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COMPTROLLER AND
AUDITOR GENERAL**

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Department of Health

Establishing social enterprises under the Right to Request Programme

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Department of Health

Establishing social enterprises under the Right to Request Programme

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Amyas Morse
Comptroller and
Auditor General

National Audit Office

22 June 2011

As part of its agenda for transforming community services, the Department of Health has supported Primary Care Trust staff joining together and leaving the NHS ('spinning out') to form social enterprises under the Right to Request Programme. In total, social enterprises formed from the Programme will be delivering around £0.9 billion of public services by the end of 2011.

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The National Audit Office study team
consisted of:

Oliver Anderson, Steve Merrifield,
Akhil Patel, Emma Taylor, Andrew Tuffin
and James Young, under the
direction of David Clarke

This report can be found on the
National Audit Office website at
www.nao.org.uk/social-enterprise-2011

For further information about the
National Audit Office please contact:

National Audit Office
Press Office
157-197 Buckingham Palace Road
Victoria
London
SW1W 9SP

Tel: 020 7798 7400

Email: enquiries@nao.gsi.gov.uk

Website: www.nao.org.uk

Twitter: @NAOorguk

Summary

1 As part of its agenda for transforming community services, the Department of Health (the Department) has supported Primary Care Trust (PCT) staff joining together and leaving the NHS ('spinning out') to form social enterprises. These have become independent bodies delivering services, previously delivered in-house, under contract to the PCT. Seven 'Pathfinder' social enterprises were spun out before 2008. Another 20 have now spun out under the Right to Request Programme (the Programme), which supports staff to apply to form a social enterprise to supply services. A further 30 are in-line to be spun out by September 2011. In total, social enterprises formed from the Programme will be delivering around £0.9 billion of public services by the end of 2011. Examples of the services they provide are at **Figure 1**.

2 Social enterprises are businesses with primarily social objectives, the surpluses from which are principally reinvested for that purpose in the business or community rather than driven by the need to maximise profits for shareholders and owners. Ownership can take many forms including conventional ownership through equity shares, mutual ownership by its staff or as a cooperative. Spin-outs from PCTs are generally Community Interest Companies owned by their staff. They are limited companies, with special additional features, created for the use of people who want to conduct a business or other activity for community benefit, and not purely for private advantage.

Figure 1
Examples of services provided by spun out social enterprises

Organisation Name	Number of staff transferred	Service Description
City Health Care Partnership	1,200	Delivers a range of services, for example, dental and GP services, sexual health, health visiting and health care services, and prisoner and offender healthcare.
Your Healthcare	502	Community focused services including inpatient and outpatient support to all age groups.
Inclusion Healthcare	6	Provides general medical and substance misuse services for homeless people and other socially excluded groups.

Source: *Relevant social enterprise*

3 The Right to Request programme is part of the wider programme to transform community services, initiated in June 2008. The transforming community services programme sought, amongst other things, to improve quality by giving greater freedom to clinical staff working in community services to innovate and lead service transformation. It required that PCTs should no longer deliver services and should separate their delivery arm from their commissioning function with delivery being provided under contract to the PCT by other bodies such as social enterprises or Foundation Trusts. By providing an option to form social enterprises, the Right to Request Programme was intended to play a part in enabling the separation of PCT provider and commissioner functions, improving efficiency and adding to the diversity of providers delivering community health services. The Department also considered that having social enterprises provide services would also be a first step in stimulating a market for community services, leading to greater patient choice, increased quality and responsiveness to patients' needs.

4 Government policy is to support social enterprises and mutuals spinning out from parts of the public sector. In 2010-11, the Office for Civil Society launched a programme supporting the spinning out of 21 'Pathfinder Mutuals'. The Government also plans to establish 'Rights to Provide' across the public sector, so that employers will be expected to accept suitable proposals from front-line staff who want to take over and run their services as social enterprises and mutuals. Ministers announced a Right to Provide scheme for staff working anywhere in the NHS and care services in March 2011. The Mutuals Taskforce have an aspiration that by 2015 one in six public servants may have formed themselves into mutuals and social enterprises to deliver public services.

5 As well as being a major programme in its own right, the Right to Request Programme will provide useful lessons for future programmes more generally. Against this background, this Report examines:

- the support provided by the Department, as well as its objectives for the Right to Request programme;
- the arrangements put in place by PCTs to ensure the delivery of services by spun out social enterprises; and
- the risks relating to achieving sustained value for money from the Programme.

As few organisations have, so far, spun out, we have drawn from our previous reports that have highlighted the risks to value for money that have to be managed as the programme progresses.

6 In examining the Programme we conducted surveys of PCTs and social enterprises. The surveys had relatively low response rates, but we followed up the issues raised in case studies. We also made direct contact about particular issues where these were significant to our findings to ensure that the findings were soundly based.

Key findings

7 It is too early to see a consistent picture of the costs and benefits that spinning out might bring. To date, only 20 Right to Request social enterprises are operational, the majority having recently launched in April 2011, and any service delivery benefits will take several years to emerge. There are, however, a number of examples where increased staff engagement and awareness of local needs from social enterprises formed earlier have delivered cost and service improvements. For example, Sandwell Community Caring Trust has made substantial savings by reducing staff sickness absences from an average of 22 days per year in 1997 to 0.34 days in 2008. As regards the costs of the programme, there is no central record and it is difficult to get accurate estimates from PCTs as most are still part way through the spinning out process. A small number of trusts told us that their costs varied from between £120,000 to £500,000, but we have no assurance that these costs are typical. In addition to the costs of PCTs, the Social Enterprise Investment Fund provided over £7 million in grants and they were supported by the Department's central unit.

8 A strong support framework in the Department of Health has been successful in generating requests from staff to form social enterprises. Key features of the framework the Department put in place to support the Right to Request are a strong policy drive to create social enterprises, a central unit regulating the Right to Request process and giving guidance and advice, and the availability of funding to assist groups in formulating their plans and to support start-up. In common with other health providers, all Right to Request social enterprises were required to demonstrate quality and productivity improvements as part of the Department's QIPP (Quality, Improvement, Productivity and Prevention) challenge. They were contracted to deliver the same savings and service improvements as those bodies remaining in the NHS. PCTs were required to assure themselves of the financial viability and sustainability of all Right to Request proposals.

