may cover a wide range of reasons for leaving. The total of 66.4 per cent is comparable to the wider public sector benchmark of 60 per cent.<sup>8</sup>



## 6 The majority of transferred staff left voluntarily

Reason for leaving	Absolute number	% of total
Voluntary Resignation	2,133	66.4
Retirement	347	10.8
Redundancy	275	8.6
Dismissal	261	8.1
Long Term Sick Leave	67	2.1
Maternity Break	15	0.5
Career Break	2	0.1
Other reasons <sup>1</sup>	112	3.5
<b>Total</b>	<b>3,212</b>	<b>100.0</b>

Source: National Audit Office analysis

### NOTES

1 Other reasons given were:

- Compromise agreements
- Contract ended
- Death
- End of temporary contract
- Illegal status
- Never started
- Overseas travel
- Personal reasons
- Transferred to other contracts within the company

## Rates of pay received by transferred staff were not uniformly higher than those received by other staff

**2.11** The next series of figures compares the average hourly rates of pay received by staff working on the deals in the survey. The figures presented in the following tables have been weighted by deal number, so that the rates of pay offered by a contractor employing 50 staff are given the same weight as those of a contractor employing 1,500; the number of contractors supplying data for each average is given in the tables (N). The data collected by the survey did not allow for the collection of data on variable pay rates within employment grades. The median hourly rates of pay are presented in Appendix 2.

**2.12** Benchmarks have been created that attempt to draw a comparison with the pay rates in the survey and those applying to similar jobs in the public sector. In order to create these we have drawn data from the Income Data Services (IDS) pay benchmark service. The figures are not directly comparable as the IDS data applies over a range of dates and the roles for which data has been collected can only approximate those roles in the survey. Differences between male and female rates of pay have not been included in the analysis as data submitted by individual contractors showed no differences.

**2.13** In recognition that all the deals in the sample started delivering services at different dates, all pay data has been adjusted for inflation. The data supplied at the time of transfer has been indexed using the seasonally adjusted Average Earnings Index to the survey date, October 2004. Using this index, in some instances the real rates of pay have decreased over time. It is important, however, to appreciate that the wage index used is a measure of the whole economy and, as such, incorporates sectors that experienced a different rate of inflation from those in the survey. It is also worth noting that the nature of the jobs themselves may well have changed over time which may have had an impact on the remuneration.

**2.14** It should be borne in mind when reading these figures that the data presented represents hourly rates of pay only and does therefore not represent the full package of terms and conditions received by staff.

**2.15** **Figure 7 overleaf** shows the rates of pay received by each grade for both transferred and other employees at the start of the contract and at the survey date. Rates of pay of transferred staff were not uniformly higher than those of other staff. For staff in the manual grade, the majority of staff covered by the survey (see Figure 3), rates of pay of transferred staff appeared marginally higher than those of other staff.

**7** Average hourly real<sup>1</sup> pay rates and number of contracts (N) – All contracts (58)

	Time of transfer				October 2004			
	Transferred (£)	N	Other (£)	N	Transferred (£)	N	Other (£)	N
Senior Management	25.93	15	23.74	26	26.13	17	24.00	32
Middle Management	15.22	36	15.39	29	14.94	33	15.03	47
Supervisors	10.12	43	10.32	23	9.84	43	9.74	44
Clerical	8.87	37	9.12	27	8.80	35	8.47	47
Manual	7.56	51	7.34	30	7.44	49	7.14	50

Source: National Audit Office analysis

## NOTE

<sup>1</sup> The data supplied at the time of transfer has been indexed using the seasonally adjusted Average Earnings Index to the survey date, October 2004.

**2.16 Figure 8** shows the percentage that the pay rates of transferred staff differ from those received by other staff at both the time of transfer and the date of the survey. The largest differences were seen at the senior management grade although this grade represents relatively few of the transferred staff in the survey. The results show that the pay of transferred staff was not uniformly higher than that of other staff and that the difference had widened in the clerical and manual grades and narrowed in all other grades.

