



National Audit Office

Report

by the Comptroller
and Auditor General

Department for Work & Pensions

Contracted-out health and disability assessments

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National Audit Office

Department for Work & Pensions

Contracted-out health and disability assessments

Report by the Comptroller and Auditor General

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Sir Amyas Morse KCB
Comptroller and Auditor General
National Audit Office

5 January 2016

This report examines whether the Department for Work & Pensions has achieved value for money in its management of contracted-out health and disability assessments.

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Key facts

7m

expected contracted-out health and disability assessments over three years, 2015 to 2018

£1.6bn

estimated cost of contracted-out health and disability assessments over three years, 2015 to 2018

13%

proportion of ESA and PIP targets met for assessment report quality meeting contractual standard (September 2014 to August 2015)

- 6** main contracts for assessments: two consecutive Employment and Support Allowance (ESA) contracts, three concurrent Personal Independence Payment (PIP), and one Fit for Work (FFW)
- 5.5 million** assessments completed in five years up to March 2015
- 65%** estimated increase in average cost per ESA assessment based on published information after transfer of the service in 2015 (from £115 to £190)
- 84%** estimated increase in total healthcare professionals required from 2,200 in May 2015 to 4,050 in November 2016
- 4** average weeks providers took to return PIP assessments in August 2015, compared with 29 weeks in mid-2014
- £92 billion** expected incapacity and disability benefit spending over three years 2015 to 2018
- £0.4 billion** latest expected reduction in annual disability benefit spending – Personal Independence Payment and Disability Living Allowance – between 2015-16 (£16.2 billion) and 2018-19 (£15.8 billion)

Summary

1 The Department for Work & Pensions (the Department) uses health and disability assessments to inform its decisions about benefits or to help people on sick leave back to work. A healthcare professional will evaluate an individual's needs and capabilities against defined criteria by reviewing relevant evidence and often conducting a face-to-face assessment or telephone discussion. The Department uses assessments for three main purposes:

- **Employment and Support Allowance (ESA)**

During 2014-15, 700,000 people made a claim for ESA because they were unable to work for health or disability reasons. The Department uses assessments to help decide if people are fit for work or assign them to groups that will offer support or help them back into work. In 2014-15, it spent £13 billion on ESA, which 2.2 million people were claiming in March 2015.

- **Personal Independence Payment (PIP)**

During 2014-15, 526,000 people made a claim for PIP to help them with daily living or mobility costs associated with living with a disability. PIP is expanding as it replaces Disability Living Allowance, and in 2014-15, the Department spent £15 billion on the two benefits which 3.4 million were claiming in March 2015.

- **Fit for Work (FFW)**

In December 2014, the Department introduced a new, voluntary occupational health assessment and advice service for individuals on long-term sick leave. The Department hopes to reduce sickness absence and its associated costs by paying for this voluntary service.

2 Health and disability assessments are central to the Department's welfare reform programme. The Department recently announced its intention to encourage people into work through ESA assessments better identifying claimants' capabilities and by continuing to roll out FFW. By better matching support to people's needs it now expects to reduce disability benefit spending – PIP and DLA – by £0.4 billion from £16.2 billion in 2015-16 to £15.8 billion in 2018-19.

3 For many years the Department has contracted-out most assessments to third-party providers: Atos Healthcare (Atos), Capita Business Services Limited (Capita), the Centre for Health and Disability Assessments (CHDA) and Health Management Limited (HML). Both CHDA and HML are wholly-owned subsidiaries within MAXIMUS. Over three years from April 2015 to March 2018, the Department expects to spend a total £1.6 billion on an estimated 7 million assessments.

4 The assessment contracts are at very different stages. Between 2005 and 2015, the Department contracted with Atos for Incapacity Benefit and then ESA assessments.¹ It now has a new contract with CHDA covering ESA assessments. Two providers, Atos and Capita, have been providing PIP assessments since mid-2013. HML started the FFW advice service in December 2014, and nationwide assessments from March 2015.

5 Providers have struggled to meet performance targets for both ESA and PIP. In our 2012 report *Contract management of medical services* and our 2014 report *Personal Independence Payment: early progress* we found backlogs arose as a result of processes taking longer than expected.^{2,3} We also found issues with contract management, performance monitoring and the quality of assessment reports. The Department now expects to make savings in disability benefit spending significantly later than originally planned.

Scope of our report

6 Contract management is an evolving area for government. In our 2014 report *Transforming government's contract management* we recommended that government make sustained improvements and strengthen its contract management capabilities.⁴ The Department is one of several departments developing new models for working with contractors.

7 This report assesses the value for money of the Department's management of health and disability assessment contracts. Contracted-out assessments are an integral part of reforms designed to reduce benefit spending, better target support and reduce time off work. We do not assess the value for money of these wider reforms. But managing contracted-out assessments effectively is a necessary condition for achieving value for money in the longer term. Not only will slow or substandard assessments delay the benefits of reforms and impose burdens on claimants, but assessment contracts are also a significant cost in their own right.

8 As the assessment contracts are at different stages, we can consider how the Department has changed its approach, manages contracts across their lifecycle and also how well-placed it is to meet future challenges.⁵ We have used our contract assessment framework (Figure 14 on page 43) to compare these contracts and consider:

- recent performance and developments (Part One); and
- how the Department has managed the contracts (Part Two).

1 Includes assessments for other benefits such as Industrial Injuries Disablement Benefit.

2 Comptroller and Auditor General, *Contract management of medical services*, Session 2012-13, HC 627, National Audit Office, October 2012.

3 Comptroller and Auditor General, *Personal Independence Payment: early progress*, Session 2013-14, HC 1070, National Audit Office, February 2014.

4 Comptroller and Auditor General, *Transforming government's contract management*, Session 2014-15, HC 269, National Audit Office, September 2014.

5 We only consider contracts in relation to ESA assessments. The 2005 contract with Atos primarily covered Incapacity Benefit assessments. The Department introduced ESA in 2008.

Key findings

Recent performance and developments

9 The Department has concentrated on tackling its immediate operational problems by managing demand and developing improvement plans with providers. During 2013-14, the number of outstanding cases increased for both ESA and PIP. From October 2013, the Department slowed the roll-out of PIP and suspended routine reassessments of existing ESA claimants. It agreed improvement plans with providers, who also hired additional staff. For ESA it agreed plans in early 2014 after Atos requested early exit from the ESA contract. The Department agreed improvement plans with Atos and Capita for PIP in mid-2014 (paragraphs 1.8, 1.12, Figure 3).

10 The Department is reducing the number of outstanding assessments, and providers are processing them more quickly. By August 2015, PIP providers were taking an average of four weeks to complete PIP assessments. This was within contractually agreed service levels and significantly better than the peak of 29 weeks in mid-2014. The Department eliminated the backlog of Incapacity Benefit claims awaiting reassessment for ESA by March 2014, but still had an estimated backlog of 280,000 ESA assessments in August 2015. The Department is now increasing the number of ESA and PIP assessments and rolling out the FFW service (paragraphs 1.12 and 1.18 to 1.19, Figure 3).

11 Despite progress, some providers continue to struggle with hiring and training staff. CHDA is not on track to complete the expected number of ESA assessments for 2015. This is largely due to problems reaching the full staff complement, particularly in London and the Home Counties. It is facing significant challenges with staff failing to complete training requirements. One possible consequence of capacity shortages is that assessment report quality is lower as staff may be less experienced. For PIP, both providers have failed to meet targets for the quality of assessment reports since October 2013. Providers have met other measures of quality and are currently reviewing quality measures with the Department (paragraphs 1.13 to 1.14, 1.20, Figures 4, 5 and 5a).

12 The Department is paying more for assessments, caused in part by capacity shortages pushing up salaries. Under the new ESA contract with CHDA, the cost of providing assessments has increased. We estimate it will now cost £190 to provide an assessment compared with £115 under Atos. The Department told us that costs have increased in part because providers are carrying out a higher proportion of face-to-face assessments and staff are being recruited at higher salaries (paragraphs 1.15 to 1.17, Figure 6).

Managing the contracts

13 While tackling its immediate operational concerns, the Department has strengthened its oversight and management of contracts in several ways:

- **The Department has increased its capacity for performance management.** It has established dedicated teams and named contract owners as primary contacts for each of the major contracts. The Department expanded its performance management team from 48 people in 2013 to 80 in 2015 (paragraphs 2.3 to 2.7, Figure 7).
- **The Department has strengthened its oversight of performance.** The Department has increased contact with providers and started to develop in-house ESA provision to better understand processes. It has also required providers to supply more detailed management information more frequently (paragraphs 2.8 to 2.14, Figure 8).
- **The Department has responded more quickly to performance issues.** Recovery was hampered by the length of time needed to agree improvement plans with providers. The Department responded more quickly in the new ESA contract and agreed a plan just one month after concerns were identified. The Department has applied service credits more often in eligible situations and allowed fewer exceptions (paragraphs 2.15 to 2.18, Figure 9 and Figure 10).
- **The Department managed contract transition smoothly.** The Department, Atos and CHDA think the transition of ESA assessments in early 2015 was well managed (paragraphs 2.19 to 2.25, Figure 11).

14 While the Department has more robust performance management, this does not address the fundamental challenge created by shortages of capacity and a desire to complete large numbers of assessments quickly and accurately. The Department recognised problems with PIP and earlier ESA contracts, but recent performance shows the Department has not tackled – and may even have exacerbated – some of these problems when setting up recent contracts:

- **The Department continues to have an unclear approach to transferring risk and managing incentives.** The Department has introduced strong statements of risk transfer in its contracts. At the same time it has increased its direct management of processes. Some providers raised concerns with us about the clarity of these arrangements and the cost to providers of complying with the Department's requests (paragraphs 2.27 to 2.29, Figure 12).

- **The Department has continued to set high targets and use assumptions without evidence of sufficient testing and challenge.** The Department set an ambitious, non-negotiable target of 1 million ESA assessments in 2015-16. It based this on the expected number of assessments it needed to manage benefit expenditure. The Department did not base its target on the modelling of available resources, and did not consider revising the target following bidders' requests, although it did make changes after contract award. The Department also allowed bidders to make assumptions about staff training that it knew were overly optimistic and difficult to achieve (paragraphs 2.30 to 2.35).
- **The Department does not yet have an overall strategy for contracting out assessments and risks damaging market interest.** In 2012, the Department set up a framework of potential providers to help build market interest. But it only used this framework for PIP and the framework will expire in 2016. A Departmental review found that tight procurement timetables, inflexibility towards critical assumptions, and lack of transparency risked damaging market interest (paragraphs 2.36 to 2.42, Figure 13).

Conclusion on value for money

15 It makes sense that the Department has prioritised its immediate operational problems by working with providers to increase capacity, improve contract management, and tighten monitoring and oversight of performance. The Department and providers have made progress reducing the number of outstanding claims and waiting times that PIP claimants have experienced in recent years.

16 Despite some progress, the Department has not yet achieved value for money in its management of assessment contracts. Overall it now expects to pay more for assessments, and is still not achieving volume and assessment report quality targets. Even if the Department is able to stabilise current performance, it needs to tackle underlying capacity challenges and set challenging but realistic targets in any future contracts. Otherwise its approach to managing contracts and critical assumptions risks perpetuating a cycle of optimistic targets, contractual underperformance and costly recovery.

Recommendations

17 As it develops its approach to contracted-out assessments, and considers its options for when current contracts end, the Department should:

- a** **Develop an overall commercial strategy for health and disability assessments.**
It should develop an integrated approach to assessments which would support longer-term market development and capacity building. It should clarify the role of in-house provision and how it will complement contracted-out services.
- b** **Assess its future commercial capacity and skills needs against future risks.**
The Department should tailor its contract management approach to the risks associated with individual contracts. Having increased staff numbers, it needs to work with the Cabinet Office to review and develop staff skills.
- c** **Set out realistic but challenging evidence-based targets and adhere to clear principles for challenging assumptions through the procurement and management of contracts.** It should challenge targets and assumptions, and reduce its reliance on responding through ad hoc changes after contracts are signed. Where assumptions are uncertain it should develop its principles for using 'allowable assumptions' clauses and extend these beyond the initial stages of a contract.
- d** **Work with providers to establish common principles for managing assessment contracts and risks.** It should increase activity to engage providers in learning lessons from recent experience, and to understand barriers to providers bidding for and providing assessments.

Part One

Recent performance and developments

1.1 The Department for Work & Pensions (the Department) uses contracted-out health and disability assessments to inform decisions about benefits and help people back into work. In this part we review recent developments and provider performance.

