

Outcome Based Commissioning

Lessons from contracting out employment and skills programmes in Australia and the USA

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Glossary

UK

BIS	Department for Business, Innovation and Skills
DWP	Department of Work and Pensions
FND	Flexible New Deal
LEC	Local Enterprise Company (Scotland)
NVQ	National Vocational Qualification
ORF	Output Related Funding
TEC	Training and Enterprise Council (England and Wales)
TfW	Training for Work
UKCES	UK Commission for Employment and Skills
YT	Youth Training

USA

HHS	Department for Health and Human Services
HRA	Human Resource Administration (NYC)
ITA	Individual Training Account
JTPA	Job Training Partnership Act
NYC	New York City
PIC	Private Industry Council
TANF	Temporary Assistance for Needy Families
WIA	Workforce Investment Act
WIB	Workforce Investment Board

Australia

AQTF	Australian Quality Training Framework
APM	Active Participation Model
DEEWR	Department of Education, Employment and Workplace Relations
IA	Intensive Assistance
JN	Job Network
JSA	Job Services Australia
TAFE	Technical and Further Education
VET	Vocational Education and Training system

Executive summary

Despite the relative effectiveness of recent reforms to the employment and skills system the Leitch Review (1996) identified some key problems. Welfare to work programmes had few incentives to focus on skills, job retention and progression; the skills system had little focus on employment outcomes; and the targets and incentives in both systems did not encourage a joined-up service for individuals or employers. The UK Commission for Employment and Skills (UKCES) subsequently proposed the integration of employment and skills provision and the use of outcome based commissioning. The Government is now seeking to implement such changes and to ensure that providers' success is defined and measured in terms of their responsiveness to labour market needs and the outcomes from their provision.

Debates about outcome based commissioning and contracting, and their application to employment and skills provision, have frequently referred to the experience of other countries, especially the USA and Australia. The USA was the first to introduce explicit performance and outcome standards in its employment and skills system and to connect these with financial incentives and penalties. Australia has sought to create quasi markets in its vocational education and training and is the only OECD country to fully privatise its employment assistance system where a major part of provider income is dependent on securing job outcomes.

This report assessed the commissioning and contracting processes through which employment and skills provision is procured in both these countries and sought to identify design and implementation issues that may have implications for the reforms currently being introduced within the British system.

The findings reveal that in the USA and Australia respective federal Governments increasingly have set explicit performance and outcome targets within wider reform strategies designed to increase employment rates, reduce welfare dependency and increase skills attainment and utilisation. Performance management systems have been redesigned with public sector employment and skills delivery agencies subject to greater scrutiny and accountability and, where service delivery has been made contestable, challenged by the entry of other providers, including those from the private sector. There are multiple variations in the performance and outcome standards that apply to training and employment services but in the USA they typically include job placement rates, earnings, retention in employment and, for training programmes, skills and qualifications obtained.

Studies in both countries show that delivery of employment and skills programmes is subcontracted to a wide range of public and private agencies with performance standards and outcome measures reflected in service delivery agreements and/or contracts with providers. The terms of such contracts differ widely, with varying amounts of provider income dependent on securing agreed outcomes or performance standards. Only in some welfare to work and employment programmes is a major part of provider income dependent on securing sustained job outcomes. It is important to note that these contracts are not exclusively outcome based and typically have other performance and process requirements embedded within them.

Views on the success of such contracting systems are mixed and even where the results may appear impressive, it is difficult to disaggregate the impact of the outcome based contracting system from that of other policy changes. Moreover, whilst the cost and efficiency gains claimed for US and Australian models appear significant relatively little is known about how far these gains have been offset by high transaction costs or reduced service quality, especially for the most disadvantaged.

There is evidence that minimising cream-skimming, creaming and parking are significant challenges in both public and private sector incentive and target driven delivery systems. Such risks may be reduced through contract design and oversight. The inclusion of measures related to job retention, wages and benefits, and earnings gains, for example, all help diminish any incentive to place participants into poor quality jobs. Measures indicating completion of assessments and activities and regular surveys of participant and employer experience help limit the ability of providers to service clients differently. The challenge is to design such process and outcome measures in ways that do not create unnecessary administrative burdens and allow providers flexibility in how they secure outcomes.