**2.17 Figure 9** shows the adjusted rates of pay received by staff on the Soft FM contracts in the survey. A benchmark was calculated for manual workers performing soft FM services in the public sector and found to be £5.92. The benchmark has been compiled using IDS data covering the range April 2004 to September 2005. For comparative purposes Soft FM manual workers have been classed as a composite of 'cleaners' and 'catering assistants'.<sup>9</sup> There are, however, limitations in this analysis as the job descriptions reflected in the benchmark may not be directly comparable with those of the survey.

**8** Percentage transferred staff pay rates are higher/ (lower) than other staff in all contracts

	Time of transfer (%)	October 2004 (%)
Senior Management	8.43	8.18
Middle Management	(1.10)	(0.62)
Supervisors	(1.97)	1.01
Clerical	(2.84)	3.73
Manual	2.87	3.99

Source: National Audit Office analysis

**9** Average hourly real<sup>1</sup> pay rates and number of contracts (N) – Soft FM contracts (27)

	Time of transfer				October 2004			
	Transferred (£)	N	Other (£)	N	Transferred (£)	N	Other (£)	N
Senior Management	17.31	4	16.88	8	19.42	4	17.39	10
Middle Management	11.86	9	13.69	8	12.01	8	13.97	20
Supervisors	7.65	18	7.17	9	7.71	19	7.49	22
Clerical	7.49	9	7.23	9	7.44	9	7.51	20
Manual	5.88	25	5.44	15	5.75	24	5.65	25

Source: National Audit Office analysis

## NOTE

1 The data supplied at the time of transfer has been indexed using the seasonally adjusted Average Earnings Index to the survey date, October 2004.

**2.18** Figure 10 shows the differences in rates of pay between transferred and other staff for the Soft FM contracts in the survey. Transferred staff received higher rates of pay than other staff in all grades except for middle management and clerical. Differences had, however, narrowed over time for the majority of the affected staff; across all the Soft FM contracts in the survey 94 per cent of transferring staff were in the manual grade where differences had narrowed to an average of 10 pence an hour.

**2.19** Figure 11 shows the rates of pay received by staff working on the Hard FM contracts in the survey. Initially, the pay of transferred staff was significantly lower than that of other staff for all grades. This is in line with other evidence, which suggests that these more technical roles are better compensated in the private sector.

**10** Percentage Transferred staff pay rates are higher/ (lower) than other staff in Soft FM contracts

	Time of transfer (%)	October 2004 (%)
Senior Management	2.46	10.45
Middle Management	(15.41)	(16.31)
Supervisors	6.27	2.92
Clerical	3.42	(1.04)
Manual	7.49	1.72

Source: National Audit Office analysis

**11** Average hourly real<sup>1</sup> pay rates and number of contracts (N) – Hard FM contracts (14)

	Time of transfer				October 2004			
	Transferred (£)	N	Other (£)	N	Transferred (£)	N	Other (£)	N
Senior Management	31.56	8	31.91	6	31.33	8	33.09	9
Middle Management	18.17	13	19.66	8	17.50	12	18.03	12
Supervisors	15.30	12	17.53	5	14.31	12	15.05	10
Clerical	10.57	13	11.30	7	10.59	12	9.87	13
Manual	12.48	12	14.73	5	12.11	11	11.45	12

Source: National Audit Office analysis

## NOTE

1 The data supplied at the time of transfer has been indexed using the seasonally adjusted Average Earnings Index to the survey date, October 2004.

**2.20** Figure 12 shows that in the Hard FM contracts in the survey the premium paid to staff who did not transfer from the public sector had fallen for the majority of grades.

## The number of staff in the survey joining employer pension schemes varied across service type

**2.21** Under The Fair Deal for Staff Pensions staff transferring from the public to the private sector must be offered access to a 'broadly comparable' pension scheme. The Government Actuaries Department is responsible for judging whether the proposed scheme is comparable and awarding a 'pension passport'. There was formerly, however, little information on the extent to which these pensions had been taken up by transferring staff. Figure 13 shows the proportion of employees who had joined the employer pension scheme at the time of transfer and the survey date; the totals are also shown without the impact of the London Underground PPPs, which account for a large number of the staff covered by the survey. These results cannot be used to draw conclusions on the quality of pension schemes covered by the survey nor on whether the employees had personal pension arrangements.