Three main reasons for assessments

1.2 The Department uses assessments for a range of services and benefits (**Figure 1** overleaf), mainly:

- to assess people's capability for work and inform decisions about claims for Employment and Support Allowance (ESA);
- to assess people's mobility and daily living needs and inform decisions about claims for Personal Independence Payment (PIP); and
- to support people on sick leave back into work as part of the Fit for Work (FFW) service.

1.3 Assessments are only one aspect of the benefit process for ESA and PIP claims. The Department remains the first point of contact for making a claim. It refers people to providers who conduct face-to-face or paper-based assessments and gather further evidence. The Department makes the final decision on benefit entitlement. The FFW assessment service allows GPs or employers to refer those on long-term sick leave for a free and voluntary occupational health assessment.

1.4 Although the three assessments are different, ESA, PIP and FFW overlap both in terms of the claimants they affect and the market for contracted-out assessments. The Department recognises these interactions and manages contracts within the same team.

Figure 1

Overview of use of assessments

The Department uses assessments in three main areas

Title	Employment and Support Allowance	Personal Independence Payment	Fit for Work
Started	October 2008	April 2013	December 2014
Description	Contributory or means-tested benefit for those unable to work Replaces Incapacity Benefit	Non-means tested benefit to help with additional costs of living with disability Replaces Disability Living Allowance (DLA)	Free occupational assessment and advice service
Assessments	Functional assessment of capability for work or work-related activity Face-to-face or paper-based By doctors, nurses, physiotherapists	Functional assessment of daily living and mobility needs Face-to-face or paper-based By doctors, nurses, physiotherapists, occupational therapists, paramedics	Occupational health assessment Telephone or face-to-face By occupational therapists, nurses, physiotherapists
Pathways	Different processes for terminally ill claimants Contributory claims time limited Non-contributory claims reassessed after set period	Different processes for terminally ill claimants All awards of two years or more have a specified review period	GPs or employers make voluntary referrals
Outcome	Two award groups: work related activity or support	A daily living and a mobility component each with two award levels	Provider develops action plan for individual
Current stage	Incapacity Benefit claimants assessed for ESA Routine reassessments of ESA claimants suspended early 2014 and restarted gradually from December 2015	Completed roll-out for new claims and natural DLA reassessments From July 2015, managed reassessments of existing DLA claims	Advice service started December 2014 Assessment service started March 2015
Caseload March 2015	2.2 million	0.2 million (2 million DLA claimants eligible for PIP reassessment)	n/a

Notes

- 1 Individuals can claim both ESA and PIP. FFW is not a benefit and is available where employers do not provide occupational health services.
- 2 The Department began to roll out FFW assessments in March 2015 and expects nearly 18,000 assessments in 2015-16.

Source: Published documents

Use of contracts

1.5 The Department has increasingly used third-party providers to provide assessment and advice services. In this report we consider six recent contracts for providing ESA, PIP and FFW assessments (**Figure 2** overleaf).⁶ These are:

- Two successive contracts for ESA assessments. In 2005, the Department awarded a contract to Atos for Incapacity Benefit and, from 2008, ESA assessments. After the early termination of Atos's contract in 2015, the Centre for Health and Disability Assessments (CHDA) took over ESA assessments. CHDA is a wholly-owned subsidiary within MAXIMUS.
- Three concurrent regional contracts for PIP assessments. In July 2012, the Department signed three regional contracts to provide assessments: two with Atos and one with Capita Business Services Limited (Capita).
- One new contract for the FFW service. In July 2014, the Department signed a contract with Health Management Limited (HML) to provide the FFW service in England and Wales. HML is a wholly-owned subsidiary within MAXIMUS.

1.6 During 2014-15, the Department spent around £275 million on contracts for health and disability assessments, not including its own contract management costs (see Appendix Three for a detailed breakdown). This cost is expected to more than double to £579 million in 2016-17 as, for example, the Department increases the number of assessments.

Some progress with earlier performance issues

1.7 Providers have struggled to meet expected performance levels. Our reports *Contract management of medical services* in 2012 and *Personal Independence Payment: early progress* in 2014 highlighted emerging performance problems and how issues with assumptions and management information contributed to backlogs and claimants waiting months for assessments.⁷

⁶ Contracts for ESA assessments also cover assessments for benefits such as Industrial Injuries Disablement Benefit.

⁷ DLA claimants being assessed for PIP and ESA claimants will (after a defined 'waiting' period) be paid while their claim is being processed. New PIP claimants will be paid from the date a decision is made.

Figure 2

Contracts for assessments

The Department has managed six recent contracts for assessments

	Employment and Support Allowance		Personal Independence Payment	Fit for Work
Contract name	Medical Services Agreement	Health and Disability Assessment Service	Personal Independence Payment	Fit for Work
Provider	Atos	CHDA (MAXIMUS)	Atos: 2 regions Capita: 1 region	HML (MAXIMUS)
Contract start	September 2005	October 2014	July 2012	July 2014
Service start	September 2005	March 2015	April/June 2013	December 2014
Contract duration (years)	7	3.3	5	5
	Extended 3 years to 2015	Can extend for 1-2 years	Can extend for up to 2 years	Can extend for up to 2 years
Value (£m)	512	595	512	133
Contractor provides				
IT	Yes	No	Partly	Yes
Estates	Partly	Partly	Yes	Yes
Assessments	Yes	Yes	Yes	Yes
Other	–	–	–	Advisory service

Notes

- 1 'Value' shows the original, estimated value at the time of procurement. It includes set-up costs and not the impact of contract extensions. Actual costs, shown in Appendix Three, differ.
- 2 CHDA replaced Atos to provide ESA assessments from March 2015. These contracts covered Incapacity Benefit, Incapacity Benefit reassessments for ESA and smaller benefits such as Industrial Injuries Disablement Benefit.
- 3 Capita provides approximately 23% of PIP assessments, covering Wales and the Midlands, and Atos the rest.
- 4 The FFW contract does not cover Scotland.

Source: Comptroller and Auditor General, *Personal Independence Payment: early progress*, Session 2013-14, HC 1070, National Audit Office, February 2015; National Audit Office analysis of Departmental plans

1.8 Between 2013 and 2014, it took both ESA and PIP providers far longer than expected to return assessment reports to the Department and the number of outstanding claims increased. Between June 2013 and January 2014, the time taken by the ESA provider doubled from 10 to 20 weeks, against a target of seven weeks. During this period, the number of outstanding ESA claims increased steadily from 384,000 to 724,000.⁸ PIP delays peaked in mid-2014 when it took providers an average of 29 weeks to return assessment reports. The Department expects providers to return assessment reports within six weeks. The number of outstanding claims almost doubled to 242,000 in the first six months of 2014.

1.9 For PIP and DLA, the Department expects savings significantly later than planned because of performance issues and changes to assumptions such as award rates. It initially expected to achieve £0.8 billion savings during the Spending Review period up to April 2015 and then £3 billion annual savings from 2018-19.⁹ It did not achieve any savings during the Spending Review period. The Department could not provide us with a comparable revised annual savings estimate. However, it now expects to reduce spending by £0.4 billion from £16.2 billion in 2015-16 to £15.8 billion in 2018-19. In March 2014, the Department forecast a £1.1 billion reduction across the same period.

1.10 It is not clear if performance issues have affected ESA spending. The Department will not achieve the £5.4 billion savings initially envisaged in the ten years to 2019-20. For incapacity benefits, including ESA and Incapacity Benefit, it expects a spending increase to £15 billion in 2015-16 and then a fall to £14.3 billion in 2018-19. The Department believes a number of factors have reduced savings and continues to see ESA as important in managing public expenditure.

1.11 The Office for Budget Responsibility identified ESA and PIP as major risks to planned spending given the uncertainty of forecasts. It expressed concern that recent changes to disability forecasts repeat a similar pattern to spending forecasts during the roll-out of ESA and described increases in expected disability spending as material.¹⁰ The Department is forecast to spend £92 billion on disability and incapacity benefits over three years from 2015-16.

⁸ Excludes outstanding Incapacity Benefit reassessments. Does not reconcile to Figure 3.

⁹ Cash terms.

¹⁰ Office for Budgetary Responsibility, *Welfare trends* report, October 2014; *Welfare trends* report, June 2015; *Economic and Fiscal Outlook*, November 2015.

1.12 The Department and providers responded to performance issues:

- For ESA, in January 2014, the Department reduced demand by suspending routine reassessments. As at August 2015, almost 1 million reassessments have been suspended. In March 2014, it announced that Atos would exit the contract and agreed revised performance arrangements for the transition period to February 2015. The time taken for the provider to return assessment reports peaked in September 2014 at 29 weeks. Reports are now being returned more quickly but the average time remains high at 23 weeks. The number of outstanding claims has reduced to 410,000 in August 2015 (**Figure 3** on page 18), of which an estimated 280,000 could be determined as a backlog.¹¹
- For PIP, the Department reduced volumes by slowing the roll-out of Disability Living Allowance reassessments. It worked with providers to develop improvement plans and increase capacity. By August 2015, PIP providers were taking an average four weeks to return assessment reports to the Department, significantly better than mid-2014. The number of outstanding claims had fallen to 57,000 in August 2015.

Continuing challenges around volume and quality of assessment reports

1.13 While providers have concentrated on reducing the number of outstanding claims, they are not yet consistently meeting all expected performance levels. These include:

- **Volume targets.** In 2015-16 the provider, CHDA, needs to complete nearly 1 million ESA assessments. It met targets for the first two months and has struggled since (**Figure 4** on page 19).
- **Assessment report quality targets.** The Department or providers audit the quality of assessment reports. ESA and PIP providers have not consistently met these targets (**Figure 5** on pages 20 and 21). They only met 13% of targets for PIP and ESA assessment reports not meeting the contractual standard in the 12 months up to August 2015. In September 2015, the Department's internal audit team raised concerns about the quality of the FFW service although they did not look at this in detail.

¹¹ Estimated backlog shows the difference between the actual and expected number of outstanding assessments, where the expected outstanding volume is 1.5 times the claims received that month.

1.14 Report quality does not necessarily affect the benefit decisions made by the Department, and reports can be graded as below standard for errors in spelling and grammar. One provider also raised concerns that there could be inconsistencies in approach and that it may not be appropriate to compare performance between providers. The Department also uses another measure of quality: the proportion of assessments returned to providers as not fit for purpose. On this measure providers have performed well against targets (**Figure 5a** on pages 22 and 23). The Department and providers have recently developed a new audit approach which aims to improve measurement of quality and support decision-making. One of the providers told us it had already completed IT changes in December 2015 to support new performance management arrangements.

Increased cost of assessments

1.15 The average costs of providing assessments have risen (**Figure 6** on page 24).¹² Under its 2005 contract the Department paid Atos around £112 million a year for 1 million ESA assessments. This was around £115 per assessment in real terms. Under its new 2015 contract with CHDA the Department expects to pay £595 million over three years for 3.4 million assessments. Including IT and estate costs, no longer covered by the new ESA contract, this is around £190 per assessment. Costs do not include Departmental staff increases.

1.16 There are a number of reasons for ESA assessment costs increasing. The Department told us it was willing to pay more for a higher proportion of face-to-face assessments and there have been higher salaries for healthcare professionals, particularly in London and the Home Counties.¹³ The estimated cost of hiring and training healthcare professionals for ESA assessments increased from an average £26,000 (spring 2014) in the earlier contract to, for example, £44,000 for a London-based nurse in 2015-16. The Department told us other reasons for assessments costing more included using a different payment model to encourage competition and market interest; better understanding of quality requirements and contracting for a more sustainable service. Based on published information, we have not been able to identify the financial impact of individual factors on the estimated average cost.