The findings show that the implementation of performance and outcome based commissioning and contracting has been dynamic and that government agencies and ‘purchasers’ frequently have had to revise performance standards and contractual terms as problems have arisen and conditions have altered. In both countries there has been much ‘learning by doing’ and constant adaptation as officials have sought to establish performance management and payment structures that now aim to increase the duration of job outcomes, reduce creaming, integrate skills provision, improve service quality, and control any potential for perverse incentives or ‘gaming’ of systems.

In this process much knowledge has been gained about different contracting models, the relationships between service delivery and performance incentives, and how to define relevant outcomes. This knowledge, and that developed within the UK, must inform policy makers’ efforts as they seek to operationalise employment and skills outcomes, such as those proposed by UKCES, into more effective performance management and contracting systems.

The review findings show that in both the USA and Australia there remain legitimate differences in the outcomes sought from ‘work first’ employment and welfare to work programmes and those sought from vocational education and training systems. Efforts to improve the connections and coordination between these ‘work first’ and skills development programmes are, however, hampered by these differences and by the distinct funding streams and bureaucratic mechanisms through which such outcomes are sought. Such problems are shared in the UK employment and skills system where variation in Government targets and incentives makes coordination and integration of services more difficult. This is particularly evident in the contrasts between the sustained job outcomes that DWP requires contracted employment providers to secure against the short term employment entries that enable Jobcentre Plus to meet its employment targets.

It is also clear in the primacy given to qualification attainments in the skills system with less regard given to subsequent employment or whether the skills acquired are actually valued and utilised in the workplace.

In addition to more general findings from this study there are three particular proposals that, when tested, might augment current efforts to better coordinate and integrate employment and skills provision in the UK.

The first proposal concerns how to better integrate skills provision within DWP employment programmes for the long term unemployed. It concerns adapting the redesign of job focused outcome payments within the Job Services Australia system for use with FND and other contracted out DWP programmes. It would involve giving incentives to providers to broker training places with employers and rewarding them when participants they have helped access training are placed in jobs that make use of the skills developed.

The second proposal concerns enhancements in the assessment of the employment outcomes from skills programmes and of the qualifications gained. This should involve the use of enrolment and destinations data, collected administratively or through leavers' surveys, to establish the employment and wage rates of participants. Such data could be used to establish whether participants improved their employment position as a result of their training and the extent to which they utilise any skills gained in their current employment. Such data could be combined into a measure of workforce quality as suggested in Australia.

Finally there would be value in swiftly reviewing the many contrasting outcome requirements that exist within the British employment and skills system, and in how they are measured, with a view to developing 'common performance' or 'return on investment' measures, similar to those being developed in the USA. Such agreed common measures would help minimise different performance, outcome and reporting requirements and facilitate co-commissioning and the alignment of skills and employment funding. They also would help facilitate greater coherence in the performance and outcome standards that providers have to meet. At the same time such a review could critically audit the varying contracting and financial practices of the different public agencies involved in procuring skills and employment provision. The aim should be how to simplify such requirements and, if budgets cannot be integrated, to consider the extent to which 'master contracts' might reduce complexity in the system and assess whether employment and skills purchasing might be better managed by the recently proposed single professional procurement agency.

1. Introduction

Since the 1980s the UK Government has procured skills and employment provision through and from a wide range of public, private and third sector agencies. Commissioning and contracting frameworks have been in a state of flux as successive reforms have sought to increase the accountability, efficiency and responsiveness of the system. Despite the relative effectiveness of reforms the Leitch Review found that the welfare to work system had no incentive to focus on skills and other interventions that would improve job retention and progression; the skills system had little focus on the employment outcomes of those improving their skills; and the targets and incentives in the employment and skills systems did not encourage a joined-up service for individuals (HMT, 2006, p. 131). These problems were exacerbated by the separate ways in which employment and skills provision are purchased, overly bureaucratic regulation and contract management, and performance targets and contracts, especially in the skills system, that have been focused on processes and outputs, such as qualifications, rather than outcomes.