**2.22** The proportion of staff joining employer pension schemes varied for the different classes of service delivery in the survey. The employees in the Soft FM contracts had a lower proportion of staff as members of the pension scheme than employees in the other contract types. In all service types but Hard FM, the proportion of staff joining the employer pension scheme had increased over time.

## More former public sector employees in the survey had joined employer pension schemes than other employees

**2.23** Figure 13 also shows the extent to which, in the different classes of service, membership of employer pension schemes was more prevalent for transferred staff. Again, removing the London Underground PPPs changes the resulting totals. Under the Fair Deal for Staff Pensions<sup>10</sup> contractors were obliged to offer only transferring employees membership of a 'broadly comparable' occupational pension scheme. More recent protection measures, such as the Code of Practice on Workforce Matters (see paragraph 3.20), require that staff subsequently joining the contract are offered access to a good quality employer pension scheme.

### 12 Percentage transferred staff pay rates are higher/ (lower) than other staff in Hard FM contracts

	Time of transfer (%)	October 2004 (%)
Senior Management	(1.11)	(5.61)
Middle Management	(8.21)	(3.07)
Supervisors	(14.55)	(5.20)
Clerical	(6.90)	6.81
Manual	(18.00)	5.46

Source: National Audit Office analysis

### 13 Pension take up rates varied across service type

	Total staff numbers in service type		Total pension uptake (%)					
	Time of transfer	October 2004	All Staff		Transferred		Other	
			Time of transfer	October 2004	Time of transfer	October 2004	Time of transfer	October 2004
Soft FM	6,859	8,660	8	12	10	15	9	10
Hard FM	7,708	9,183	84	82	89	97	26	50
Mixed FM	3,507	3,830	22	26	27	32	7	17
Admin	420	523	11	83	41	79	66	84
Professional	24	25	50	92	100	100	92	87
<b>Total</b>	<b>18,518</b>	<b>22,221</b>	<b>45</b>	<b>45</b>	<b>50</b>	<b>60</b>	<b>17</b>	<b>27</b>
<b>Excluding London Underground PPP</b>	<b>11,971</b>	<b>14,491</b>	<b>21</b>	<b>23</b>	<b>21</b>	<b>27</b>	<b>19</b>	<b>19</b>

Source: National Audit Office analysis

## PART THREE

# Government departments have addressed the policy aim of harmonising terms and conditions in different ways

**3.1** The Government made a commitment that investment through PPP/PFI should not be made at the expense of an erosion in the terms and conditions of the staff delivering the services. This was set out in the Treasury's *Meeting the Investment Challenge*<sup>11</sup> document and more recently reiterated in *PFI: Strengthening Long-term Partnerships*.<sup>12</sup> These documents make clear that PFI should only be adopted 'where it can be shown to deliver value for money and does not come at the expense of employees' terms and conditions'. In seeking to enforce this principle a range of approaches has been employed, which are considered in this section of the report.

### The Department of Health model keeps support staff in NHS employment

**3.2** The Department of Health rolled out the Retention of Employment model (RoE) in September 2002 after it had been piloted in three PFI hospitals (see paragraph 3.5). It was based on a Labour Party commitment to 'seek ways in which, within the framework of PFI management, support staff could remain part of the NHS team'.<sup>13</sup> One perceived benefit of this approach was to strengthen partnership working between teams, leading to improved service delivery in such areas as ward management.

**3.3** The RoE model involves Soft FM staff having the option to remain within the employment of the NHS but being managed on a day to day basis by the private sector contractor. This is achieved by the majority of staff being seconded to the contractor for the duration of the contract. Those staff responsible for supervising the delivery of the services are transferred to the private sector under TUPE legislation to ensure that the risk transfer sought under PFI is not compromised. Hard FM staff are also transferred under TUPE legislation.

### The Department of Health engaged Trade Unions in the formation of the model

**3.4** The RoE model was developed jointly by Unison, the Office of Government Commerce (who then had responsibility for PFI policy) and Partnerships UK in mid 2001. The Department of Health have overall responsibility for the policy. The RoE model was seen as the optimal workable solution to fulfilling this 2001 manifesto pledge.