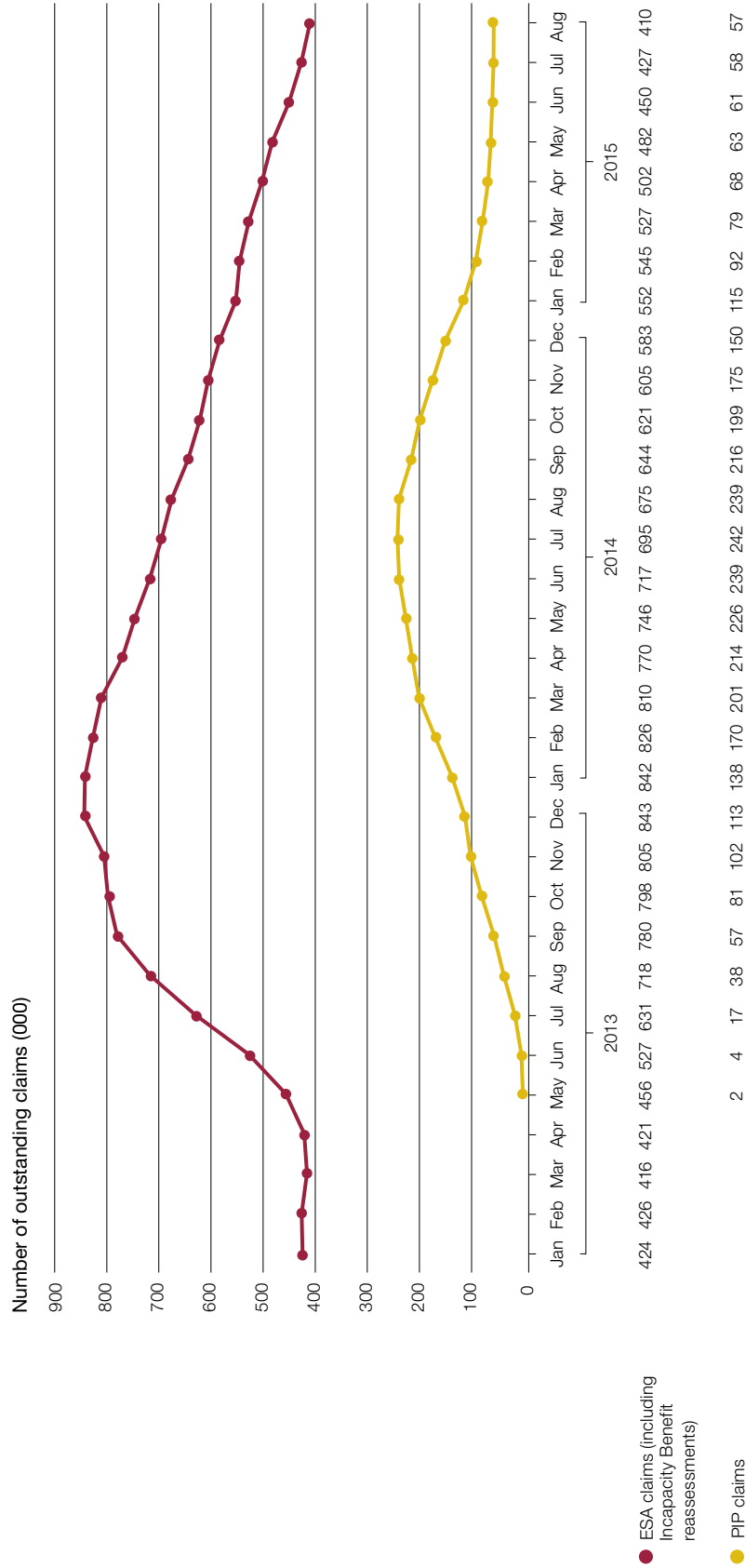
1.17 The Department has also spent more than expected because of delays in setting-up PIP systems. It was delayed in developing an IT tool for providers to record assessments electronically, planned for October 2013, and has not yet introduced this for most claims. The Department told us it preferred to wait until backlogs had reduced. Providers told us the system is not yet ready and they have continued to conduct assessments using their own systems or manually, costing the Department an estimated £76 million more.

¹² We do not include exact costs because of concerns about commercial sensitivity.

¹³ In 2011-12, under the old ESA contract, 67% of assessments were face-to-face. The Department expected CHDA to conduct 70% of assessments face-to-face at the time of the contract.

Figure 3
Monthly outstanding ESA and PIP claims between January 2013 and August 2015

The Department has reduced the number of outstanding ESA and PIP claims

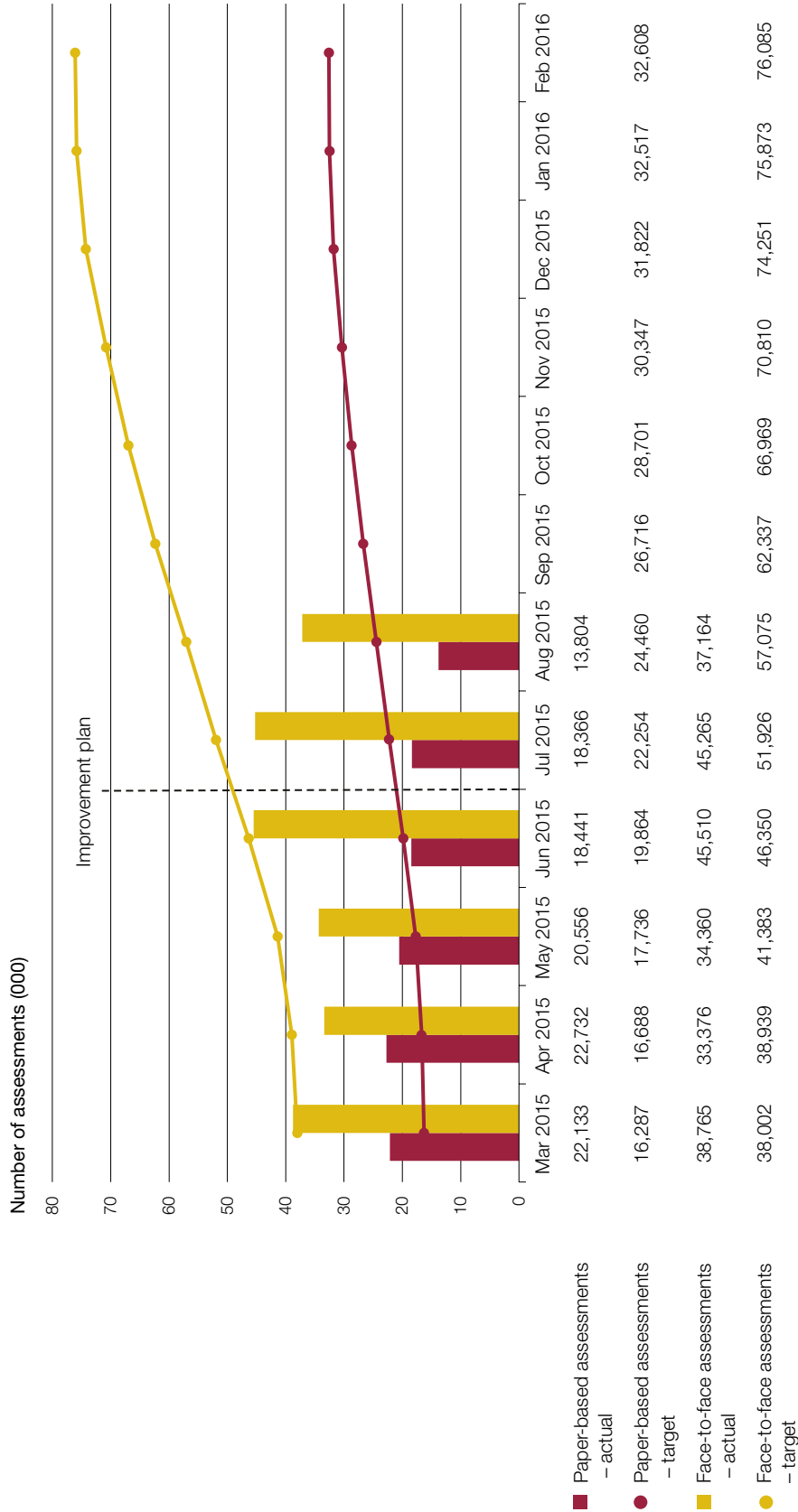


Notes

- 1 Includes all claims awaiting a decision across both provider and Departmental parts of the process. There will always be outstanding claims at different stages of the process.
- 2 ESA outstanding claims include those for Incapacity Benefit reassessments, which peaked at 197,000 outstanding in August 2013.

Source: National Audit Office analysis of Departmental information

Figure 4
 ESA volumes: actual against target between March and August 2015
 Centre for Health and Disability Assessments (CHDA) has struggled to meet volume targets since the start of the contract



Notes

- 1 Target volumes to June 2015 reflect those agreed in the initial contract. In June 2015, the Department and CHDA agreed to reduce the expected annual target volume from 1 million to 980,000 given a lower number of healthcare professionals transferred from the previous provider than the contractual assumption agreed by the Department and CHDA. In September 2015, they agreed to reduce the target number of paper-based assessments by 69,000, and therefore the overall target to 911,000, to complete proportionally more face-to-face assessments.
- 2 The Department did not apply volume-based service credits in the first three months of the contract. It did not alter the annual target so any shortfall across the start of the year would still be applied. CHDA forecast they will not complete the expected number of face-to-face or paper-based assessments and have communicated this to the Department.
- 3 The Department and CHDA agreed an improvement plan given lower than expected volumes.

Source: National Audit Office analysis of Departmental data

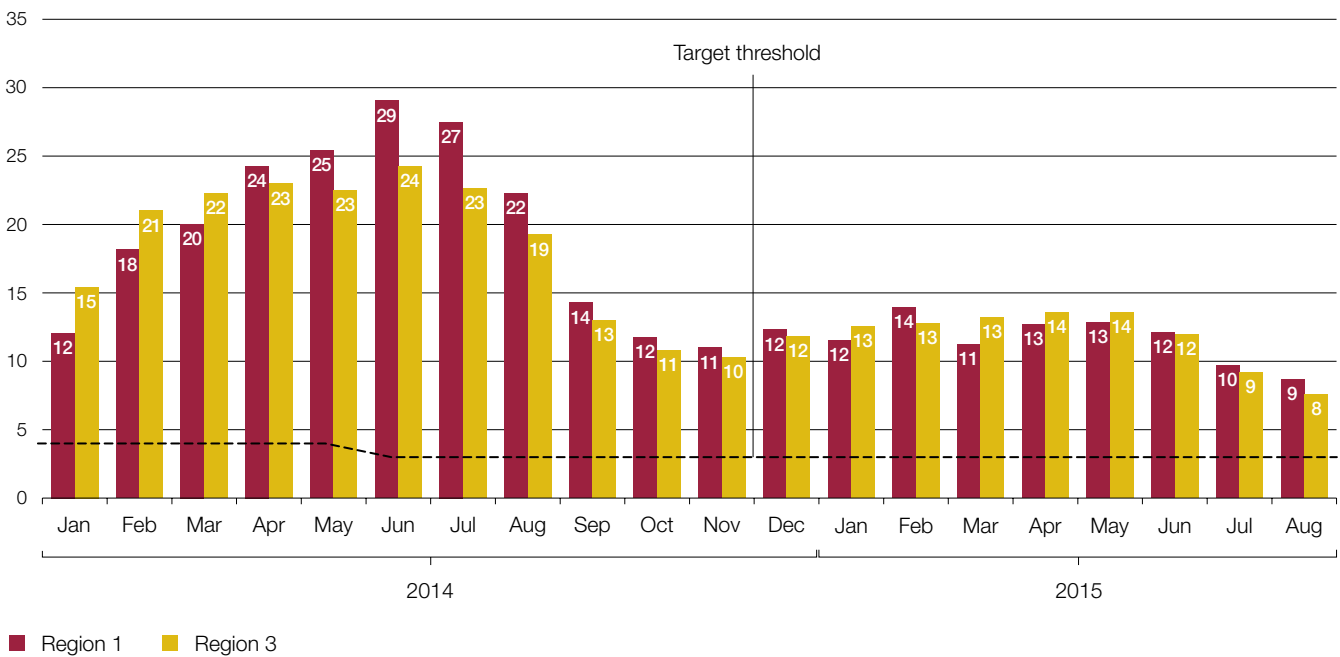
Figure 5

ESA and PIP assessment report quality: proportion of assessment reports below contracted quality standards between January 2014 to August 2015

Providers have not consistently met expected standards for the quality of assessment reports