The UK Commission for Employment and Skills (UKCES), established after the Leitch Review, has since proposed that outcome based commissioning is part of the systemic change needed to improve the efficiency and effectiveness of British employment and skills provision. UKCES suggests that the full transition to such a system should be part of a dramatic simplification of commissioning and contracting arrangements where providers' success is 'defined and measured' in terms of their responsiveness to labour market needs and the outcomes from their provision. In addition to the qualification outputs secured the outcome measures favoured by the Commission include 'progression in learning or work, wage gain, learning achievement, customer satisfaction and quality' (UKCES, 2009, p. 5).

Outcome based commissioning and contracting and the skills and employment system

Within Government there has been an increased emphasis on the use of outcome based commissioning and contracts in the management and procurement of a wide range of public services, especially in local government and social care (ODPM, 2005; Glendinning *et al*, 2006).

Outcome based *commissioning* refers to the overall process whereby a public sector agency identifies the service delivery outcomes to be secured, the procurement of such services, and the subsequent monitoring of their effective delivery. The desired outcomes tend to refer to measurable changes in the condition, behaviour and satisfaction of service recipients or programme participants. Outcome based *contracting* refers to the ways in which service providers are rewarded for securing explicit measurable outcomes. Such contracts typically combine start-up and service fees and they may include payments for intermediate or 'milestone' achievements. Crucially a significant portion of payment or other incentives are linked directly to the realisation of agreed outcomes (PST, 2009). Some outcome based contracts seek also to realise efficiency gains through transferring risk to providers, giving them greater flexibility in delivery, but paying full fees only in return for successful performance.

The use of outcome based commissioning and contracting in British employment and skills provision is most developed in the 'Commissioning Strategy' currently being implemented by the Department of Work and Pensions (DWP).¹ This involves radical changes in the design and delivery of contracted out employment programmes with DWP now seeking to work with a smaller number of prime providers to be paid increasingly in respect of sustained job outcomes. DWP contracts now have differing combinations of service fee and outcome payments but the proportion dependent on sustained job outcomes can, as in the Flexible New Deal, account for 80 per cent of the contracted payment. Other developments include experiments with 'invest to save' and 'accelerator' funding contracts to test the effectiveness of differentiated outcome payments with varied incentives for providers to get benefit recipients into sustained employment.

Parallel changes are underway in the procurement and delivery of skills provision as the Government seeks to create a 'demand-led' system, with provision being made more responsive to employers and eligible adults through skills brokers and learning accounts.² Performance of skills programmes is now commonly assessed in terms of attainment as well as enrolment or 'starts' but the use of outcome based payments is less extensive. Nevertheless pre-employment training and other programmes targeted at workless people reward sustained job outcomes and 'Train to Gain' funding is paid in instalments, with 25 per cent contingent on the learner achieving a specified qualification (NAO, 2008, p. 13).

The Department for Business, Innovation and Skills (BIS) plans to extend job outcome based funding "to a broader spread of provision where employment based outcomes are a key purpose of the learning" (BIS, 2009, p. 61) and the 'single purse' for training workless people planned by BIS and DWP "will reward providers for getting people into sustained employment with progression" (DWP, 2009, p. 61). In the long term DWP's 'Commissioning Strategy' envisages that as employment and skills provision becomes more integrated the Department will build longer-term incentives into contracts 'perhaps' involving outcome payments being stretched over 18 months (DWP, 2008, p.22).

At local level employment and skills partnerships, in particular in London, are also seeking to extend outcome based contracting by, for example, paying for employment retention that is sustained for 52 weeks and seeking to integrate employment and skills provision within a single outcome based contract. Opportunities for such co-commissioning of employment and skills outcomes remains limited, however, with BIS and DWP programmes procured through separate systems and still largely steered by different targets that prioritise either employment outcomes or attainment of qualifications.

¹ DWP is responsible for the benefit system and employment programmes throughout GB. In Northern Ireland these services are delivered through the Department of Social Development and Department for Employment and Learning. The latter Department has introduced a similar contracting model as DWP with prime contractors now delivering 'Steps to Work' which replaced the New Deals for the unemployed in Northern Ireland in 2008.

² Adult learning and skills provision is devolved to Scotland, Wales and Northern Ireland, and from April 2010 such provision became the responsibility of the Skills Funding Agency (SFA) in England.

The research and report

Debates about outcome based commissioning and contracting, and their application to employment and skills provision, have frequently referred to the experience of other countries, especially Australia and the USA. This report assesses the commissioning and contracting processes through which employment and skills provision is procured in both these countries and seeks to identify design and implementation issues that have arisen and the implications these may have for the British employment and skills system.