9 The Department has not formulated separate objectives against which to evaluate the success of its Right to Request programme. The Right to Request Programme is a sub-set of the wider programme 'Transforming Community Services' which has objectives around promoting patient choice, separating the commissioning and provider function, empowering staff to improve patient care and providing value for money to taxpayers. The Department did not set separate objectives for the Right to Request Programme but set out in an assurance framework the tests that proposals to form social enterprises would have to meet. The Department consider that Right to Request has contributed to meeting the objectives of the Transforming Community Services programme by facilitating the separation of the PCT provider and commissioner functions, adding diversity to the providers delivering community services, enabled the driving up of clinical standards by giving greater freedom to clinical staff to innovate and lead services, improving efficiency, developing responsive services and adding diversity to the providers delivering community services. However, we found that there is currently very little hard evidence of the benefits social enterprises are delivering because they have not had time to demonstrate a track record. The Department needs to establish a framework that will enable it to evaluate the contribution that the Right to Request Programme has made.

Without separate objectives specifically attributable to Right to Request, a measurable articulation of the costs to be incurred or the benefits to be achieved, it is difficult to assess the success, or otherwise of the Programme and whether the resources devoted to the Programme are value for money.

10 PCTs approved proposals for spinning out social enterprises where enterprises promised more benefits than the alternatives but did not generally contract for them to deliver these additional benefits. PCTs evaluated staff proposals to create a social enterprise with other options such as transferring service delivery functions to Foundation Trusts or other parts of the NHS. As a minimum, social enterprises were expected to deliver the same level of savings and service improvements that parts of the NHS and other providers were required to deliver. PCTs, however, approved the spinning out of social enterprises when they considered that, compared to the alternatives, the proposed social enterprise offered the greatest benefits across a range of tests on quality, efficiency and sustainability. But, in practice, PCT commissioners did not contract social enterprises to deliver cost or service benefits beyond what the alternatives would have offered. There is a risk that if cost savings and benefits achievable through separating the commissioning function, whether the provider is a social enterprise or an alternative, are not enshrined in contracts, they will not be delivered.

11 The PCTs have retained a number of risks and liabilities that will need to be managed carefully. They include a number of risks and potential liabilities relating to the ownership of capital assets and continued cover against clinical negligence claims. And in the last resort, the PCT or its successors will be responsible for ensuring that essential services continue to be provided. At least for a time, social enterprises and other community providers are highly dependent on work and cash flow from their respective PCTs. They will also be operating in an increasingly competitive market place due to changes in health legislation, currently going through Parliament. This legislation may introduce the idea of ‘any qualified provider’ relatively early in the lives of the final wave of Right to Request spin-outs and before they become fully self sufficient.

12 PCTs or their successors will need to have a clear idea of how they will react if enterprises run into financial difficulty or fail. In common with other independent health providers, there is a risk that social enterprises might fail. Before agreeing to launch social enterprises PCTs assured themselves that the enterprises were viable businesses in the short and medium term. In the longer term, as contracts with PCTs become subject to competition, there is a risk that some enterprises will struggle to become self sustaining businesses, for example, being able to attract finance, to react to and withstand variations in demand and to compete in the market place. Whilst some social enterprises, such as Ripplez, have secured additional contracts, some pre-Right to Request spin-outs have been over-optimistic about the amount of extra work they will win in competition. The Department’s plan is for competition to take its course. Against this background, there has been no assessment of what the failure rate of enterprises will be, how this will impact on the value for money case for the Right to Request programme, or on the case for encouraging employees to take on the risk of the enterprise failing at a time when the Department has not yet settled commissioning and competition arrangements.

13 Getting sustained value for money from social enterprises will be dependent on how PCTs or their successors commission services in the future. Given the high degree of interdependency between social enterprises, PCTs and their successors, much will depend on how commissioners approach the commissioning of services from these businesses. Success will require highly developed commercial skills, for example, in how to manage the market so as to stimulate competition or encourage new providers, and how to set the tariff that providers will receive.

Conclusion on Value for Money

14 It is too early to assess the costs and benefits from the Programme as only 20 social enterprises are operational, and have not yet established a track record. The majority have only recently launched in April 2011. Nevertheless, there are a number of risks to be managed if value for money is to be achieved for the sums expended on the programme and for the £900 million contracts awarded to the enterprises non-competitively. Not setting separate objectives for the Programme makes it difficult to judge whether success and value for money is achieved. PCTs have not contracted for any benefits that social enterprises could deliver over and above what they would have required of alternatives, reducing the likelihood that such benefits will be delivered. Many risks and liabilities still reside with PCTs and will need to be managed if value for money is to be achieved. The sustainability of social enterprises is, currently, heavily dependent upon funding and cash flow from the NHS.

Recommendations

To the Department of Health and PCTs

a The Department has not set out separate, measurable objectives against which to evaluate the success of the Right to Request Programme.

The Department should put in place arrangements that enable it to evaluate whether the Programme is value for money or not, including specifying what it expects the costs and benefits of the Programme to be and what the actual cost and benefits are.

b PCTs have not generally specified in initial contracts all the benefits that social enterprises are expected to deliver. The Department and PCTs should monitor the extent to which social enterprises are able to deliver cost savings and benefits over and above the services they have contracted for and above those provided by other delivery models. They should also identify to whom these benefits are accruing.

- c PCTs have retained a number of risks and potential liabilities.** PCTs should clearly identify all risks and potential liabilities associated with individual approved proposals within the Right to Request Programme, and put in place arrangements to monitor and manage them.
- d There is a risk that some enterprises will struggle to survive when the contracts they have with PCTs are put out to competition.** The PCTs or their successors should have contingency plans on how to react in these circumstances, and should evaluate any action they take carefully to ensure that they do not infringe competition and State Aid rules.

To the Cabinet Office

- e The setting up of new mutuals created by moving out from the public sector is at an early stage.** The Cabinet Office should ensure frameworks are in place so that new and emerging mutuals and public sector commissioners have access to appropriate information and support. This should include access to information and advice on adopting good financial practices such as: having clear objectives; ensuring that the means for evaluating success are established at the outset; and ensuring that cost or service improvements are secured.

Part One

Supporting the creation of health social enterprises

1.1 This Part sets out the role of social enterprises, mutuals and cooperatives (referred to collectively as ‘social ventures’) in delivering public services. It also considers the benefits that social enterprises, in particular, can deliver, and government policy on increasing the role of these bodies in delivering public services. Finally, it examines the framework of support provided by the Department of Health (the Department) within which individual decisions are made on whether to support staff leaving the NHS (‘spinning out’) to form social enterprises to deliver services, previously delivered in-house, under contract to Primary Care Trusts (PCTs).