PIP – Atos Regions 1 and 3

Percentage of reports not meeting contractual standards



PIP – Capita Region 2

Percentage of reports not meeting contractual standards

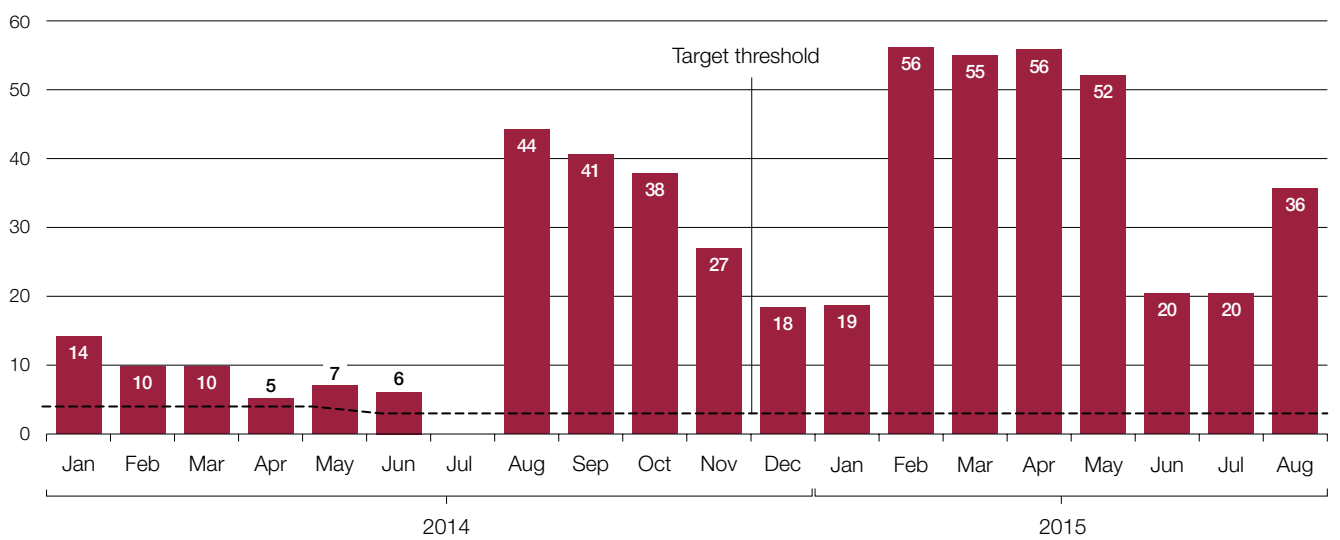
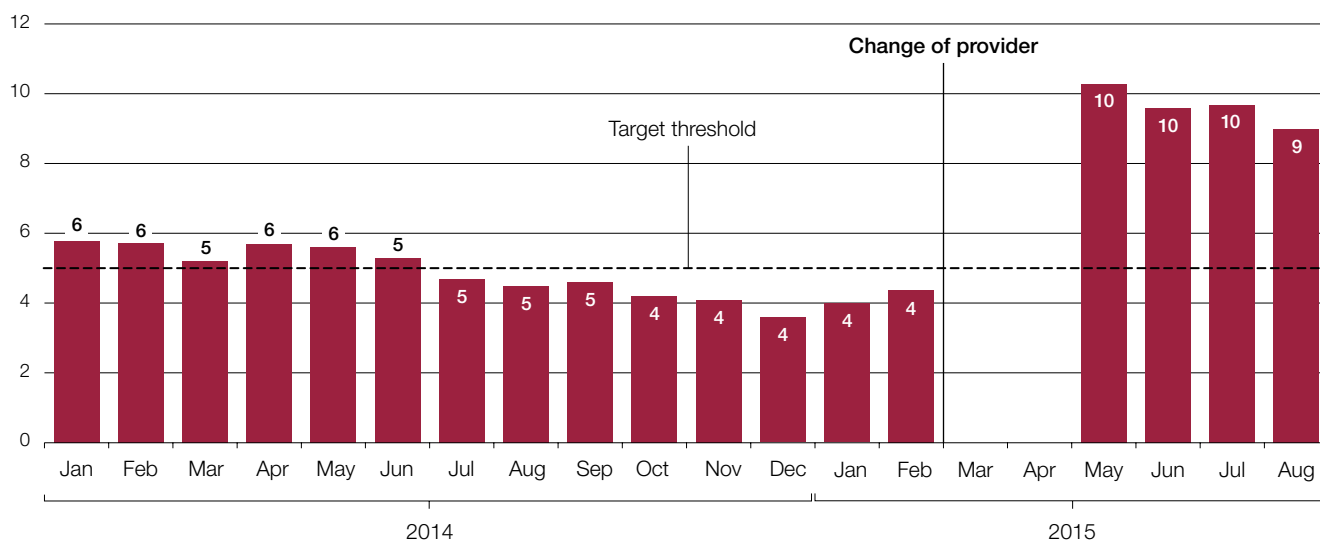


Figure 5 *continued*

ESA and PIP assessment report quality: proportion of assessment reports below expected quality standards between January 2014 to August 2015

ESA providers

Percentage of reports not meeting quality standards



Notes

- 1 Reports not meeting a Department or provider quality assessment may contain errors in spelling and grammar or the excessive use of acronyms and abbreviations but they may still be judged fit for purpose by the Department and used as part of the decision-making process.
- 2 Shows three-month rolling average. As such, data for the new ESA provider from March 2015 were not available until the third month of the contract. Under the new contract, new assessment report quality audit arrangements are in place. Changes include having a single, dedicated, independent audit team (compared to multiple provider audit teams); how assessment reports are selected for testing and when selected reports will drop out of the sample.
- 3 The Department expected 4% of PIP reports sampled to not meet contractual quality standards, reducing to 3% in subsequent years. Data for Capita was unavailable for July 2014. Quality audits conducted by providers and not independently assured. Capita raised concerns over the comparability of performance across providers. The Department and providers are currently reviewing report quality audit arrangements.

Source: National Audit Office analysis of unaudited provider data

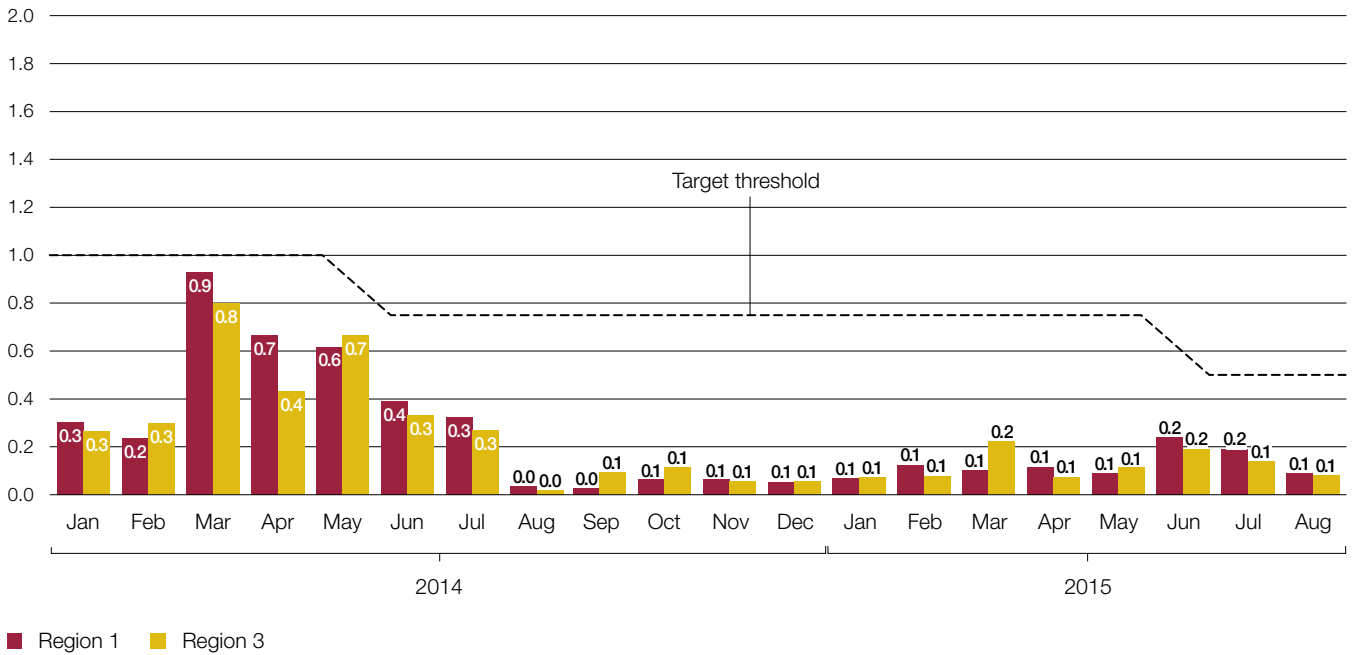
Figure 5a

ESA and PIP assessment quality: proportion of assessments not fit for purpose, January 2014 and August 2015

Providers have performed well against targets for the proportion of assessments returned by the Department

PIP – Atos Regions 1 and 3

Percentage of assessment reports returned to provider



PIP – Capita Region 2

Percentage of assessment reports returned to provider

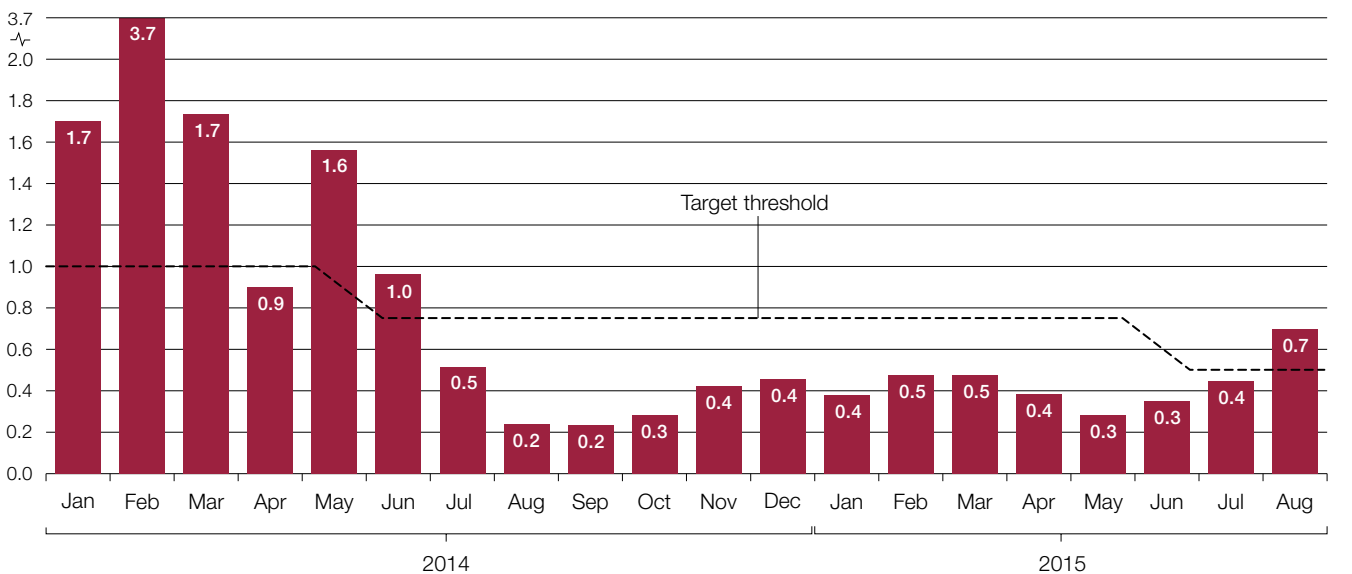
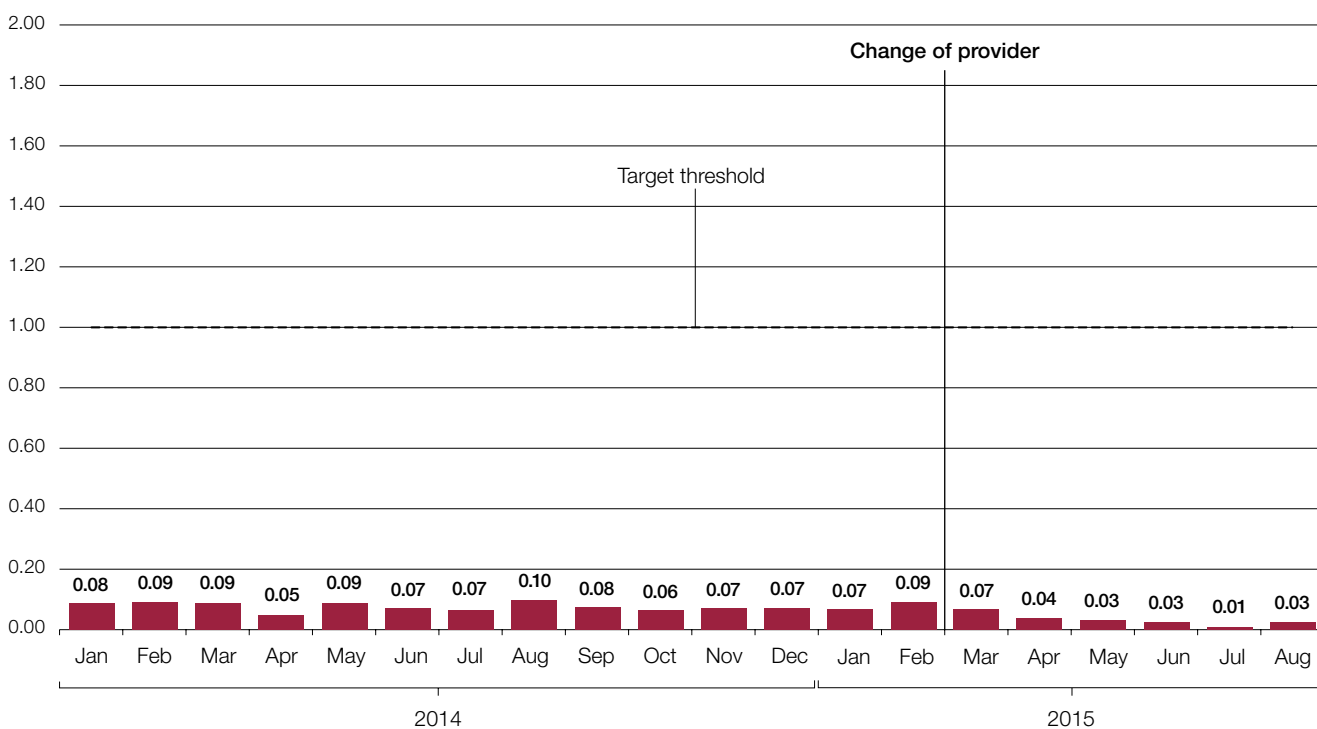