**3.5** The model was initially piloted in three PFI schemes (Havering, Stoke Mandeville and Roehampton) that were already well advanced but had not then appointed a preferred bidder. This allowed the impact of RoE to be judged in a competitive environment. A fourth pilot scheme, Walsgrave, was added at a later stage as it progressed quicker than anticipated.

**3.6** Given that the form of the solution had been broadly agreed between the Government and Unison, further consultation was limited. Industry groups, including the Business Services Association, and the private sector consortia and NHS trusts involved in the pilots were consulted along with other trade unions in advance of formally submitting the final proposal to Unison in March 2002.

**3.7** The final negotiations focussed principally on the how disciplinary matters would be handled and the definition of a ‘manager’, as under RoE all such ‘managers’ would be required to transfer to the private sector. It was agreed that contractors would apply the Trust’s disciplinary procedures on its behalf but that only the Trust would have the power to dismiss staff. The definition of a ‘manager’ for the purposes of RoE was not rigidly defined and is instead negotiated on a deal by deal basis with an assumption that the total number of ‘managers’ would not exceed 15 per cent of the workforce.

The Department of Health’s analysis showed that the RoE model created a cost premium of between 1–2 per cent on the pilot schemes

**3.8** The Department of Health made it clear that it would not accept the RoE model unless it was shown that the inclusion of the model would not jeopardise the value for money of PFI. In order to test this, the Department of Health

asked all bidders on the pilot schemes to re-submit their bids taking account of the RoE model. The Department of Health compared the revised cost of the four pilot schemes with the Public Sector Comparator.<sup>14</sup> This analysis is presented in **Figure 14**.

**3.9** Although this analysis was carried out at an earlier stage than usual (before final business cases had been submitted) it was decided to accept the RoE model. The Department of Health noted that where RoE was adopted in smaller schemes, PFI may come at a greater cost than conventional procurement, but felt that PFI brought intangible benefits in addition to those highlighted by the financial analysis. Although not explicitly examined the inclusion of RoE into the bids generated additional costs of between 1 and 2 per cent. This additional cost was seen as worthwhile in light of the security provided to the affected workers and it was felt that it would reduce over time as contractors became more comfortable with the RoE model.

#### **14** Incorporating RoE results in the service being more costly than the PSC in some cases

	<b>PSC</b>	<b>With RoE</b>	<b>Difference</b>	<b>% change in costs</b>
	Net Present Cost £m	Net Present Cost £m	Net Present Cost £m	
Walsgrave	3,248	3,230	(18)	(0.6)
Havering	392	380	(12)	(3.1)
Roehampton	303	307	4	1.3
Stoke Mandeville	102	104	2	2.0
<b>Total</b>	<b>4,045</b>	<b>4,021</b>	<b>(24)</b>	<b>(0.6)</b>

Source: Department of Health

## The legal stability of the model has been thoroughly investigated

**3.10** The legal basis for RoE was a contentious area and the Department of Health sought extensive advice in this area. There are principally two areas of difficulty:

- The first relates to the interaction of the secondment approach with TUPE legislation. When the responsibility for delivering the services is transferred under a PFI contract, under TUPE legislation, a 'transfer of undertaking' is deemed to have taken place. This obligates the staff delivering the service to transfer to the new provider. Legal advice suggested that the most effective mechanism for avoiding this would be for staff to formally object to the transfer thereby voluntarily terminating their employment with the NHS. The staff would then be rehired by the NHS on the basis that they will be seconded to the private sector on the same terms. If this mechanism was legally challenged by an affected employee at a subsequent date, it is possible that staff would be obliged to transfer to the private service provider as TUPE legislation cannot be deliberately avoided by agreement.
- The second difficulty arises because the seconded staff are to be directed on a day to day basis by the private sector contractor, even though they are not the legal employer. This could lead to the staff being deemed employees of the contractor despite their employment contract being held by the NHS. The Department of Health has addressed this issue in part by ensuring the NHS Trust has the sole ability to terminate contracts of employment for seconded staff while maintaining a right of veto over other disciplinary matters which are the generally the responsibility of the employer. The private sector contractor is also obliged to follow the policies of the NHS trust.

**3.11** On balance the Department of Health considers that it is highly unlikely that any stakeholders would seek to challenge the legal grounds for RoE.