Characteristics of social enterprises, mutuals and cooperatives

1.2 Social enterprises, mutuals and cooperatives are not legally defined. However, the Government has defined social enterprises as “businesses with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or community, rather than being driven by the need to maximise profits for shareholders and owners.”

1.3 The terms ‘mutual’ and ‘cooperative’ refer to the ownership arrangements that may apply to a range of businesses, including social enterprises. They all, however, have common characteristics, and often have social aims at their core. Appendix Two provides further information.

There are already a number of social enterprises that have spun out of the public sector, and this is set to increase

1.4 Most social enterprises have been started up by social entrepreneurs or by groups of individuals but there has been an increasing trend for them to spin out of public sector bodies. Under this model, employees transfer out of the public sector and form an independent organisation to take over the running of services. While there is no reliable data on the number and value of organisations that have spun out of the public sector in England, they have become most established in the health and leisure and culture sectors.

1.5 The Government is committed to creating more social ventures and has recently launched a variety of initiatives to encourage the creation and expansion of social ventures delivering public services. This includes the launch of 21 'Pathfinder' mutuals many of which are being or will be run by staff formerly in the public sector who will take over delivery of public services. It is not yet clear how many of the mutuals will adopt the social enterprise model. The Mutuals Taskforce have an aspiration that by 2015 one in six public servants may have formed themselves into mutuals and social enterprises to deliver public services.

1.6 This Report focuses on the spinning out of social enterprises from PCTs, since this is the largest established programme for the formation of social enterprises to date.

Objectives of delivering health services through social enterprises

1.7 The Department aims 'to create the largest and most vibrant social enterprise sector in the world'¹. It considers the benefits of social enterprises to include:

- improving local services;
- empowering staff;
- enabling decision-making to take place at local level;
- enhancing the quality of health and social care provision;
- ensuring services are tailored to local needs;
- contributing to the wider regeneration of communities;
- boosting social inclusion; and
- tackling unmet need, delivering services to communities that often receive little or no support.

The Department has not indicated which, if any, of these benefits are unique to social enterprises but many are also a feature of other delivery models. At a local level, in common with other health providers, all Right to Request social enterprises must demonstrate quality and productivity improvements as part of the Department's QIPP (Quality, Improvement, Productivity and Prevention) challenge. PCTs must also assure themselves of the financial viability and sustainability of all Right to Request proposals.

¹ Department of Health, *Equity and excellence: Liberating the NHS*, Cm 7881, July 2010.

The policy context

1.8 In recent years there has been a clear policy drive within the NHS for the creation of social enterprises as part of a wider programme to transform community services which aims to generate greater competition and choice in the provision of health services, separate PCTs' commissioning and provider functions and empower staff to improve patient care. In 2006, the Government set out plans for changes to the way that care is delivered in England. This involved increasing patients' choice, as well as the delivery of more integrated services by a range of organisations, including social enterprises.² In 2008, *Lord Darzi's NHS Next Stage Review* included recommendations to create new social enterprises to deliver primary and community services, and a commitment that NHS employees were to be given a 'Right to Request' to set up these organisations to deliver services.³ Under these arrangements, PCTs are obliged to consider, but not necessarily agree to, such requests.

1.9 Under the terms of the Department's revised national operating framework for 2010-11, all PCTs are to achieve full separation of commissioner and provider roles by April 2011 or, where a new organisation is being created, to have made substantial progress based on agreed plans.⁴ In achieving this split, Trusts had to consider which delivery model for community services, including social enterprises, best met the needs of service users across a range of tests on quality, efficiency and sustainability.

Support arrangements

1.10 In 2006, the Department launched its Social Enterprise Pathfinder Programme and established a Social Enterprise Unit to coordinate policy on social enterprises and to ensure that a network of support was in place to encourage their wider use in health and social care. The Unit offers support and guidance to those PCTs and staff wishing to spin out. For example, it developed guidance on the assurance and approval process to be followed under the Right to Request Programme from the point at which staff make their initial request to the launch of the enterprise.

1.11 Staff establishing these enterprises are able to apply for financial support to help them develop their plans and to apply for start-up funding from a range of sources. These sources include: the Social Enterprise Investment Fund, provided by the Department and managed on its behalf by the Social Investment Business in partnership with Local Partnerships; bodies such as Capacity Builders (a non-departmental public body which leads government investment in support services for charities, voluntary groups and social enterprises); and the parent PCT.

2 Department of Health, *Our health, our care, our say: a new direction for community services*, Cm 6737, January 2006.

3 Department of Health, *High Quality Care For All: NHS Next Stage Review Final Report*, Cm 7432, June 2008.

4 Department of Health, *Revision to The Operating Framework for the NHS in England 2010/11*, June 2010.

1.12 The Social Enterprise Investment Fund provides advice and funding for enterprises that are starting up. It also offers development investments, including loans for established social enterprises delivering health and social care services. The Department has allocated £100 million to the Fund to be disbursed between April 2007 and May 2012. As at 31 March 2011, the Fund had provided funding totalling over £80 million, of which £8.3 million was to 51 applicants in the process of spinning out under the Right to Request Programme.

1.13 Within the overall funding available to them, social enterprises including NHS organisations eligible under the Right to Request Programme and whose PCT boards have approved their proposals can apply to the Fund for grants to obtain specialist advice on, for example, legal, business consultancy, corporate finance and accounting, tax, VAT, learning and development issues. By 31 March 2011, Fund administrators had approved grants to Right to Request applicants totalling £6.3 million for these purposes. Staff at the Social Investment Business told us that individual social enterprises often need similar types of specialist advice. This was supported by findings from our survey of social enterprises. For example, each of the six enterprises responding to our survey had commissioned external assistance about managing issues relating to pensions, while assistance about contract drafting and negotiation, and TUPE issues had been commissioned by five and four social enterprises respectively.

1.14 A wide range of other national and regional bodies offer direct support. These include the Social Enterprise Coalition, which provides best practice guidance and training, and informs government policy in this area, and Local Partnerships, which provides investment appraisal and support for service transformation. Other bodies active in supporting civil society, such as the New Economics Foundation and umbrella bodies representing voluntary and local organisations, provide indirect support such as access to support networks and research on social enterprise.