Figure 5a *continued*

ESA and PIP assessment quality: proportion of assessments not fit for purpose, January 2014 and August 2015

ESA providers

Percentage of assessment reports returned to provider



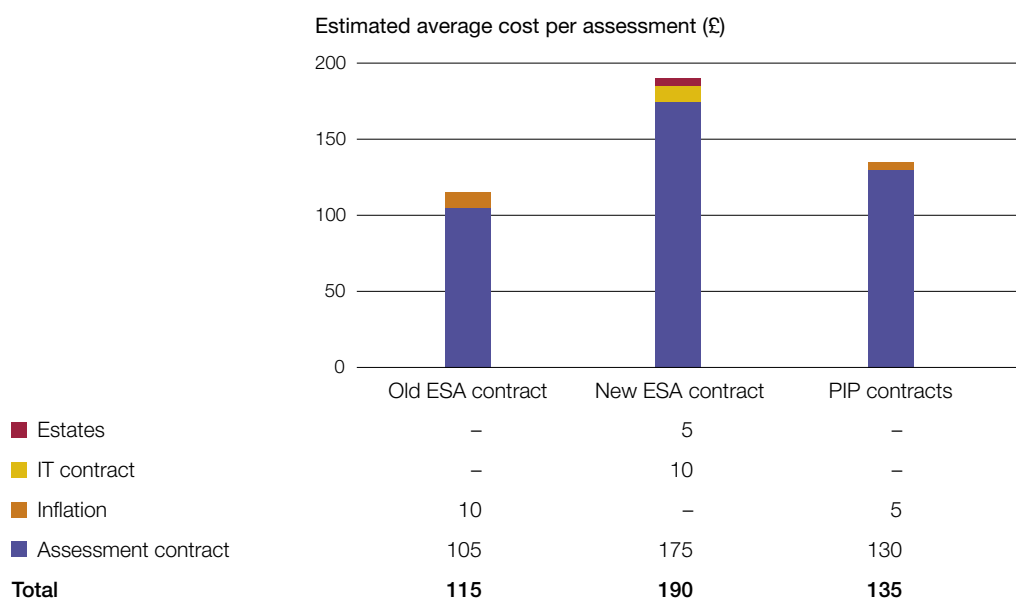
Notes

- 1 Department returns assessment report to provider if deemed not fit for purpose and it cannot be used to make a benefit decision.
- 2 PIP target reduced from 1% in year one, to 0.75% in year two and 0.5% year three onwards.

Source: National Audit Office analysis of unaudited provider data

Figure 6 ESA and PIP estimated average costs per assessment

The estimated cost per ESA assessment has increased



Notes

- 1 New ESA contract shows real costs as at October 2014 when the contract signed. Old ESA costs inflated by 7.82% and PIP by 5.26% based on the consumer price index for the health sector.
- 2 For reasons of commercial sensitivity we primarily use published information and have made a number of assumptions. Exact numbers confirm similar findings.
- 3 The old ESA (Atos) estimated average cost uses actual costs and assessment volumes for 2011-12 as an indication of costs and volumes across the contract. This does not include set-up costs.
- 4 The new ESA contract (CHDA) and PIP estimated average costs use forecast costs and assessment volumes across the whole contract from the time of award. This includes set-up costs.

Source: Comptroller and Auditor General reports, *Contract management of medical services*, Session 2012-13, HC 627, October 2012; *Personal Independence Payment: Early Progress*, Session 2013-14, HC 1070, National Audit Office, February 2014; Department for Work & Pensions, *ESA: outcomes of Work Capability Assessments*, September 2015; Contracts archive available at: <https://data.gov.uk/data/contracts-finder-archive/>

Increasing volume of assessments

1.18 Over the next 18 months, the Department plans to significantly increase the number of assessments conducted by providers. The Department needs providers to complete the planned number of assessments so it can achieve expected benefit savings and manage expenditure. Increases in assessments include:

- **ESA.** During the final 12 months of the contract, Atos conducted 820,000 ESA assessments, of which 52% were face-to-face. In the first year of the new contract, CHDA is contractually required to complete nearly 1 million assessments, of which 75% must now be carried out face-to-face. This will increase to 1.2 million in years two and three. Having suspended the reassessment of existing ESA claimants in early 2014, the Department began reassessments in December 2015 and will gradually assess those already outstanding from January 2016.
- **PIP.** In July 2015, the Department began managed reassessments of existing Disability Living Allowance claimants to check whether they are eligible for PIP. It will take into account providers' capacity and performance when deciding the pace of reassessments. By 2018, the Department originally expected to reassess 1.7 million claimants and process 1.9 million new claims. It has now extended this by a year.
- **FFW.** The service is in its early days and take-up has been slower than expected. The provider completed 238 assessments in August 2015. Monthly volume is expected to increase to over 30,000 within the next year.

1.19 Overall, as at August 2015, the Department expected to increase the monthly number of assessments from around 160,000 in September 2015 to 270,000 by March 2017. Delays to the original PIP roll-out, lower than expected take-up on FFW and ESA providers not delivering contracted volumes have reduced the expected number of assessments in the short-term. The Department needs to share revised forecasts for PIP with providers when they are ready.

1.20 A simultaneous increase in the number of assessments presents challenges for both providers and the Department. These include recruiting, training and retaining healthcare professionals and providing enough centres for training and assessments. In April 2015, the Department estimated providers would need to increase the number of healthcare professionals by 84% from 2,200 in May 2015 to 4,050 in November 2016 based on its current plans. This will be particularly challenging given market pressures. In the Department's analysis of the wider healthcare professional market, only 3% of 3,970 vacancies are advertised for more than 30 days, suggesting there are relatively few long-term vacancies. Along with the Department, all providers told us they identified healthcare professional capacity as high risk.

Part Two

Managing the contracts

2.1 The Department for Work & Pensions (the Department) has changed the way it contracts for and manages assessment contracts. In this part we consider how the Department has:

- managed providers; and
- developed and set up contracts.

To structure our review, we have used our contract assessment framework which is described in Appendix One.

Strengthening management and oversight

2.2 In our previous reports on contract management across government we have highlighted the need for departments to strengthen contract management actively throughout the contract lifecycle. In reports on health and disability assessments we also found problems with oversight and performance management.¹⁴ The Department has made progress in several areas.

Expanding management capability

2.3 To manage contracts effectively, the Department needs to have enough people with the right skills and to break down barriers between roles. The Department has several teams involved including a commercial team and a performance management team responsible for liaising with providers and managing performance.

2.4 The Department has invested heavily in the size of its performance management team. It has expanded to allow it to dedicate people to individual contracts and improve understanding of processes. The performance management team grew from 48 people in 2013 to 80 in 2015.

¹⁴ Comptroller and Auditor General reports, *Managing government suppliers*, Session 2013-14, HC 811, National Audit Office, November 2013; *Personal Independence Payment: early progress*, Session 2013-14, HC 1070, National Audit Office, February 2014; Department for Work & Pensions, *ESA: outcomes of Work Capability Assessments*, September 2015.

2.5 The Department recognises that, despite increasing the number of staff, having insufficient skills and expertise is a major risk. It assessed the commercial team's skills in 2015 and found that 74% had procurement skills, 85% were able to demonstrate the right behaviours, but only 57% had sufficient business knowledge. The performance management team – which draws heavily on existing Department staff – is still developing its experience and approach to managing contracts.

2.6 As well as expanding its performance management capacity, the Department has reorganised responsibilities for managing commercial relationships (**Figure 7**). Performance management teams act as primary contacts for providers. Detailed guidance sets out governance and performance structures. In September 2015, the Department's internal audit team found effective supplier monitoring arrangements in place for FFW. Providers told us they were generally clear where responsibilities lay within the Department.

2.7 The Department recognises that the rapid expansion and new arrangements may lead to duplication across commercial and performance management roles. It plans to consider where efficiencies can be made as part of a wider review.

Figure 7

Contract governance and responsibilities in 2013 and 2015

The Department has reorganised responsibilities for contracts

	2013	2015
Overview	Tripartite relationship between finance, operations and commercial	Dedicated team with specialists contributing
Senior contract owner	No	Yes
Governance	Monthly performance reviews including all teams	Weekly and monthly reviews
Team responsibilities		
Performance management	n/a	Front-line connection – analyses provider performance and develops relationships
Operations	Monitors performance and manages changes	n/a (contract management provides link)
Commercial	Collates service credit data and provides commercial perspective	Commercial management, understanding and developing the market
Finance	Financial perspective	Business partners provide expertise and challenge financial reports
Programme teams	Dedicated commercial teams within programmes	Commissions commercial services

Note

1 The senior contract owner works within the performance management team. This includes account directors for each contract and dedicated performance management teams.

Source: National Audit Office analysis of departmental documents

More active contractual oversight

2.8 Our previous reports have highlighted the importance for contract managers to understand end-to-end processes and performance. The Department has taken steps to better understand providers' processes, including:

- Developing detailed contract guidance for Employment and Support Allowance (ESA) that explains governance and performance monitoring arrangements. The Department plans to introduce similar guidance for other contracts.
- Increasing contact with providers to better understand provider processes and share good practice. The ESA contract requires the provider to train departmental staff and transfer skills.
- Recruiting in-house healthcare professionals. Since September 2014, the Department has contracted Pertemps People Development Group (now APM) to recruit healthcare professionals. It employed 18 staff and will set-up two assessment centres to process ESA claims and test proposed changes to the process.
- Improving access to detailed information through weekly or daily updates rather than the monthly arrangements stipulated in contracts. The ESA and Fit for Work (FFW) contracts also increase transparency through access to provider accounting systems.
- Increasing assurance over provider data. The latest ESA contract introduces more robust independent audit of assessment report quality and the FFW contract introduces independent assurance of report quality and provider data.

2.9 In our view, it has been appropriate for the Department to exercise greater oversight and control in light of past performance. As contracts mature the Department will need to streamline and tailor arrangements to the risks of individual contracts. We have previously recommended it strengthens the validation of key performance data used to assess provider performance. This continues to be an area for improvement.

Better performance measurement

2.10 Our past reports have highlighted the importance of timely and quality information about performance. The Department needs good information both to manage performance and incentivise providers, and to identify emerging risks.

2.11 The Department monitors a range of contractual performance measures on turnaround time, quality and customer service (**Figure 8**). These are broadly similar across contracts, although there are some differences, such as the use of volume targets in the new ESA contract with CHDA.