## The operation of the model is not being actively monitored

**3.12** The Department of Health has not formally reviewed the impact that RoE has had operationally and has no plans to do so. It considers the policy as being successful in terms of improved employee relations as, to date, there have been no industrial relations difficulties on the schemes where RoE has been employed. There may be wider qualitative implications relating to reduced flexibility in managing the workforce delivering the service and on overall deal costs.

## The Local Government approach guarantees new starters terms and conditions that are 'no less favourable' than existing staff

**3.13** The Office of the Deputy Prime Minister (ODPM) sought to address Trade Union concerns in early 2002. It took the view that quality services and good value can only be delivered by contractors who manage their workforce well, an important element of which is equal pay for equal work.

## The Local Government Code attempts to retain flexibility

**3.14** The chosen solution, known as the Best Value Code of Practice on Workforce Matters, is intended to ensure that employees hired to work on Local Authority contracts receive terms and conditions that are 'overall no less favourable' than their public sector counterparts. It also provides, for both transferring and subsequently hired staff, access to the Local Authority pension scheme or membership of an alternative, good quality scheme (with the employer matching contributions up to 6 per cent for defined contribution schemes or stakeholder pension schemes). The code has been incorporated into the Local Government Act 1999, which requires Local Authorities to apply the code unless it can be demonstrated it is 'Best Value' to do otherwise.

**3.15** There is no formal guidance on how the term 'overall no less favourable' should be interpreted. Instead the aim is to create a flexible solution that involves a negotiated package of terms that all parties are prepared to agree. For this reason a dispute resolution procedure has been incorporated into the Code allowing the Local Authority to mediate over any problems. The Code itself is enforceable through the service contract.

### The Best Value Review Group considered how best to address the issue

**3.16** A number of potential models were considered including extending the legal provisions of TUPE and adopting the RoE model being trialled in NHS PFI projects. The code was drafted by the Best Value Review Group<sup>15</sup> and drew heavily on a draft voluntary code submitted by the Confederation of British Industry (CBI). This sought to ensure that the solution would offer contractors an element of flexibility whilst still protecting staff. Negotiations took place to agree the precise wording of the code and it was circulated to Local Authorities and Trade Unions for comment before coming into force in March 2003.

### There was no formal cost benefit analysis or pilot

**3.17** The ODPM did not carry out a formal cost benefit analysis or Regulatory Impact Assessment. There was no quantification of the expected benefits to service delivery. Financial analysis was conducted to judge the potential cost of applying the Code to future PFI contracts and outsourcing agreements and this put the cost impact at between £8 million - £12 million annually. On this basis the ODPM decided this was an acceptable price to pay to ensure that employees were adequately protected.

### Compliance with the Code is being monitored in most cases

**3.18** The ODPM has stated that it 'will monitor the operation of the Code and consult with stakeholders to assist this process'. The Code requires each contractor to demonstrate their compliance when requested by the contracting authority – this can involve trade union/client inspection.

**3.19** The monitoring arrangements were examined in the first of a four part evaluation of Local Government procurement commissioned by ODPM.<sup>16</sup> The review is being carried out by the Institute of Local Government Studies (INLOGOV), and incorporates a small number of questions on the application of the Code. The early results of the survey showed that Local Authorities were including the provisions of the Code as standard in contracts and that the majority relied on the contractor to confirm compliance with the code; 40 per cent of Local Authorities supplement this with client inspection although in a minority of cases (25 per cent) no monitoring arrangements had been implemented.

### The Cabinet Office has extended the protections offered by the Local Government Code throughout government

**3.20** Following the adoption of the Local Government Best Value Code in March 2003, the Cabinet Office extended the provisions across the wider public sector in March 2005. This extended code provides all staff hired to work on outsourced public services with terms and conditions 'no less favourable' than the staff who had transferred. It also provides access to either a good quality employer pension scheme or an equivalent stakeholder pension scheme. The Code of Practice is forward looking, applying to contracts signed after March 2005.



**3.21** Expansion of the Code of Practice was agreed to in principle as part of the Warwick agreement. The Warwick agreement was negotiated at Warwick University in July 2004 between the Labour Party and Trade Unions and concerned public sector policy and trade union law.