1.15 The policy framework, together with the support arrangements in place, have been successful in encouraging applicants from the health sector to come forward. Prior to 2008, seven social enterprises spun out of PCTs. Since the launch in 2008 of the Right to Request Programme the number of emerging health sector spin-outs has grown. As at November 2010, there were 60 projects within the Programme, of which ten subsequently dropped out either because the PCT determined it as not financially viable, a lack of staff support or funding issues. By January 2011, four had launched, by the end of April 2011 a further 14 and by June 2011 a further two. The Department expects that the remaining 30 projects will be running by September 2011. Once fully operational, the Department estimates that the Programme will account for some £886 million of community services annually and involve the transfer of 24,000 NHS employees to independent enterprises, around 10 per cent of staff previously employed by PCTs. The Programme has now closed to new applicants.

Objectives of the Right to Request Programme

1.16 The Right to Request Programme was launched as part of the NHS Next Stage Review in June 2008, and was a sub-set of the Transforming Community Services programme. The rationale for the Transforming Community Services programme were articulated in the *NHS Next Stage Review Final Report* and included driving up quality by giving greater freedom to clinical staff working in community services to innovate and lead service transformation. Within the context of the wider Transforming Community Services programme, the Right to Request Programme facilitated the separation of PCT provider and commissioner functions, and added to the diversity of providers delivering community health services. In addition to the objectives around quality, clinical autonomy and separation of functions, the Right to Request Programme was also (alongside limited competitive tendering) a first step in stimulating a market for community services, leading to greater patient choice (a further objective of the NHS Next Stage Review) and increased quality (including responsiveness to patients' needs). Against this context, the Department considers that the Right to Request Programme has contributed to achieving the wider objectives of the Transforming Community Services programme, as evidenced by the significant proportion of community health services that have, or will, transfer to the social enterprise sector, estimated current value of this £900 million representing around 10 per cent of community health spend.

1.17 The Department has not established separate objectives for the Right to Request Programme against which to evaluate success, although it has set out in guidance some of the benefits that social enterprises might provide. The decision to support proposals is taken at a local level by the PCT. The Department considered that having top down, target driven objectives would contradict this approach. Without objectives or a measurable articulation of the costs to be incurred or the benefits to be achieved, it is difficult to assess the success, or otherwise of the Programme and whether the resources devoted to the Programme are value for money.

1.18 There remain risks to value for money from not having sufficiently specific objectives for programmes of expenditure against which to assess whether funds have been used effectively. We have previously pointed to similar failings in other government sectors. For example, in our report on BBC estates, we noted that the BBC had not set out the intended benefits of its estates projects at the outset with sufficient clarity to provide a basis for a meaningful measurement of subsequent achievements.⁵

⁵ *The BBC's management of three major estates projects*, National Audit Office, January 2010.

Evaluation arrangements are lacking

1.19 The lack of separate objectives will seriously impede the Department's future ability to arrive at meaningful assessments of the success of the Right to Request Programme. The Department has commissioned the Social Enterprise Coalition to evaluate the Right to Request process and the support provided, and to report its findings in April 2011. It has also commissioned an evaluation of the Social Enterprise Investment Fund over a two-year period from 2009. The Department told us, however, that it currently has no arrangements in place to evaluate the benefits delivered by the Programme since currently so few businesses are established.

1.20 Good practice suggests that departments should have detailed evaluation plans in place from the outset to ensure that all stakeholders such as PCTs and social enterprises are clear about when and what information is required to be collected and how this is to be achieved. Departments also need to establish effective mechanisms for learning, disseminating and applying lessons from a range of individual evaluation reports. To enable shared learning, the Department provides learning events and an online network for staff involved in the Right to Request.

Part Two

The process of spinning out

2.1 This Part sets out the process by which PCTs spin out services. It examines whether the stated benefits of social enterprise are being prioritised and contracted for. It also examines the treatment of assets and liabilities when social enterprises spin out.

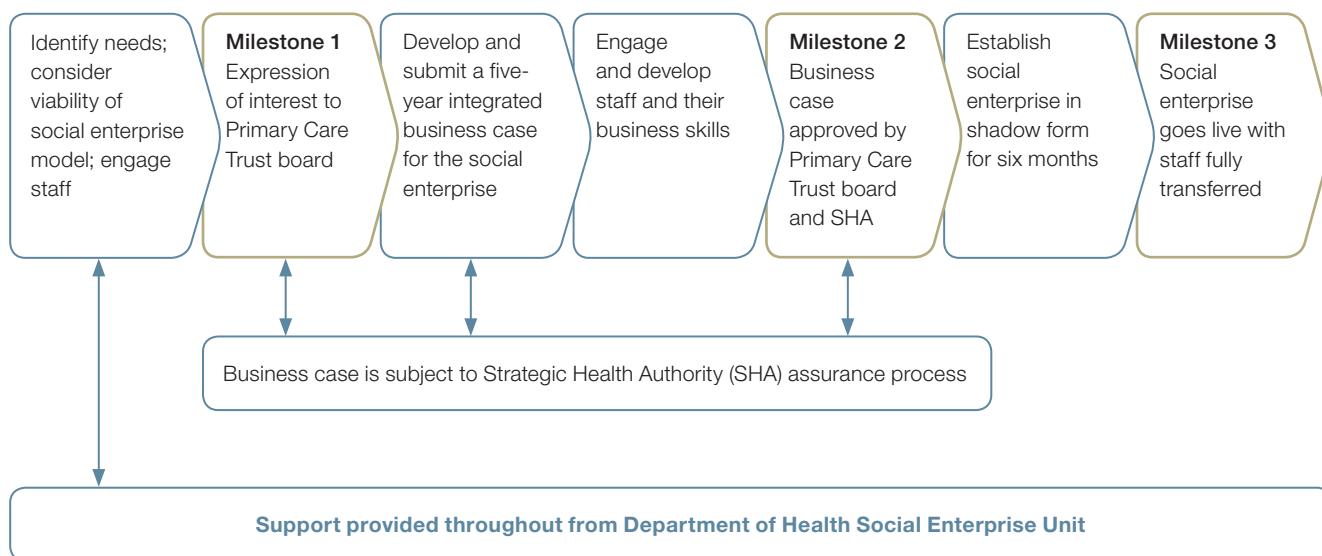
The process for spinning out to a social enterprise

2.2 The decision to spin out has been taken by PCTs in two main stages. These are, a review examining how all their services could best be delivered in the light of the requirement to split the commissioning and delivery functions; and, consideration of proposals from staff exercising the Right to Request option (paragraph 1.8).