Figure 8

Comparison of contractual performance levels

The Department has adopted similar performance levels across contracts

		Employment and Support Allowance		Personal Independence Payment	Fit for Work
		Atos	CHDA		
Turnaround	Volume		Year 1: 1.0 million Year 2: 1.2 million Year 3: 1.2 million		
	Turnaround time	35 days	Terminally ill: 99% in 2 days, 100% in 5 days Advice: 99% in 1 day	97% in 30 days Terminally ill: 99% in 2 days, 100% in 5 days	90% remote assessments in 2 days 90% face-to-face assessments in 5 days 85% return to work plans in 3 days 97% advice line queries in 2 days
Quality	Report does not meet standards	No more than 5%	Year 1: max 5% Year 2: max 5% Year 3: max 4%	Year 1: max 4% Year 2+: max 3%	Range of criteria: Year 1: 90% Year 2: 92% Year 3+: 95%
	Rework	No more than 1%	Year 1: max 1% Year 2: max 0.75% Year 3: max 0.5%	Year 1: max 1% Year 2: max 0.75% Year 3+: max 0.5%	
Customer	Waiting time	Average 15 minutes	90% in 30 minutes (60 minutes if home assessment)	90% in 30 minutes (60 minutes if home assessment)	
	Customers sent home unseen	No more than 1%	Year 1: max 4% Year 2: max 3% Year 3: max 2%	No more than 1%	
	Calls answered	90% (80% in 30 seconds)	90% (80% in 30 seconds)	90% (80% in 30 seconds)	90% (80% in 30 seconds)
	Customer satisfaction	90%	90%	90%	Year 1: average 90% Year 2: 92% Year 3+: 95% Service credits: <85%

Notes

- 1 Reflects initial contract. Expected timings measured in working days.
- 2 'Quality' – For ESA and PIP relates to assessment reports and not the benefit decision. Other quality targets include the percentage of reports that require amendment but meet contractual standards. For FFW, assessment and report quality are both audited.
- 3 'Rework' – Department returns assessment report to provider if deemed not fit for purpose.
- 4 'Volume' – Work Capability Assessments, predominantly ESA, and includes regional targets.

Source: National Audit Office contract analysis

2.12 Since our report, the Department has improved its use of performance information for Personal Independence Payment (PIP). The Department now reviews information from providers weekly and has developed leading indicators of risks, such as staff attrition. It is now considering how critical assumptions affect performance, for example by increasing PIP volumes slowly to allow staff to train and become more efficient.

2.13 There are some areas the Department will need to address to improve its understanding and use of performance information including:

- **Matching performance to objectives.** FFW aims to help those on long-term sick leave back into work. The provider's performance is monitored by outputs, such as the timeliness and quality of assessments. The Department does not monitor long-term outcomes such as the number of people returning to work.
- **Monitoring quality.** The Department has strengthened its approach to auditing assessment report quality by introducing independent auditors and a single, dedicated audit team, and changing how cases are selected for testing. Despite these changes, it has based the current ESA target on the previous provider's performance in the last two months of the contract. The Department has also been reconsidering the criteria used to assess assessment report quality. It has not yet considered how quality impacts other measures, such as rework, and decision-making.
- **Understanding trade-offs.** The Department needs to improve its understanding of the balance between cost, quality, speed of processing and customer satisfaction. Some providers' efforts to reduce backlogs, where these have arisen, appear to have affected other measures of performance, such as quality. During fieldwork, we received conflicting messages as to the Department's direction to providers on whether to focus on volumes over quality of assessment report targets.

2.14 In our view the Department has largely addressed existing concerns about information on ESA and PIP through improved performance information and a better understanding of operational processes. It is working to improve its understanding of quality, this should be a priority for future performance metrics.

More responsive to performance

2.15 A key theme from our recent review of government contracts has been the need for departments to manage providers throughout the life of a contract. Departments should always expect performance variations and should react quickly when they arrive.

2.16 The Department's day-to-day contractual lever for managing performance is service credits. However, they can be difficult to apply where, for example, the Department changes processes which impact performance. Between September 2005 and March 2012, the Department only applied 10% of accrued service credits on the earlier ESA contract due to service credit suspensions, earn back provisions and agreed mitigation.¹⁵ Recently the Department appears to have applied service credits with fewer exceptions and better enforced available financial levers (**Figure 9** overleaf).

2.17 When major performance problems arise, service credits are insufficient and more formal plans are needed. For both ESA and PIP the Department has had to request providers produce improvement plans. Up to the latest ESA contract, it has taken a long time to agree effective plans:

- **ESA.** In 2012, we found the service credit regime had not operated effectively and service credit suspensions had inhibited effective contract and performance management.¹⁶ In March 2012, the Department agreed an interim service credit regime with Atos to help reduce outstanding ESA assessments. This approach reduced the number of outstanding assessments but not to expected levels. In early 2014, the Department significantly reduced volumes by suspending routine reassessments of ESA claims. As at August 2015, almost 1 million reassessments have been suspended.
- **PIP.** In August 2013, the Department identified that claims were taking longer than expected. It took nine months to sign plans with Capita and 12 months with Atos, during which time performance worsened (**Figure 10** on pages 33 and 34). The plans included measures to increase capacity, revise governance arrangements and address weaknesses in performance management. Atos and the Department told us capacity had already begun to increase during this time in line with plans first discussed with the Department in April 2014. Also during this period, the Department responded to ESA assessment quality issues and increased the number of contract management staff.

2.18 The new ESA contract better defines how the Department will respond when a provider fails to reach expected performance levels. It also allows additional flexibility through the Department being able to appoint a remedial adviser. In late spring 2015, the Department and CHDA identified that volume targets were not being met as fewer staff than expected completed training requirements. They agreed a performance improvement plan just weeks later in early July 2015.

Smooth contract transition

2.19 Contract transition is an important part of the contract life cycle. It represents both a risk if renewal is left too late or the transition is badly handled, and an opportunity to learn from the experience of previous contracts.

¹⁵ The Department and Atos agreed to suspend service credits between September 2009 and March 2010 and then June and December 2011.

¹⁶ Comptroller and Auditor General, *Contract management of medical services*, Session 2012-13, HC 627, National Audit Office, October 2012.

Figure 9

ESA and PIP service credits accrued and paid between March 2014 and August 2015

The Department has applied service credits with fewer exceptions

	Employment and Support Allowance	Personal Independence Payment	
	CHDA (from March 2015, 6 months)	Capita	Atos
Service credits accrued (£m)	11	6	35
Service credits paid (£m)	8	5	6
Percentage service credits applied (%)	75	70	17

Notes

- Figures do not sum due to rounding.
- ESA includes service credits covering ESA and other assessments.
- Not all service credits accruing will be paid given, for example, providers claim 'mitigation' where factors outside their control impact performance, service credit suspensions agreed or a service credit cap applied.
- PIP Atos includes service credits accruing for two contractual service levels that were suspended during the recovery period (£25 million). The Department replaced, rather than suspended, these service levels with Capita. This explains some of the difference in the percentage of service credits applied.
- For ESA, the Department did not apply volume-based service credits for the first three months of the contract as the provider sought to stabilise performance. The annual volume target still applies. At the end of each year, services credits paid to date will be compared with annual performance, and any differences paid by or credited to the provider.
- As at August 2015, no FFW service credits have been applied.

Source: National Audit Office analysis of departmental data

2.20 In 2013, Atos notified the Department that it wished to exit the ESA contract. This followed their concerns over the negative impact of the contract on claimants, and Atos's reputation, staff and profitability. In March 2014, the Department and Atos agreed the exit terms. Atos had to complete a revised number of assessments and have 700 healthcare professionals in post at the time of transition.

2.21 The Department received an exit settlement from Atos at the time of transition. This included a cash payment and discounts against charges due for other services. We have not yet been able to fully audit the settlement due to delays receiving the evidence requested. In the past we have recommended the Department clearly sets out the financial position of revised commercial approaches and evaluates the impact of terminating a contract.¹⁷

2.22 In October 2014, the Department signed a contract with CHDA, a subsidiary of MAXIMUS UK, to replace Atos by March 2015. The Department, Atos and CHDA had four months to transfer services which included over 1,400 clinical and administrative staff, 30 assessment centres managed by Atos and access to the IT infrastructure developed by Atos. The Cabinet Office recognised the challenges of such a tight timetable and seconded a member of staff to the Department to support the transition between providers and earlier negotiations.

Figure 10 Average outstanding time for providers to return assessment reports between June 2013 and August 2015 against recovery plan milestones

The Department and providers took too long to agree improvement plans, during which time performance worsened

Capita Region 2

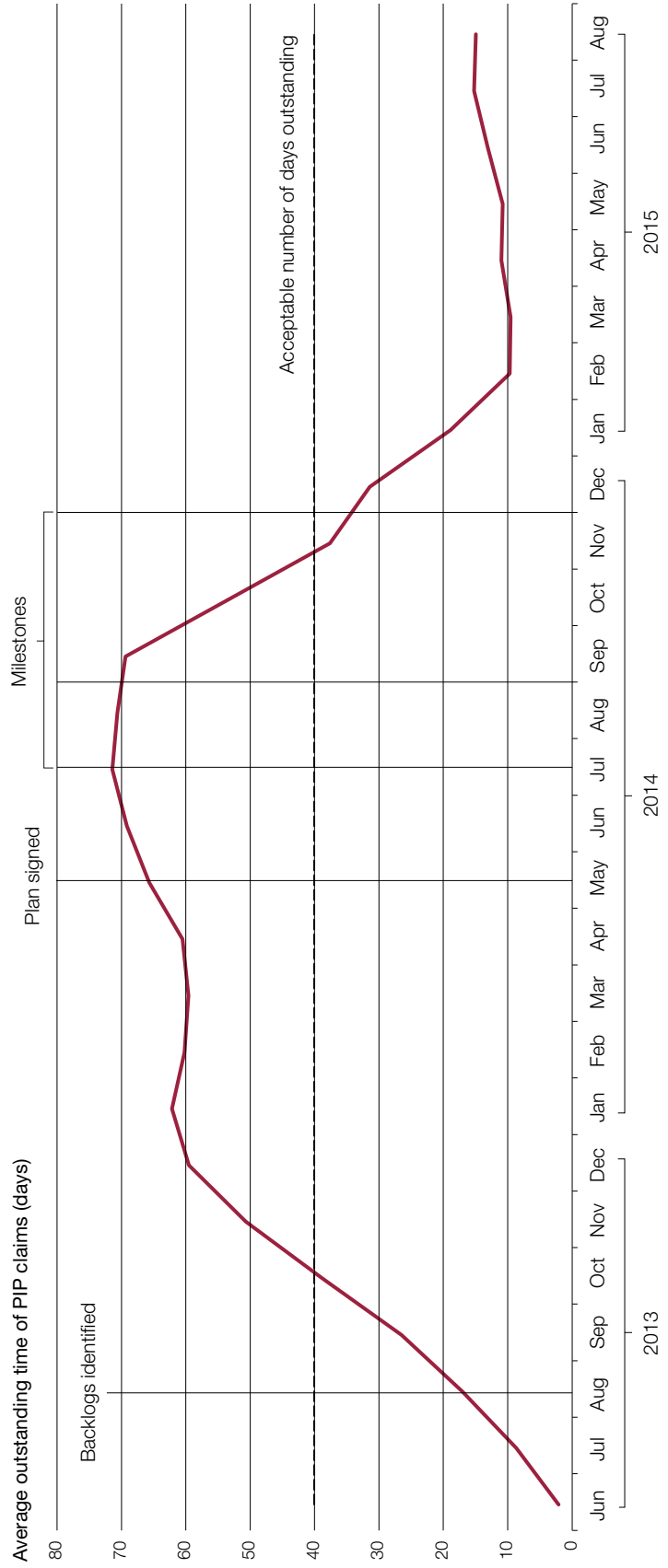
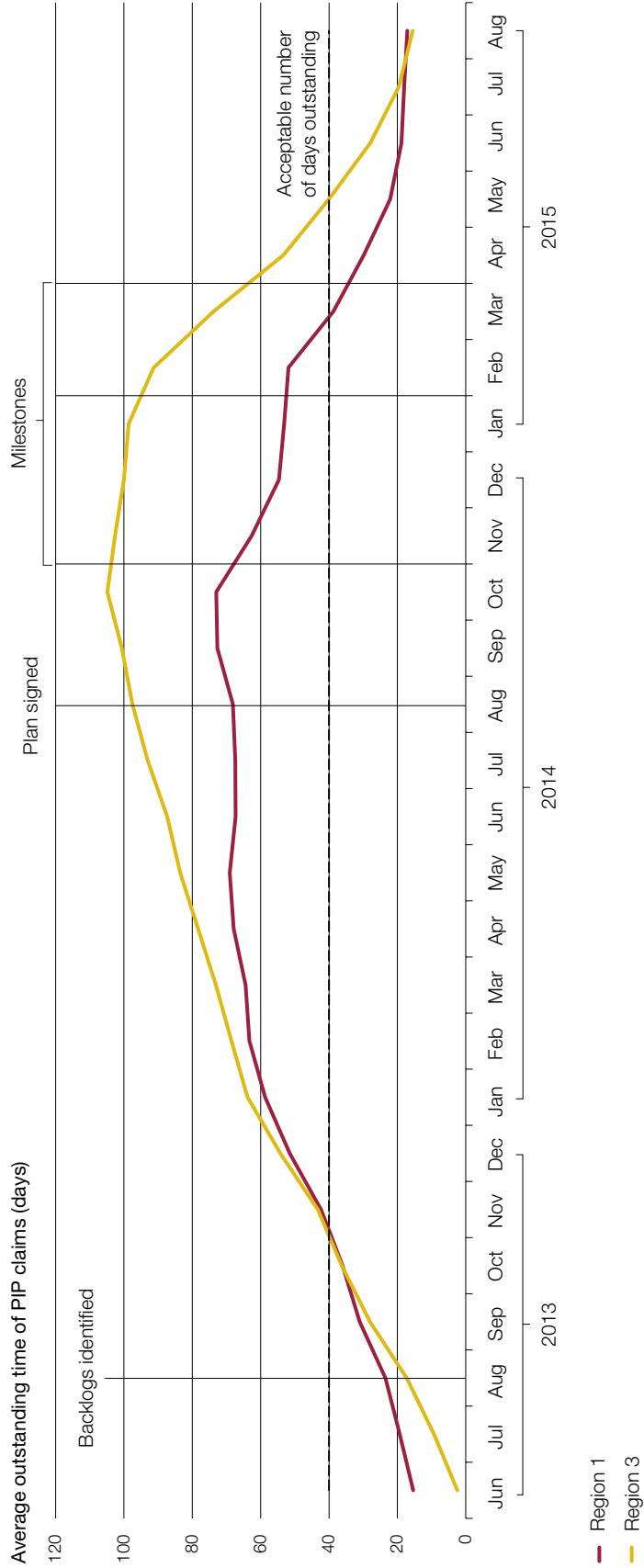


Figure 10 continued
 Average outstanding time for providers to return assessment reports between June 2013 and August 2015 against recovery plan milestones

Atos Regions 1 and 3



Notes

- 1 Nationwide processing of new claims began in June 2013.
- 2 Shows the average number of working days that claims outstanding at the end of a calendar month have been awaiting processing. For PIP, the contractual target is 40 days. This compares to a 30-day target for providers to return assessment reports to the Department.