### The consultation process was simplified by the acceptance of the Local Government solution

**3.22** The Local Government Code provided a framework which had been agreed by the major stakeholders from all sides. The consultation and implementation phases of this extended code were greatly simplified by the previous agreement of the Local Government Code. This left the consultation process centred on the exemptions to the Code and the minimum level and type of pension provision to be provided by the private sector.

**3.23** The extended Code does not apply to Public Corporations, Trading Funds, Higher and Further Education institutions and Academies, which are independent of direct government control.

### No cost benefit analysis was undertaken

**3.24** No formal cost benefit analysis was carried out before the guidance was brought into force. The Cabinet Office took assurance from the previous roll-out of the Local Government Code and the analysis that was undertaken at this time. The Cabinet Office therefore believed that the resulting increase in costs across Government would not be prohibitive.

### Monitoring arrangements are in place

**3.25** Public sector organisations are now obliged to incorporate benchmarking and monitoring criteria within all service contracts signed after the Code came into effect in March 2005. Compliance with the Code is enforced by the public sector organisation that let the contract. This follows the principle of 'light touch' oversight where information requests are restricted to that required for the purpose of monitoring compliance, though a whistleblowing line to the sponsoring Department is available to all staff for complaints to be registered.

# Appendix 1

## Sample details

This appendix gives further information on the final survey sample of 58 service providers.

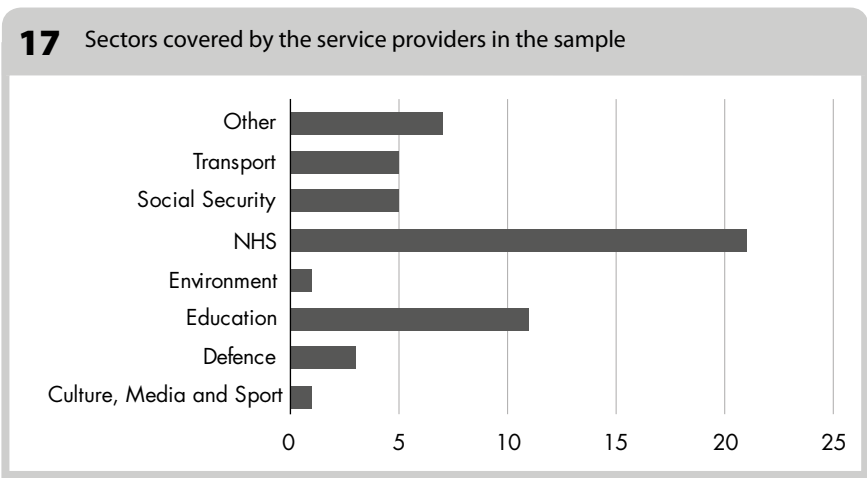
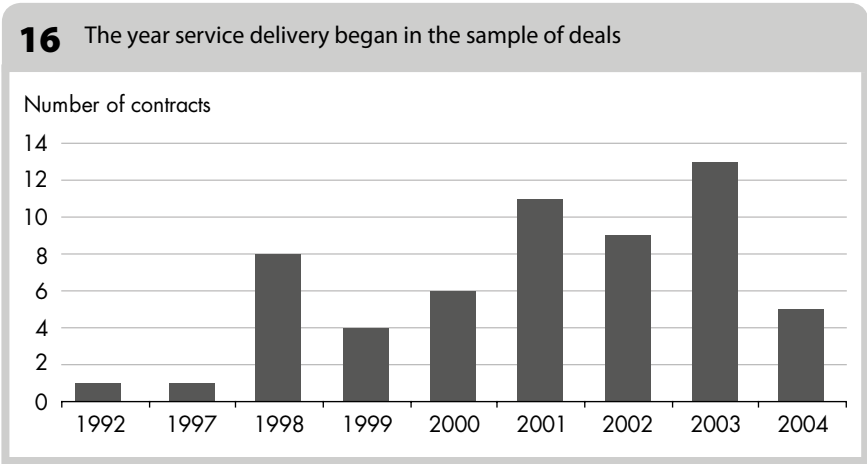
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Regions covered by service providers in the sample

London	South East	South West	North East	North West	East Midlands	West Midlands	Yorks. & Humber	Eastern
Number of service contracts operating in each region <sup>1</sup>								
15	18	13	12	11	8	14	9	8

NOTE

1 Some service providers operated in more than one region.



## Appendix 2

### Pay rate analysis

This appendix shows the median hourly rates of pay collected through the survey and the number of contractors that supplied the data.