2.3 The Right to Request process begins with social enterprise being identified as a possible organisational form to deliver community services. An initial period of staff consultation is followed by three key milestones set out in **Figure 2**. At Milestone 1 the prospective organisation, which can vary in size from small groups of clinicians to large provider organisations, submits an expression of interest to the PCT board. The majority of Right to Request projects have been led by groups of clinicians. Of the 50 Right to Request projects, 22 involve less than 50 members of staff.

2.4 After consideration of the case for a social enterprise by the PCT Board, the Strategic Health Authority conducts its own assurance review of the initial business case to examine whether the proposed organisational form will offer sufficient quality, efficiency and sustainability, and that these benefits are appropriately evidenced by the PCT. On approval by the Trust board and endorsement by the Strategic Health Authority, the prospective organisation develops a five-year integrated business case, engages with staff and wider stakeholders, and develops its business skills. At Milestone 2, the integrated business plan requires approval by the PCT's board and the Strategic Health Authority. The business is then established in a shadow form for approximately six months before, at Milestone 3, it goes live with staff fully transferred.

Figure 2
Right to Request process



Source: Department of Health

Options appraisal process

2.5 In total, ten out of 11 of the PCTs that responded to our survey had conducted some form of option appraisal of alternative organisational models, but had not in every case considered all potential alternatives. The Department's Transforming Community Services Assurance and Approvals process⁶ encouraged PCTs to consider organisational forms which achieve the best match for individual services with local commissioning priorities. It listed the most likely organisational forms as being:

- integration with an NHS acute or mental health provider;
- integration with another community based provider; and
- social enterprise.

2.6 The Department considers the following further alternative options to be less typical:

- Community Foundation Trust;
- continued PCT direct provision; and
- Care Trust.

⁶ Department of Health, *Transferring Community Services: The assurance and approvals process for PCT-provided community services*, February 2010, p. 4.

2.7 While the options set out by the Department were not intended to be exhaustive or prescriptive the guidance did, in effect, steer some PCTs towards using a social enterprise model. The Department told us Right to Request proposals took precedence over other models to provide protection for staff groups that may otherwise have been ignored.

The objectives are not prioritised and contracts do not mandate greater levels of efficiency than would have been required of alternative providers

2.8 PCTs have access to a large volume of guidance that sets out the stated benefits of the social enterprise model, but these are not prioritised into clear, quantified objectives. The Department's view was that PCTs could approve the spinning out of social enterprise if that enterprise offered at least as good levels of service and cost effectiveness. In practice, PCTs approved the social enterprise model where it offered greater levels of efficiency over alternative organisational forms (paragraph 2.5). The Department considers that there should be no requirement to secure through contracts the additional benefits that social enterprises, when compared to alternative providers, might generate as they will be driven by the local community and the social aims of the enterprise. The Department told us that its QIPP challenge (paragraph 1.7) requires social enterprises, in common with other providers, to make minimum cost savings and service improvements.

2.9 The Right to Request Programme's lack of separate objectives has had implications for how PCTs contract with social enterprises. For example, in our survey, PCTs considered the most important objectives of the spin out to be, in ten out of 11 cases, 'maintaining service provision' and, in seven out of 11 cases, both 'complying with the Right to Request policy' and 'increasing the involvement of service users'. The objective 'to reduce costs' was amongst the least commonly cited as 'critical' or 'very important' (in three out of 11 cases). This contrasts with our survey of local authorities operating in the leisure and culture sectors which cited 'to reduce costs', 'improving value for money' and 'innovation' as being most important (in four out of five cases).

2.10 The contrasting priority given to cost saving objectives, for example, is reflected in the contractual arrangements between the social enterprises and their parent bodies. For example, the leisure enterprise Link4Life was contracted by Rochdale Metropolitan Borough Council to deliver explicit efficiency targets beyond levels expected had provision remained in the public sector. In contrast, Right to Request spin-outs are not contractually required to deliver any greater cost savings than alternative providers.

2.11 In common with other independent health providers, Right to Request spin-outs are contracted to deliver efficiency savings in line with those required of the PCT (a minimum of 3 per cent). However, they incur higher rates of, for example, VAT and corporation tax, which therefore require them to deliver additional savings relative to in-house arrangements. There are generally provisions in the contract that after a

three-year protected period an increasing proportion of their services may be subject to competition. In contrast, we found that most leisure social enterprises have contracts that reflect lower funding levels from their parent bodies assuming that additional cost savings and efficiencies will be made compared to expectations for in-house provision.

In most cases social enterprises have not been required by their contracts to deliver additional service improvements

2.12 PCT commissioners chose the social enterprise model over alternative organisational forms (paragraph 2.5) on the basis it can deliver additional service improvements other forms cannot. In most instances, the PCTs are not then contractually requiring delivery of these additional service improvements. The Department does not expect PCT commissioners to secure from social enterprises additional services compared to those expected from alternative providers in the public sector, unless contracted to do so. It is the Department's policy to extend choice of suppliers and they consider that it would be unfair to require social enterprises to demonstrate efficiency gains or service improvements not required of other providers. While there are instances of PCTs requiring social enterprises to deliver additional service improvements, generally there is no contractual requirement for additional services.

2.13 Eight of the nine PCTs that we examined that were participating in the Right to Request Programme were planning, or had in place, contracts with social enterprises which did not require service improvements above those that would have been expected of alternative providers. For example, Suffolk PCT did not view the delivery of improved levels of service as the main driver of the Right to Request. It expects its social enterprise to deliver service improvement in line with other service providers. The exception, Salford PCT, plans to pay extra to a forthcoming spin out to introduce and develop additional quality improvements. This Trust has also required Salford Health Matters (a pre-Right to Request social enterprise we examined) to deliver greater service improvements than equivalent public sector providers, for example, by providing improved access to health services such as evening and Saturday surgeries.

2.14 Health commissioners in England have used the Commissioning for Quality and Innovation payment framework to encourage quality improvements by linking part of a social enterprise's income to achievement of local quality improvement goals. These improvements can sometimes see services redesigned and delivered in a different way. For example, North East Lincolnshire PCT is planning a spin out to provide older people's Mental Health Services under a model where dementia care is provided within an individual's own home for as long as possible, rather than through admission to a unit. This is designed to benefit the patient by providing them with care in a familiar environment, and increase efficiency by making better use of unit specialist staff and reducing the use of hospital beds.