Source: National Audit Office analysis of provider data

2.23 The Department, Atos and CHDA all consider the transition to have been well-managed. After signing the ESA contract, CHDA developed detailed transition plans. In November 2014, all three parties signed a legal agreement to work together. Success factors included tripartite governance arrangements, shared goals and reporting arrangements across specific work streams with clear deadlines.

2.24 More broadly, the Department needs to prepare for transition earlier. The actual transition between ESA providers was only six months earlier than the planned end date of the original contract. Despite this, the Department had done limited preparatory work for contract transition. In April 2015, it identified lessons learned from the transition which included better understanding processes and prioritising issues earlier.

2.25 **Figure 11**, our assessment of lessons learned, suggests the Department has learned from recent experience in the way it manages contracts once they are running, but has missed opportunities to improve the contract approach. We consider the set-up of assessment contracts in the remainder of this part.

Figure 11

Department's response to lessons from PIP and earlier ESA contracts

The Department has learned lessons in contract management but missed opportunities in contract set-up

	Lesson	Reflected in later ESA and FFW contracts	
Contract management	Unclear roles and responsibilities create confusion	Yes	Dedicated contract owner with primary responsibility
	Improved understanding to identify and respond to performance	Yes	Weekly (or daily liaison) with providers Speedier response (ESA)
	Need to gain assurance over provider performance	In part	Departmental teams audit ESA assessment report quality and independent auditors assess FFW data No independent verification of other data systems Open book access
Contract set-up	Tight procurement times lead to unresolved issues and costs	No	Short timetables for FFW and latest ESA contract led to unresolved issues
	Unrecognised, uncertain assumptions create risks to service (and increased cost/reduced market interest)	No	ESA contract allows one change for allowable assumptions Lack of rigorous testing of ESA volume targets
	Contracts need to be flexible to respond to uncertainties	No	ESA and FFW do not have defined contract review period
	Costs should be simpler and more transparent	Yes	Clearer financial models and pricing structures
Strategic approach	Multiple providers reduce risk of provider failure and increase competitive pressure	In part	Moved to three regional contracts for PIP, but still uses single provider for other contracts Contractor failure identified as a high risk

Note

1 Lessons learned include those identified by the National Audit Office and the Department.

Source: National Audit Office analysis

Underlying challenges in the development of contracts

2.26 In previous sections we found that in many cases the Department has strengthened the way it manages contracts and invested heavily in ways to monitor and manage performance. But actively managing providers within existing contracts cannot solve all problems arising from how contracts were set up. In this section we review the Department's approach to contracts.

Unclear approach to risk and incentives

2.27 In developing any contract the Department should set out the distribution of risks and create appropriate incentives for providers. The central role of assessments in the Department's claim decision-making process makes it particularly important to clarify these risks and incentives.

2.28 The Department has adopted different financial and contractual models for assessment contracts. It has introduced additional ways to incentivise performance but has not yet set out a clear approach to balancing risks and incentives in different circumstances (**Figure 12**). This results in challenges with:

- **Consistency between the Department's approach to setting up contracts and the way it manages those contracts.** CHDA and HML raised concerns with us, and the Department's internal auditors, that detailed oversight requirements were inconsistent with the nature of the contract and what they understood during contract procurement – a more hands-off outcomes-based form of performance management.
- **Aligning incentives created by volume targets and service credits.** Following concerns over the ratio of face-to-face to paper-based assessments in the new ESA contract, the Department introduced separate targets for each type of assessment and reduced the number of paper-based assessments required from 294,000 to 225,000. This strongly incentivises CHDA to focus on face-to-face assessments in the first year. The contract incentivises the provider to complete large volumes – if targets are not met, service credits could eliminate the provider's profit.
- **Matching risk and control.** In the new ESA contract, the Department set a volume target but does not guarantee the number of assessments referred to the provider. The provider's only recourse will be to take action for contract frustration if there are insufficient referrals.¹⁸ Based on new claims alone, CHDA estimated it will not have enough to provide the required number of assessments in all regions. Having suspended the reassessment of existing ESA claimants in early 2014, the Department began reassessments in December 2015 and will gradually assess those already outstanding from January 2015.

¹⁸ In claiming 'contract frustration' a contracted party can seek to set aside a contract where unforeseen events either render contractual obligations impossible, or significantly change the party's main purpose in entering into the contract.

Figure 12

Comparison of contractual mechanisms across ESA, PIP and FFW contracts

The Department has introduced additional contractual measures to incentivise performance

	Employment and Support Allowance		Personal Independence Payment	Fit for Work
	Atos	CHDA		
Contract date	September 2005	October 2014	July 2012	July 2014
Service cost basis	Fixed/variable unit cost	Target cost with incentivisation fee	Volume banded output pricing	Service fee/fixed unit cost
Cost gain/pain share	No	Yes	No	No
Agreed profit level	No	Yes	No	No
Service credits	Yes	Yes	Yes	Yes
Service credit cap	30% of monthly invoice	Actual fee +5% actual cost	15% of monthly invoice	15% of monthly invoice
Early performance award	Yes	Yes	No	No
Milestone payments	No	Yes	No	Yes
Allocation of risks				
Volume variations	Provider	Provider	Provider	Provider
Cost increase	Provider	Mixed	Provider	Provider
IT	Provider	Department	Mixed	Provider
Estate	Mixed	Department	Provider	Provider
Insufficient staff	Provider	Provider	Provider	Provider
Decision wrong	Department	Department	Department	n/a

Notes

- 1 Reflects initial contract. Alongside cost mechanisms, non-financial mechanisms such as performance improvement plans and reputational risk incentivise performance.
- 2 Early performance awards paid when certain conditions met over the start of the contract. Milestone payments to be agreed by both parties.
- 3 The Department can terminate the contract if the service credit cap applied every month over three month rolling period or in any six months across a rolling 12-month period.
- 4 Allocation of risks National Audit Office assessment.

Source: National Audit Office analysis of contracts

2.29 We recognise that the Department's contracts are evolving and that in some cases it has had to increase oversight in response to performance issues. Our concern is that the Department relies on a reactive approach to managing risks and incentives which has continued even into recent contracts for FFW and ESA.

Insufficient challenge of targets and assumptions

2.30 In our reports *Personal Independence Payment: early progress* and *Welfare reform – lessons learned*, we found that insufficient challenge of critical assumptions had led to problems with performance which were difficult to resolve.¹⁹ We recommended that the Department model and test assumptions and encourage challenge from providers.

2.31 The Department has significantly improved its monitoring and approach to critical assumptions in existing contracts. It has revisited the PIP contract and performance measures, and strengthened the quality of information and monitoring of contractual measures.

2.32 We are concerned that in more recent contracts the Department has continued to develop targets and assumptions without sufficient evidence. Getting such assumptions right is crucial for bidders to determine whether the Department's requirements are deliverable and at what price. For example:

- **Setting high volume targets without fully considering feasibility.**
The Department introduced a target of 1 million ESA assessments to be carried out in 2015-16. It told us it derived the non-negotiable target from the number of assessments needed to achieve expected benefit savings rather than from discussions with bidders or modelling of the possible number of assessments. The provider is not on track to meet the target in the first year.
- **Rejecting provider concerns.** Bidders told us that they had raised concerns about the target number of assessments for ESA with the Department during the bidding and asked it to consider other options. The Department did not do so and decided to rule out any bids with lower volumes, despite previous difficulties with these contracts. One experienced bidder withdrew from the process because it could not meet the required number of assessments.
- **Failing to share evidence about operational assumptions.** During the ESA bidding process, CHDA used a capacity model that assumed 95% of staff would still be in post after one month. In practice around half of those recruited by CHDA completed their training. CHDA told us that the Department did not challenge CHDA's assumption despite being aware that only 70% of staff completed their training with the previous provider. CHDA has developed plans to improve training and staff retention.
- **Failing to inform providers about wider policies affecting the contract.** The Department had to revise the FFW implementation approach after the contract was signed but had not informed the provider, HML, about marketing restrictions during the election period. This contributed to delays in ramping up the service and a significant contract variation four months after the initial contract. Internal audit found that the contract variation was well managed.

¹⁹ Comptroller and Auditor General, *Welfare reform – lessons learned*, Session 2015-16, HC 77, National Audit Office, May 2015.

2.33 In the Department's view it considered and challenged potential bidder optimism and did not know bidders' assumptions were unrealistic. It told us optimism in targets was not its responsibility, rejecting provider concerns is a normal outcome in negotiations, and that as providers signed contracts they had accepted the contract terms and risks.

2.34 In our view, contract risks are never fully transferable. It is important to set achievable but challenging targets based on an open discussion of assumptions and risks. Although the Department provided evidence of its review of ESA bidders' assumptions, we were not able to assess the level of challenge.

2.35 In July 2015, the Department and CHDA agreed changes to the latest ESA contract. An 'allowable assumptions' clause allowed them to agree the accuracy of certain assumptions, but only once up to ten days after the start of the service. This reduced the number of assessments required in the first year from 1 million to 980,000 as fewer staff transferred from the previous provider than the contractual assumption agreed by the Department and CHDA. Going forward, if assumptions – such as the proportion of staff completing training – are identified as no longer valid, any changes to requirements will be considered as normal contract changes. The Department subsequently reduced the number of assessments on which service credits would apply to 911,000 by requiring 69,000 fewer paper-based assessments.

An inconsistent approach to contracts and providers

2.36 A clear overall strategy helps to improve performance and protect value for money on individual contracts. It increases opportunities to learn from experience and ensures that short-term priorities are balanced with longer-term market development.

2.37 The Department has begun to take a more integrated approach to contracts. In 2014, it set up a central risk register to monitor risks across assessment contracts. Programme directors meet regularly to discuss common issues such as peaks in recruiting healthcare professionals. Within the last 12 months the Department has reviewed both the provider and healthcare professional markets to understand capacity and future risks.

2.38 Despite these steps the Department does not yet have a clear strategy for contracting-out assessments, citing uncertainty about the Spending Review settlement in autumn 2015 (**Figure 13** overleaf). It entered into a three-year ESA contract so it could consider how ESA assessments should be delivered. It is now exploring using regional contracts and has introduced new opportunities for completing assessments in different ways, such as using a small number of healthcare professionals to provide ESA assessments in-house.