The research involved a review of literature from both countries, including official reports and evaluations, independent studies from various policy institutes and academics and findings from audit, oversight and regulatory authorities. The report briefly describes how central government in both countries manages the performance of their respective employment and skills systems. It considers the ways in which public sector purchasers in the USA and Australia have designed contracts and outcome measures to promote job placement, retention and skill acquisition. The paper evaluates debates about the effectiveness of these contracting mechanisms and their impact on service users and outcomes.

Procurement of employment and skills programmes

In most OECD countries employment and skills provision traditionally has been delivered through public sector agencies, colleges and institutes linked with trade unions or employers. Where provision has been contracted out the various agencies responsible for purchasing typically specified the detailed design of the particular employment intervention or training course to be delivered. The public body also usually determined the price to be paid, the terms of the contract, and that payment would take the form of recurrent funding, a grant, staged payments to the provider or fees paid for services delivered.

The ‘performance revolution’ that gathered pace in the UK and a number of other countries in the 1980s saw the public bodies responsible for organising such services adopting a wider range of management techniques. Clearer distinctions were made between those who purchased and those who provided services and conventional public service models of hierarchical planning, bureaucratic control and budgetary allocation were reframed as market-based transactions. This often involved management via performance agreements and contracts. Many public services were subject to ‘market testing’ and/or were contracted out to private providers. Such changes enabled the purchaser to shift the focus of their relationships with public sector and external providers from ‘inputs’ and processes towards securing the specific results that governments wanted. Greater emphasis was put on measuring and paying for ‘outputs’ and, more recently, for the ‘outcomes’ secured.

This transition took place initially in the USA and was associated with the introduction of explicit and measurable performance standards in the delivery and procurement of public services. These were first introduced to the employment and skills system through the 1982 Job Training Partnership Act, a programme targeted at the unemployed and disadvantaged youth. Through this legislation funding and purchasing power were devolved to states and, through them, to a national network of employer led Private Industry Councils (PICs). Significantly, JTPA linked explicit performance outcomes with financial incentives to motivate agency staff. The federal Department of Labor was able to reward high performing PICs with bonuses amounting to as much as 20 to 30 per cent of its regular budget which then could be used with more flexibility than could mainstream funds (Nataraj Kirby, 2004, p. 54). These incentive systems were reflected in the contracts and payment systems between PICs and delivery subcontractors and by the end of the 1980s 80 per cent of PICs were making at least some element of payment to their subcontractors dependent on performance outcomes (Felstead, 1998).

In time JTPA outcomes were amended to include placement in unsubsidised employment, retention for not less than six months in such employment, increased earnings, and skills acquisition – including basic skills and credentials. The standards established under JTPA served as the ‘prototype’ for their extension to other federal employment and training programmes, including the welfare to work programmes targeted at lone parent families (Heinrich, 1999).

The US approach influenced other countries. In the UK Training and Enterprise Councils (England and Wales) and Local Enterprise Companies (Scotland) were modelled on PICs. Between 1987 and 2001 these employer led entities were funded through performance based contracts with an increasing proportion of funding dependent on job outcomes and qualifications gained (see Appendix A). Outcome contracts subsequently were central to the design of the new market based employment services systems introduced in Australia and some other countries, including the Netherlands (Ingeus, 2008; Lilley and Hartwich, 2008).

The advantages and risks involved in delivering employment and skills provision through outcome based contracts

The transition to outcome based employment and skills procurement offers potential for innovation, flexibility and efficiency savings, and can act as a powerful tool for driving institutional and organisational change. It also poses new challenges to policy makers who must design contracting systems that balance the incentive effect of outcome payments with the entitlement of service users to equitable treatment. Such challenges sometimes have gone unmet. Poor design in outcome based incentives combined with ‘trade-offs’ in programme objectives have been associated with risks to service access, costs, quality and accountability (Considine, 2005; Sol and Westerveld, 2005; Finn, 2008).