Sometimes the way contracts are specified may militate against the achievement of some benefits that social enterprises bring

2.15 Securing the benefits that social enterprises are expected to deliver will require highly skilled commissioners. The benefits of the model will not be fully achieved unless they are explicitly contracted for, and doing this is still a relatively underdeveloped skill. It is made more complicated by the need to balance different objectives in a climate of cost reduction. For example, objectives to deliver services at a lower cost may conflict with objectives that require delivery of a broader range of services. It is also clear that existing ways of specifying service delivery may restrict the flexibility for delivering other benefits.

2.16 PCT contracts with Right to Request spin-outs include a range of requirements from specifications in terms of outputs, for example, the average length of patient stay, block contracts⁷, and outcome targets, such as reducing hospital admissions. Excessive use of output specifications, however, can restrict freedom to deliver services in an innovative way. One enterprise we interviewed has to meet 486 separate output targets in a single contract. These serve to mandate the way an outcome is delivered by way of a succession of prescribed steps.

2.17 Some parent bodies are seeking better ways of specifying and measuring what social enterprises should deliver. One organisation we interviewed, Your Healthcare, has a combination of output, block contract and quality targets. For forthcoming spin-outs, one approach would be for parent bodies to specify fewer outputs, such as average length of patient stay, and identify more outcomes, for example, reducing hospital admissions. This would allow the organisation more flexibility in deciding how it would deliver those outcomes.

2.18 The Department is intending to move to a system where any qualified provider will be able to register to supply services rather like on a call-off contract. There will, therefore, be common tariffs and quality targets and competition will be about which services individuals choose to use. However, none of this is yet decided.

No health social enterprises have spun out owning significant assets

2.19 To date, no health social enterprises have spun out owning significant assets. PCTs retain ownership of all major assets such as land and buildings. Trusts have in place a range of lease arrangements for the use of assets by social enterprises. For example, in our survey, Trusts indicated that land and buildings are typically leased at either market or preferential rates, which equate to the capital charge incurred by the parent body. In some cases the assets are owned and managed in the same way as before. The organisation is not charged but told of a notional rent so that it could take this amount into account if it bids for other work on a full-cost basis.

⁷ A block contract is a contract with a fixed cost, regardless of the number of patients treated.

2.20 Because the NHS property arrangements are very complex, careful due diligence is required. We found in some cases that the lease arrangements can be numerous and complex to negotiate. For example, Hull PCT has 19 separate lease and sub-lease agreements in place with City Health Care Partnership. We also found in the case of one pre-Right to Request enterprise occupying accommodation on three sites that some leasing and maintenance arrangements remain to be resolved some three years after spinning out.

2.21 The arrangements in place to govern use of equipment range from commercial rates to no charge. For those PCTs responding to our survey, the leasing arrangements for equipment such as beds and medical equipment varied from commercial leases between the social enterprise and parent body or separate company, to the transfer of small items with no book value for a nominal fee. For example, Central Surrey Health is part of a consortium led by Surrey PCT and Surrey County Council with a contract for the provision of patient equipment with a commercial provider. The parent body, Surrey PCT, gave small items with no book value, such as blood pressure machines and scales, to the enterprise.

2.22 Surveyed PCTs tended to allow their respective spin-outs to use IT equipment for no charge. Furthermore, the PCTs had agreed to bear the cost of replacing IT that reaches the end of its useful life. This is not the case in every instance. For example, Central Surrey Health social enterprise does not lease IT from Surrey PCT. It bears the cost for its IT systems and for replacing equipment.

It is too early to estimate the costs of spinning out

2.23 There are costs of spinning out including staff costs incurred in managing the spin out and social enterprise investment funding (paragraph 1.12). Our survey found in some cases that because the business is not yet operational, the PCT had yet to finalise the costs to it of spinning out. In other cases, the PCTs were able to provide estimates of the cost of each spin out ranging from £120,000 to £500,000. There is no central estimate of the costs of the Programme.

Liabilities retained and transferred to the social enterprise are neither quantified nor documented systematically by PCTs

2.24 PCTs with active spin-outs have varying degrees of clear sight over which liabilities have been retained and which have been transferred as part of the spin-out. For example, Hull PCT has a Business Transfer Agreement which sets out, at a high-level, transfer arrangements and associated legal principles governing those transfers. It also has a working paper that quantifies assets and liabilities that have been transferred to the social enterprise.

2.25 We have previously reported that public bodies transacting with non-public sector organisations have sometimes been unable to supply bidders with adequate records of assets and liabilities, for example, in the case of the New Millennium Experience Company, which negatively affected the levels of competition for the contract and reduced the likelihood of achieving the best value for money.⁸

⁸ Comptroller & Auditor General, *English Partnerships: Regeneration of the Millennium Dome and Associated Land*, Session 2004-2005, HC 178, National Audit Office, January 2005.

Part Three

Managing the longer-term outcomes

3.1 This Part sets out the emerging benefits of social enterprises and examines some of the issues and challenges that need managing to help secure the longer-term outcomes.

It is too soon to see widespread evidence of benefits from spun out social enterprises

3.2 Many of the benefits PCTs hope to capture from spinning out take a long time to emerge, and so in order to realise them commissioners will need to carefully manage the longer-term risks to value for money. We found it is too early to draw conclusions from our survey of spun out organisations on the benefits they are delivering. However, some of the emerging benefits from spinning out, in the health and social care sector, have previously been highlighted by representative bodies such as the Social Enterprise Coalition, but are unaudited by us. These include:

- **Innovative service delivery:** for example, Central Surrey Health is streamlining and coordinating clinical services to give patients a more integrated experience either in community settings or in their own homes.
- **Providing a wider range of services:** for example, Local Care Direct based in West Yorkshire delivers additional services including: a Safe Haven service for patients removed from mainstream primary care; in-hours cover for GP practices in crisis; and, primary care streaming to support Accident and Emergency departments.
- **Efficiency savings:** for example, Sandwell Community Caring Trust made substantial savings from reduced staff absence with a reduction in sickness levels from an average of 22 days a year in 1997 to 0.34 days in 2008.

It is difficult to measure or specify some of the benefits social enterprises are expected to bring

3.3 There is a risk to establishing whether value for money has been achieved as many of the benefits that social enterprises are expected to deliver, such as increased wider social impacts, are difficult to measure. Commissioners will need to find ways of ensuring that less easily measurable benefits are delivered, and of specifying outcomes or outputs in ways which encourage innovation and cost-effective delivery.