Figure 13
Comparison of contract approaches

The Department has not adopted a consistent approach and has seen limited improvement in market interest

	Framework	Personal Independence Payment	Fit for Work	Employment and Support Allowance (CHDA)
Contract start	April 2012	July 2012	July 2014	October 2014
Contract approach				
Initial approach		National (2011)		Regional (November 2013)
Adopted approach				
Coverage	National/regional	Regional	National	National
Contracts	n/a	3	1	1 (plus in-house provision)
Rationale	Long-term plans to diversify; reduce procurement time	Develop market interest; greater flexibility	Consistency; reduce contract management costs	Short time frame available; in-house provision mitigates market failure risk
Procurement approach				
Method	Open tender	Framework	Open tender	Negotiated procedure
Length (weeks)	6	13	16	7
Bids	39	19 (6 bidders)	6	7 (4 invited to negotiate of which 2 bid)

Notes

- 1 Before October 2014 the Department had a national contract with a single provider for ESA assessments. In November 2013, it requested expressions of interest to provide ESA regionally. It received 42 expressions of interest. In spring 2014, it terminated this tender process. Two bidders withdrew from the later negotiated procedure.
- 2 In 2011, the Department began to procure PIP assessments nationally. It restarted the procurement process regionally to mitigate the risk of supplier failure. One bidder withdrew leaving five bidders in Regions 1 and 3. One contractor, Atos, holds two of the three PIP contracts. Capita holds the third.
- 3 Procurement length measures the time between issuing the invitation to tender and submission of best and final offers.
- 4 Health Management Limited provides FFW across England and Wales. In Scotland it is delivered by the Scottish Government.

Source: National Audit Office document review

2.39 The Department and the Cabinet Office have recognised that the government plays an important role in developing the market for assessments and that potential providers are concerned about risks to reputation. The Department and providers recognise that inconsistency in contract approach, inflexibility in setting terms, and potential financial losses reduce the attractiveness of contracts. There is a risk providers continue to make losses on assessments contracts. In November 2015, MAXIMUS forecast a lower than expected earnings outlook given the slower ramp-up of the ESA contract.

2.40 The Department has not always followed through with efforts to improve market interest. In April 2012, it established a framework contract for providers to build expertise, better understand the market and develop potential providers' capacity. But it has not used the framework beyond the PIP contract in 2012. CHDA and HML told us that given the significant resources MAXIMUS committed to bidding for the framework they would like to see it used.

2.41 The Department is working with providers to develop a more partnership based approach for PIP. But the combination of strong statements of provider responsibility in contracts and the likelihood of missing ambitious targets, could discourage potential providers from bidding for assessments.

2.42 In our view, the Department has concentrated heavily on tackling immediate priorities and responding to changes over the last few years and must now develop a more systematic and considered approach. By summer 2016, the Department will need to decide how to procure future PIP and ESA assessments.

Appendix One

Our audit approach

1 This study examined whether the Department for Work & Pensions (the Department) has achieved value for money in its management of contracted-out health and disability assessments. This includes the contracts for assessments associated with Employment and Support Allowance (ESA) and Personal Independence Payment (PIP) benefits and the Fit for Work (FFW) service. We do not consider the PIP contract for assessments in Northern Ireland or the Department's arrangements for FFW in Scotland. As the contracts considered are at different stages we considered the current situation and how things had changed over time. We reviewed:

- recent performance against expected levels;
- how the Department has set up contracts;
- the Department's approach to contract management; and
- the Department's approach to contracting-out assessments and the market.

2 Contracted-out assessments are an integral part of reforms designed to reduce benefit spending, better target support and reduce time off work. We do not assess the value for money or success of these wider reforms. Effective contract management will be one of many necessary conditions for achieving value for money in the long-term. We consider whether the Department's approach to contract management is value for money.

3 To structure our review, we used the National Audit Office's new commercial assessment framework. The framework has been developed to help audit commercial relationships across seven stages of a contract's lifecycle. It uses existing knowledge and experience from across government to identify what good practice looks like. Our audit approach is summarised in **Figure 14** on pages 43 and 44.

Figure 14
Our audit approach

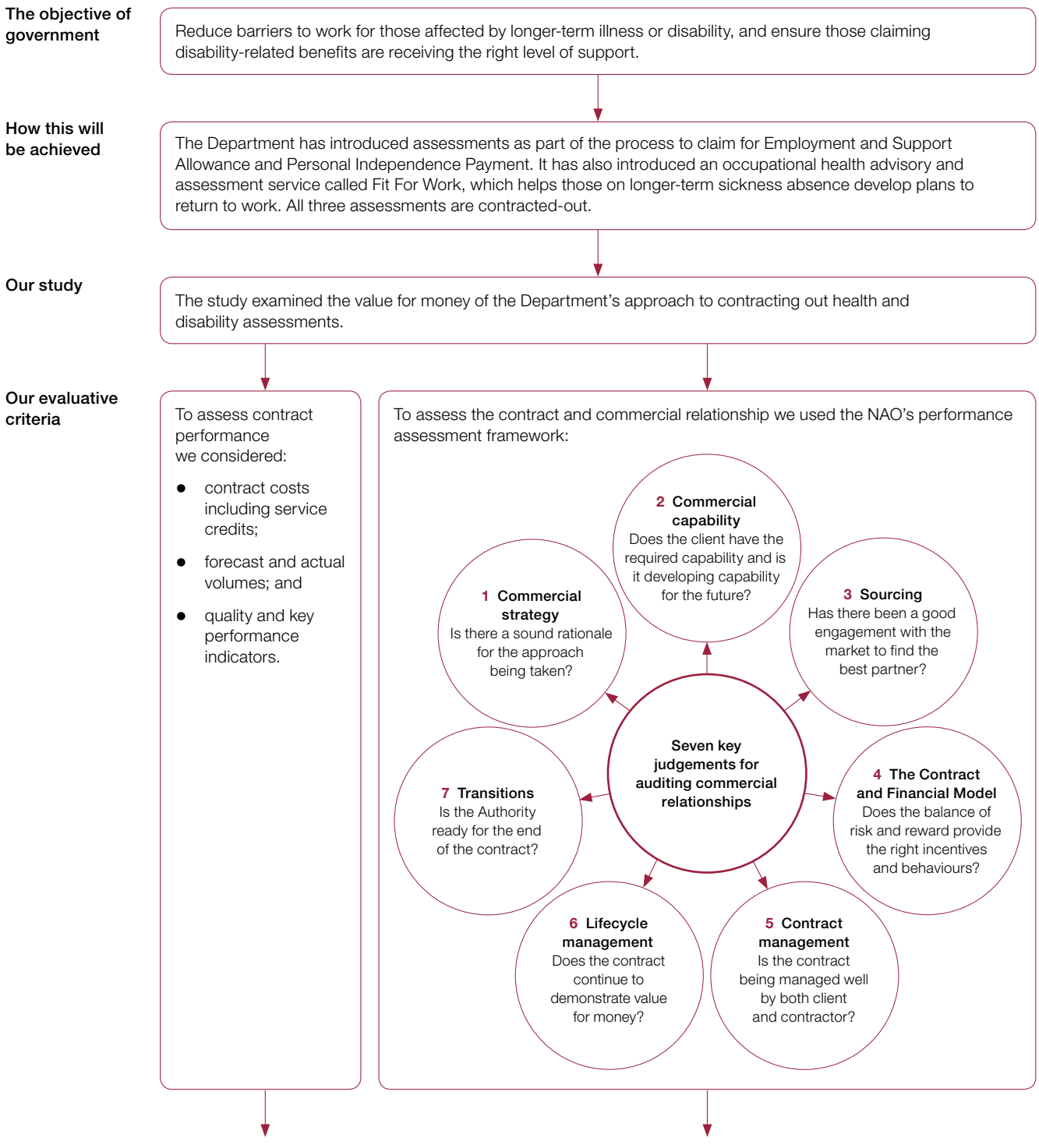


Figure 14 *continued*

Our audit approach

Our evidence

(see Appendix Two for details)

We examined:

- management information showing performance against service levels; and
- financial data across contracts and over time (including the application of service credits and incentives).

We assessed contract management by:

- interviewing members of the contract management and commercial teams;
- interviewing senior management at providers;
- reviewing assessment processes on site; and
- reviewing contracts, internal documentation and other communication with providers.

Our conclusions

The Department prioritised immediate operational problems by working with providers to increase capacity, improve contract management, and tighten performance monitoring and oversight. Progress has been made reducing outstanding claims and PIP waiting times.

Despite this, the Department has not yet achieved value for money in its management of contracts. It now expects to pay more and is still not achieving volume and assessment report quality targets. Even if it stabilises performance, it needs to tackle underlying capacity challenges and set challenging but realistic targets. Otherwise its approach to managing contracts and critical assumptions risks perpetuating a cycle of optimistic targets, contractual underperformance and costly recovery.



Appendix Two

Our evidence base

1 To assess the value for money of the Department for Work & Pensions (the Department's) approach to health and disability contracts, we conducted analysis between July and October 2015.

2 We assessed the performance of the Department and contractors up to August 2015 by analysing:

- management information used by the Department to monitor providers and understand performance against agreed contractual levels. We triangulated this data against provider information;
- Departmental financial data to understand when service credits are applied and the use of incentive fees and other payments; and
- publicly available information to estimate the average cost for Employment and Support Allowance and Personal Independence Payment assessments. This included caseload numbers and estimated contract values. We adopted this approach because of commercial sensitivities associated with using information held by the Department. Limitations of this approach include using forecast data for the latest Employment and Support Allowance contract against actual data for the earlier contract and not being able to fully analyse the reasons for cost differences.

3 We assessed the Department's commercial approach and contract management against an analytical framework developed by the National Audit Office. The framework, covering seven stages of the contract lifecycle, outlined what good looks like. We undertook peer review using our existing contracting and commercial team's expertise to challenge our findings and help set them within wider government experiences. In assessing the Department we:

- reviewed the contractual documentation, including contract changes and Heads of Term agreements, in place for all contracts to compare contract set-up (such as use of service credits and incentives). This helped us understand the Department's contractual approach to risk allocation and uncertain assumptions;
- reviewed Departmental documents including commercial and programme board minutes, risk registers and commissioned reviews to understand the difficulties faced, how the Department responded to challenges and the approach to contracted-out health and disability assessments;

- conducted 13 semi-structured interviews with Departmental officials. Meetings were triangulated with further evidence to better understand the Department's approach to contracted-out assessments, how contracts worked and how they have been managed;
 - held four semi-structured discussions with providers to understand their perspective on how contracts are managed and the challenges faced. We met MAXIMUS to discuss contracts in place for Employment and Support Allowance and Fit for Work. We visited administration sites for both assessment services to understand how MAXIMUS managed their parts of the process. We met Atos Healthcare to discuss the earlier Employment and Support Allowance and Personal Independence Payment contracts. We did not discuss the Personal Independence Payment contract with Capita Business Services Limited because of ongoing commercial negotiations at the time of our report;
 - interviewed departmental officials from the Cabinet Office to understand their role and also perspective on the commercial risks faced by the Department; and
 - sought to analyse the financial impact of the early termination of the ESA contract. We identified offsetting payments but were unable to use the information available to us to fully understand the financial impact.
- 4** Throughout our review we requested evidence of the Department's challenge of bidders' assumptions during the new ESA contract procurement. The Department provided a timeline of meetings but there were no minutes of these meetings or evidence that assumptions had been rigorously tested.

Appendix Three

Contracted-out assessment costs

Figure 15

Actual and forecast Departmental spending on assessments, 2012-13 to 2016-17

The Department expects to quadruple spending on assessments

	2012-13 (actual) (£m)	2013-14 (actual) (£m)	2014-15 (actual) (£m)	2015-16 (forecast) (£m)	2016-17 (forecast) (£m)
ESA (Atos)	114	57	71	0	0
ESA (CHDA)	–	–	11	155	196
PIP	–	19	190	214	364
FFW	–	–	1	10	14
FFW Scotland	–	–	2	3	5
Subtotal	114	77	275	381	579
Other contracts					
In-house recruitment	–	–	1	2	5
FFW assessment assurance	–	–	0	1	1
Subtotal	0	0	1	4	7
Non-contract costs					
IT	0	0	1	12	14
Estates	0	0	1	5	5
Exit costs	0	0	15	(1)	0
Other	0	0	(1)	2	3
Contract management	Not provided	Not provided	3	5	5
Subtotal	1	0	19	23	27
Total	115	77	295	407	613
Percentage increase since 2012-13		(33)%	157%	254%	434%

Notes

- 1 ESA (Atos) and ESA (CHDA) costs cover the provision of ESA assessments alongside assessments for smaller benefits such as Industrial Injuries Disablement Benefit and Incapacity Benefit reassessments.
- 2 In September 2014, the Department contracted Pertemps, now APM, to directly recruit healthcare professionals. In March 2015, it contracted PricewaterhouseCoopers to independently assure FFW data.
- 3 Other non-contract costs include claimant expenses, quality assurance and income from other government departments.
- 4 Contract management costs do not include commercial staff.
- 5 Figures may not sum due to rounding.

Source: National Audit Office analysis of departmental financial data

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