Three particular risks are generally held to be heightened by outcome based or pay-for-performance contracts. The first is ‘cream-skimming’, where contractors, paid by results, select more job ready or more easily trained participants who enable them to meet targets rather than selecting those who might gain more in the longer term. This is a particular risk when the group eligible for a service exceeds the number of available places and/or when providers can choose whom to admit to a service. ‘Creaming’ can occur even when the provider is required to take designated participants. The risk then is that a provider may, deliberately or unconsciously, concentrate efforts on those participants perceived as more easily trained or likely to be faster placed in employment. The third risk is ‘parking’ where more costly to help participants receive only minimal services and make little progress in a programme. Arguably the most disadvantaged, those with the greatest employment barriers, are the most likely to be ‘parked’.

These risks are thought to be further exacerbated in the strongly ‘work first’ welfare to work regimes of Australia and the USA. It is argued that contract incentives deter providers of employment services from investing in the education and skills of participants due either to potential delay in early job placement or on the grounds of cost, or both.

Other risks involve the balance between the flexibility given to providers to facilitate innovation in delivering contracted outcomes and the degree and form of regulation and inspection required to ensure the quality of service delivery. There is also concern about the impact that poor provider performance has on the quality of service delivery as cash flow is squeezed from failure to secure outcome payments. These risks, including that of provider failure, are even greater when external economic shocks, such as the recent ‘great recession’, play havoc with earlier assumptions and actual outcome performance, even amongst the higher performing providers.³ Additional concerns include the potential for providers to ‘game’ the system by, for example, using operational expertise to secure outcomes for little effort. At its worst this may involve the falsification of job outcomes or learning achievements.

The case studies that follow assess the experience of outcome based commissioning and contracting in skills and employment services in the USA and Australia. They describe how the respective federal governments set objectives and outcomes for their employment and skills systems and hold states and, through them, providers accountable for their performance. The report analyses how employment and skills performance and outcomes are defined and rewarded, and reviews findings on the impacts of the contracting systems through which provision is commissioned. Given the diversity of delivery systems in the USA, detailed consideration is given to New York City as it has extensively used performance based contracting, with provider income heavily dependent on sustainable job outcomes.

³ The recent increase in British unemployment is one of the factors that undermined the performance and viability of the outcome based funding model through which the Pathways to Work programme has been delivered (Hudson *et al*, 2010).

2. Performance standards and welfare to work and workforce development programmes in the USA

The transition to commissioning and paying for outcomes in the US employment and skills system occurred within a broader process of public sector reform. From the 1980s federal and state programmes increasingly have used measurable standards, outputs and outcomes and performance has been steered through both positive and negative incentives. Federal agencies hold states accountable for performance and, in turn, are accountable to the Congress and Office of Management and Budget for meeting legislative requirements and related performance standards.

The development of employment and skills performance measures and the increased emphasis on outcome incentives has been associated with two major changes in the US workforce development and welfare systems. These were the Personal Responsibility and Work Opportunity Reconciliation Act (1996), designed to 'end welfare as we know it', and the replacement of JTPA with the Workforce Investment Act (WIA) (1998). These federal programmes are managed by separate departments at the national (and often the state) levels, with the Department for Health and Human Services (HHS) responsible for 'welfare to work' and the Department of Labor responsible for WIA.

Welfare to work performance standards

The 1996 welfare legislation replaced earlier programmes for low income parents with a new time limited cash entitlement: 'Temporary Assistance for Needy Families' (TANF). It defined a number of key purposes for TANF, including the reduction of welfare dependency through the promotion of 'job preparation, work and marriage'. The legislation created a 'block grant' which gives states flexibility in benefit design and programme delivery in return for meeting work participation rates and continuing to match federal with state resources.

HHS utilises a range of performance measures to monitor and assess state progress but there is particular emphasis on the work participation rate where the legislation requires states to enrol 50 per cent of all families and 90 per cent of two parent families in work or work related activities for specified hours per week. HHS also assesses state progress on moving TANF recipients into work through outcome measures on job entry, job retention, and earnings gain; and monitors any increase in children living in married, two-parent families.