3.4 The Department does not require social enterprises to deliver more than other providers, but some PCTs have attempted to develop key performance indicators to try and capture data on the wider benefits social enterprises provide. So far, however, these are relatively underdeveloped. Organisations that we interviewed also said that techniques to capture wider benefits were at an early stage of development.

3.5 To date, there have been several different ways of measuring such benefits. One recognised approach that has been developed and has been used by a number of civil society organisations is Social Return on Investment. This approach is similar to cost-benefit analysis, but focuses on the benefits as assessed by stakeholders. Results are expressed in terms of a ratio of savings to cost, for example, that for every £1 spent there was £6 of benefit or cost saving. Some organisations, however, find the methodology time consuming to apply and there are limits to how the results of the methodology can be used, for example, it is not appropriate for comparing the Social Return on Investment of different organisations.

3.6 It will become increasingly important to be able to demonstrate the benefits social enterprise can deliver. The health market is opening up and becoming more attractive to the commercial sector with the Department's introduction of the 'Any Qualified Provider' model⁹, aimed at increasing access and choice for service users. Enterprises we spoke to recognise the importance of being able to demonstrate the wider benefits of their work in order to win new business in this increasingly competitive environment, particularly with the advent of commissioning consortia.

Significant risks and liabilities are retained and need managing

3.7 Ultimately, it is the PCT that bears the risks and liabilities if any provider organisation, including social enterprises, fails or performs badly and this needs carefully managing. The PCT is responsible for ensuring that services continue and would have to find an alternative provider, as happened in the case of a failed social enterprise in Wandsworth (**Figure 3**). With the abolition of PCTs, from April 2013, primary responsibility for continuity of service will pass to commissioning consortia.

Spun out social enterprises are dependent on PCTs

3.8 A further risk that needs managing to secure longer-term benefits is that for at least an initial period, social enterprises, like other providers, will be almost entirely dependent on the contract and associated funding provided by the PCT. As noted at paragraph 2.19, to date, no organisation has spun out of a PCT with major fixed assets. Spinning out without estate assets and a lack of trading track record reduces the ability of Right to Request social enterprises to secure funding from financial institutions and, consequently, increases their dependence on commissioners in terms of cash flow.

⁹ The Any Qualified Provider model means that any local healthcare provider meeting minimum quality standards and able to offer a particular service at a particular price can be considered as a provider of that service. The model began phasing in for community services from April 2011.

Figure 3

Example of a failed social enterprise

Secure Healthcare Limited

In 2007, Secure Healthcare Limited, a spin out from Wandsworth PCT, became the provider of healthcare services for Wandsworth Prison. In September 2009, after experiencing cash flow problems the business went into voluntary liquidation. Wandsworth Community Services, the provider arm of the PCT, stepped in to transfer the staff back into the NHS and to ensure the continued provision of health services for the prisoners until a longer-term solution is found.

Source: National Audit Office

3.9 The lack of significant assets also puts into question whether, when the initial service contract ends, the enterprise will be able to compete on an equal footing with other semi-independent bodies, such as Foundation Trusts that own their assets. The Department told us that this should not be such an issue in future as many providers of community services do not require major estate assets and under any qualified provider providers will compete on quality.

3.10 In contrast, leisure organisations spinning out of local authorities often have a range of assets transferred to them. These assets can include land and buildings, equipment (IT or otherwise), and fixtures and fittings, as well as intangibles such as licences and intellectual property. Enterprises we surveyed indicated that the value of these assets can range from less than £10,000 to in excess of £10 million.

The ability of the spin-outs to be self sufficient businesses in the medium and longer term

3.11 As part of the process of spinning out, PCTs assured themselves that the proposed social enterprises were viable in the short and medium term (the medium term being three to five years). The PCTs scrutinised business plans and other documents which set out the enterprise's market assessment, their competitive position and how they would respond to competition. Most enterprises planned to win new business, but in practice the main part of business would still come from the PCT or its successor commissioning body. In the future, the Department expects patient choice will mainly determine demand for provider services.

3.12 Ultimately the enterprises will need to become self sustaining businesses with the ability to attract outside sources of finance, the ability to compete in a competitive market place and the ability to react to variations in demand. The Department has no view as to how this should happen as it would be up to the individual enterprise to react in the market.

3.13 There is a risk that the initial expectations for future growth and income of spinning out are unrealistic, thereby increasing social enterprises' dependence on income from PCTs – although some enterprises, such as Ripplez, have secured additional contracts. The evaluation of the Department's Social Enterprise Pathfinder Programme¹⁰ found just three of the 26 pathfinders reported an increase in income as expected, and several had not yet won contracts as anticipated. This was largely due to the timescales involved in securing contracts caused by delays resulting from changes faced by PCTs and the time taken to set up and establish the business so it is ready to deliver services.

3.14 In a keen, competitive market it is likely that some of the service providers, including new social enterprises, will prosper and some will struggle. In such circumstances it will be important that the commissioning body has a clear idea of how it will operate when faced with the possibility of a social enterprise failing. In addition to having arrangements where they get an early indication that problems are occurring they will need to have contingency plans setting out how they would react if failure is threatened or occurs. In particular, the commissioners should evaluate carefully any action they take with a struggling enterprise to ensure that they do not contravene competition or State Aid rules.

3.15 There has been no assessment of what the failure rate of providers will be, how this will impact on the value for money case for the Right to Request Programme or on the case for encouraging employees to take on the risk of the enterprise failing at a time when the Department has not yet settled commissioning and competition arrangements.

Responsibility for managing the long-term outcomes rests with commissioners

3.16 The dependence of spun out organisations, in common with other providers, on PCTs and the fact that the PCTs will be the dominant source of work (effectively they are the market) means that much of the responsibility for managing the long-term outcomes rests with commissioners. Securing the benefits from spinning out will require highly skilled commissioners. Under any qualified provider the success of providers will be influenced by a number of factors including: patient choice; the capacity of the social enterprise to grow; and, the skills of commissioners in contracting with providers on behalf of patients. In order to secure quality and value for money services commissioners will need to be skilled in specifying care pathways using an outcomes focus; tariff setting that considers the viability of providers; and, stimulating the market to provide choice for patients.

¹⁰ Department of Health, *Social Enterprise Pathfinder Programme Evaluation Final Report*, September 2009.