#### 18 Median hourly real<sup>1</sup> pay rates and number of contracts (N) – All contracts (58)

	Time of transfer				October 2004			
	Transferred (£)	N	Other (£)	N	Transferred (£)	N	Other (£)	N
Senior Management	25.01	15	24.77	26	23.00	17	22.00	32
Middle Management	14.62	36	15.19	29	15.14	33	15.58	47
Supervisors	9.09	43	8.90	23	8.69	43	9.11	44
Clerical	7.86	37	8.09	27	7.93	35	7.95	47
Manual	6.27	51	5.92	30	6.10	49	6.23	50

Source: National Audit Office analysis

#### NOTE

1 The data supplied at the time of transfer has been indexed using the seasonally adjusted Average Earnings Index to the survey date, October 2004.

#### 19 Median hourly real<sup>1</sup> pay rates and number of contracts (N) – Soft FM contracts (27)

	Time of transfer				October 2004			
	Transferred (£)	N	Other (£)	N	Transferred (£)	N	Other (£)	N
Senior Management	17.36	4	16.51	8	21.06	4	16.40	10
Middle Management	11.41	9	14.61	8	11.83	8	14.05	20
Supervisors	7.20	18	6.53	9	6.86	19	7.33	22
Clerical	7.30	9	7.88	9	7.28	9	7.71	20
Manual	6.04	25	5.40	15	5.53	24	5.50	25

Source: National Audit Office analysis

#### NOTE

1 The data supplied at the time of transfer has been indexed using the seasonally adjusted Average Earnings Index to the survey date, October 2004.

#### 20 Median hourly real<sup>1</sup> pay rates and number of contracts (N) – Hard FM contracts (14)

	Time of transfer				October 2004			
	Transferred (£)	N	Other (£)	N	Transferred (£)	N	Other (£)	N
Senior Management	29.65	8	27.94	6	24.78	8	25.57	9
Middle Management	17.32	13	18.97	8	17.13	12	16.50	12
Supervisors	15.47	12	16.46	5	13.63	12	14.54	10
Clerical	9.88	13	11.18	7	8.49	12	9.34	13
Manual	10.44	12	13.48	5	12.45	11	11.65	12

Source: National Audit Office analysis

#### NOTE

1 The data supplied at the time of transfer has been indexed using the seasonally adjusted Average Earnings Index to the survey date, October 2004.

## Endnotes

- 1 *UK public sector outsourcing – the big picture to 2008-09*, Kable Consulting, July 2006
- 2 *Strengthening Long Term Partnerships*, HM Treasury, March 2006
- 3 Figures collected by Partnerships UK
- 4 *Contracting Out and the Two Tier Workforce*, Unison, September 2000
- 5 *The Retention of Employment model*, Department of Health, June 2001
- 6 *The Best Value Code of Practice on Workforce Matters*, Office of the Deputy Prime Minister, March 2003
- 7 *The Code of Practice on Workforce Matters*, Cabinet Office, March 2005
- 8 *Retention and Turnover Survey*, CIPD Recruitment, 2004
- 9 It was not possible to develop a comparable benchmark for Hard FM workers from the available job descriptions
- 10 *A Fair Deal for Staff Pensions*, HM Treasury, 1999
- 11 *Meeting the Investment Challenge*, HM Treasury, July 2003
- 12 *Strengthening Long-term Partnerships*, HM Treasury, March 2006
- 13 Labour Party 2001 manifesto
- 14 The Public Sector Comparator is the hypothetical cost of providing the service in the public sector
- 15 The Best Value Review Group comprised representatives from the TUC, GMB, Unison, T&G, BSA, CBI, LGA and LGEO
- 16 *Evaluation of the Local Government Procurement Agenda – Baseline Survey Report*, INLOGOV, 2004