The agency has a number of incentives and penalties to steer state performance. Incentives include a 'High Performance Bonus' system⁴, where states may be paid up to a maximum of 5 per cent of their annual federal TANF award. Penalties apply only, however, to work participation rates, which give these standards a higher priority. Where participation rates are unmet HHS will send a penalty notice to the state concerned. The state then has the opportunity to avoid a penalty by providing reasonable cause or submitting a compliance plan indicating how it will ensure that parents receiving cash benefits will meet the required work participation requirements.⁵

The 1996 legislation further allowed states to contract out all services, including eligibility for TANF financial assistance, and to let contracts to faith based organisations on a new basis (known as 'charitable choice'). When implementing the new system states and local governments reorganised their welfare delivery systems to provide work focused eligibility and case management services and typically expanded employment programme and service capacity through contracts with voluntary sector and private providers. This expansion in contracted out provision was associated with an increase in the use of financial incentives linked to outcomes, especially in states such as Wisconsin and in cities such as New York (Bryna Sanger, 2003; De Parle, 2005).

Workforce development performance standards

Whilst states were implementing welfare reform the US Congress passed the Workforce Investment Act (1998), overhauling the federally funded employment and training system. WIA required states to replace Private Industry Councils with employer-led state and local Workforce Investment Boards (WIBs). These bodies were given a stronger policy role including a remit to secure more effective connections between workforce and economic development.

⁴ One of the high performance outcomes is a 'success-in-the-workforce rate' measured by combining the job retention rate and earnings gain rate and the change in each of these rates over the previous year.

⁵ The impact of the 'work rate' requirement was undermined by a rapid fall in the number of welfare clients which meant most states met their targets easily, leading to significant variation in work obligation regimes. This was controversial and federal policy makers criticised those states that were not implementing the legislative intent designed to require more TANF cash recipients to engage in work or work activities. State flexibility was subsequently reduced by the Deficit Reduction Act (2005) which tightened rules regarding the measurement of caseload reductions and work participation standards, and restricted the employment related activities that could be counted towards meeting requirements.

WIBs were required to overcome fragmentation through the creation of a 'one-stop' delivery system in which local agencies operating 18 federally funded programmes are required to participate. Up to three possible types of services are provided, depending on individual needs and eligibility. These comprise (Silverberg *et al*, 2004, p. 149):

- Core services – primarily information on employment opportunities – which are available to all service users.
- Intensive services, for those needing more assistance. These include individualised assessments, case management services, and short term pre-vocational courses such as language training or basic adult education.
- Training services which are primarily offered to eligible individuals, such as dislocated (redundant) workers or disadvantaged adults or youth, for whom the two previous services have proved insufficient in helping them to obtain employment.

One aim of the WIA reform, reinforced through the sequencing of services, was to place greater emphasis on job placement, in contrast with the previous JTPA emphasis on increasing individual human capital through training. Federal funding for WIA also was progressively reduced which further constrained investment in more expensive forms of vocational training (Eberts, 2009).

When providing access to training, local WIBs generally have to provide eligible individuals with training accounts (ITAs). These vouchers or accounts take many forms and service users have varying degrees of guidance and freedom in how they use them. Individuals can select providers using comparative performance and cost information generated from management information and data given by providers. Providers normally have to be registered with the WIB to be eligible for referrals and to receive ITA funding and actual payment systems vary from state to state.

There are specified federal performance measures associated with WIA for which states and WIBs are held accountable. These incorporated many of the JTPA standards such as entry into unsubsidised employment, retention and earnings after six months, but they also now explicitly included skills attainment and 'customer satisfaction'. States were required to test satisfaction ratings by both individuals seeking employment and employers looking for qualified workers (Nataraj Kirby, 2004, p. 57).

'Performance goals' are negotiated with each state and based on historical data, economic conditions and services provided. When agreed the goals are incorporated into a five-year workforce development plan. Programme delivery is the responsibility of the state which has some latitude to modify and augment federal performance standards.

A state that fails to meet its agreed level of performance for one year is given 'remedial' support and assistance. After two years of failure it may be subject to a five per cent reduction in its annual WIA grant. Similar conditions often apply to state contracts with providers where some states may impose financial penalties for continued failure but where more generally weak "performance on required measures appears to be more important in contract re-competitions and exercise of subsequent-year options" (Dunham *et al*, 2006, p. III-12). If a state meets or exceeds their performance targets they are eligible to receive incentive grants ranging between \$750,000 and \$3 million (Nataraj Kirby, 2004, p. 58).