3.17 As the market is relatively undeveloped, commissioners will have to be clear about the extent to which they wish to promote the sustainability of the public sector spin-outs. In future, this is likely to be of increasing concern as the Government plans, for the first time, that the health sector will be subject to competition law under planned changes in the legislation. The role of Monitor, which currently regulates foundation trusts, will change and it will become the regulator of the NHS, including having responsibility for applying competition law and acting against anti-competitive behaviour by providers or commissioners.

3.18 There is a risk to value for money where barriers to competition arise meaning service users may experience less choice and quality. The Office of Fair Trading¹¹ has previously highlighted some of the barriers to competition that commissioners need to manage. These include:

- Differences in costs or other parameters of competition which arise solely from differences in ownership or control, such as differences in tax treatment, access to NHS staff pensions and insurance cover or major assets.
- Incumbency advantages enjoyed by existing organisations (usually public sector owned), such as access to information.

3.19 The comparatively short length of contracts under Right to Request places the sustainability of spun out social enterprises at risk. Both PCTs and social enterprises we interviewed thought that three- and five-year contracts were not long enough to enable them to get sufficiently established to become sustainable by securing additional sources of income and be able to compete on an equal footing with other providers. The Social Enterprise Coalition thought that contracts need to be long enough to get sufficiently established to become sustainable, ideally a minimum of three years but longer depending on the type of service. In contrast, leisure sector organisations have spun out of local authorities mostly with longer contracts, ranging from seven to 25 years, allowing more time for them to become sustainable. Guidance from the Social Enterprise Coalition and Hempsons Solicitors indicates that contracts should be of an appropriate length to allow the enterprise the opportunity to innovate and develop the business.¹² The extended time needed to develop was also a finding of the Pathfinder programme evaluation.

¹¹ *Competition in mixed markets: ensuring competitive neutrality, A working paper*, OFT 1242, Office of Fair Trading, July 2010.

¹² *Healthy Business a guide to social enterprise in health and social care*, Social Enterprise Coalition and Hempsons, 2008.

3.20 In common with other providers, there are potential risks to the longer-term sustainability of Right to Request social enterprises and their ability to deliver outcomes given the pace and depth of change in the health and social care sector, and the tensions resulting from competing initiatives. For example, the Department wants more social enterprises to provide services and in parallel is supporting more choice and competition by allowing any qualified provider into the market. This means newly spun out organisations will be operating in markets where there are no longer guaranteed contracts and will potentially be competing with more experienced commercially minded businesses. The Department expects that the wealth of experience newly created social enterprises have in the sector and their existing relationships with their patients, as the incumbent provider, will to some degree mitigate the risks to sustainability.

Appendix One

Methodology

1 The main elements of our fieldwork took place between November 2010 and January 2011. Our research methods were:

Method

1 Survey of commissioners and social enterprise organisations – We conducted a web survey of all PCTs involved in spinning out social enterprises (11 out of 55 responded, giving a 20 per cent response rate) and associated social enterprises that had spun out (6 out of 11 responded, giving a 55 per cent response rate).¹

Web survey of all Local Authorities (24 out of 349 responded giving a response rate of 7 per cent) and associated leisure and culture social enterprises that had spun out (18 out of 76 responded giving a response rate of 24 per cent).

We followed up responses in greater depth through face-to-face and telephone interviews.

2 Interviews – We conducted semi-structured interviews with representatives of around 20 organisations including commissioners and social enterprises, the Cabinet Office and Department of Health, and third parties working with social enterprises and mutuals in the delivery of public services.

Purpose

To evaluate the extent to which services are being spun out in the Health, and Leisure and Culture sectors.

To examine from the perspectives of both commissioner and social enterprise, the contractual and monitoring arrangements in place for services spun out, and the main challenges and critical success factors.

To establish the views of commissioners and social enterprises on the spinning out process, and gain a Department and government wide strategic perspective.

To gather evidence on the types of arrangements in place for services spun out, and the main challenges and critical success factors.

To establish the views of third parties who work with social enterprises.

Method

3 Case-studies – We conducted six case-studies (four health and two leisure and culture) of spun-out social enterprises and their associated commissioning body. We selected four of the more established social enterprises and two of the first Right to Request social enterprise that launched.

4 Document review – We analysed strategy documents, contracts and minutes from decision-making groups, of commissioners, Cabinet Office and the Department of Health.

Purpose

To provide specific examples of the spinning out process and to examine in greater detail the arrangements in place, challenges and critical success factors.

To inform our understanding of the strategic objectives of spinning out and, more specifically, how these objectives are articulated in individual contractual arrangements.

NOTE

1 Some PCTs have not advanced sufficiently in the Right to Request process to have established a social enterprise to contact.

Appendix Two

Definition of social enterprises, mutuals and cooperatives

1 **Figure 4** describes some of the characteristics of social enterprises, mutuals and cooperatives and paragraphs 2 to 4 set out formal definitions.

Social enterprise

2 There is no legal definition of social enterprises and, in practice, they encompass a wide range of different organisations. The Government has defined social enterprises as “businesses with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or community, rather than being driven by the need to maximise profits for shareholders and owners.” There are no hard and fast rules about how much of its profits a business needs to reinvest in its social aims to qualify as a social enterprise. However, to qualify for the ‘Social Enterprise Mark’ – an accreditation scheme run by the Social Enterprise Coalition – a business needs to reinvest more than 50 per cent of its profits in its social purpose. Ownership of social enterprises can also take several forms, ranging from a company with share equity to companies owned by their staff in the form of mutuals or cooperatives.

Figure 4
Characteristics of social enterprise, mutuals and cooperatives

Organisation Type	Aim	Ownership	Legal Form
Social enterprise	Social	Service users/ employees/other stakeholders as shareholders/ members	Various including Company Limited by Guarantee, Community Interest Company and Industrial and Provident Society
Mutual	Community/ social	Service users/ employees as members	Various (as above)
Cooperative	Social/economic/ cultural	Service users/ employees as members	Industrial and Provident Society or Community Benefit Society

Source: National Audit Office

Mutuals

3 The defining features of mutual organisations are that they are owned by, and run in, the interests of existing members, as in the case of employee- or user-owned cooperatives, or they are owned on behalf of the wider community and run in the interests of that community. Often the individual member has no right to share in the underlying value of the business.

Cooperatives

4 Cooperatives can take many legal forms, but ultimately are employee and/or user-owned organisations that operate according to specific, well-established principles such as equal participation or democracy. They are defined by the International Cooperative Alliance as being “an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly owned and democratically controlled enterprise.”



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