Outcome based contracts in the US employment and skills delivery system

There has been no comprehensive review of the performance standards or the contracting out of welfare to work or workforce development services in the USA. There are, however, various studies which give insights into the use of performance based contracts including into those jurisdictions which have made greater use of outcome based payments to steer provider behaviour.

Each of the nearly 600 local WIBs is responsible for administering the WIA programmes in their area and for contracting with local organisations to provide services. Most WIBs subcontract programmes, services and 'one stop' centres to a wide range of public, for-profit and non-profit organisations, which also may include local secondary school districts and community colleges. Local delivery areas and providers usually are held accountable for their performance against a combination of process and performance standards that include job placement rates, earnings, retention in employment and skills and qualifications obtained. Failure to meet these standards may result in financial sanctions whilst high performance is rewarded.

Surveys of welfare to work provision suggest that nearly all states contract out at least some of their employment assistance services and several states contract out the delivery both of case management services, employment programmes and the payment of cash benefits (GAO, 2002; McConnell *et al*, 2003; Bryna Sanger, 2003). Typical outcome measures used in such contracts include participation in work activities, employment placement, job retention, and wages or earnings. Other process standards measure, for example, the number of programme enrolments, completion of assessments, and accuracy of referrals.

Studies of the US welfare and workforce development market have revealed multiple variations in performance standards and in the scale and types of contract favoured. Many states and WIBs have developed their own performance standards and reporting systems, especially as outcomes on federal measures take time to feed through, and programme managers need management information more quickly.

One review of welfare to work contracts distinguished between ‘fixed price’, ‘cost-reimbursement’ and ‘pure pay-for-performance’ variants (McConnell *et al*, 2003, p.xx). In practice many states used ‘*hybrid contracts*’ seeking to establish a balance between performance incentives, provider viability, and the delivery of particular services and outcomes. Even in the locality with the highest proportion of pay-for-performance contractor viability was underpinned by a fixed monthly payment of 15 to 25 per cent of their budgets, irrespective of their performance (McConnell *et al*, 2003, p.xxii).

It is important to note that in most parts of the USA the proportion of provider income dependent on employment outcomes tends to be relatively low, ranging between 10 and 20 per cent. The key incentives in the US system concern the requirement that service providers meet a range of performance and outcome standards to remain eligible for funds or face the risk that a purchaser will choose not to renew a contract in an environment where annual contracts or renewals are the norm. In Wisconsin, for example, a provider will be given a ‘Right of First Selection’ if they meet required performance standards with the contract only put out for competitive tender if the existing provider fails to meet such standards. It appears that the US performance system for skills training and welfare to work has, as with the earlier JTPA, tended to rely “more on procedural sticks than [outcome] carrots” (Felstead, 1998, p. 47).

There are exceptions with some states and cities who have designed contracts where provider income is far more dependent on securing job outcomes. New York City (NYC), for example, is a useful comparator because it has made extensive use of pay-for-performance contracts and lets some of the largest value welfare to work contracts in the USA. This partly reflects its use of prime contractors, who are awarded three year contracts, and the fact that the city has one of the largest welfare caseloads in the country.

Outcome based contracts in New York City

NYC has been at the forefront of implementing performance indicators, milestones and contracting in the delivery of public services (Krauskopf, 2008). This is reflected in the way it delivers its welfare to work and workforce development programmes.

Cash benefits and welfare to work programmes are delivered by the city's 'Human Resources Administration' (HRA) which operates through a network of 30 'Job Centres', staffed by public sector Job Opportunity Specialists, with responsibility for eligibility, case management and sanctions. The city's welfare programme has a strong emphasis on 'full engagement workfare' and employment placement.

Employment assistance services are delivered through a network of prime contractors. These comprise a relatively small group of for profit and non profit organisations who deliver a mainstream 'Back to Work' programme, a 'WeCare' programme targeted at participants with physical and/or mental health conditions, and a 'BEGIN' programme which provides adult basic education and language training. 'Back to Work' is largely funded through job outcome payments; Wecare is partly performance based and partly cost-reimbursement funding; and BEGIN contracts base performance payments on undertaking orientation sessions, client work readiness progress scores, and receipt of basic qualifications, in addition to job placement.

The transition to the prime contractor system in the late 1990s was controversial and, over time, attracted criticism that contractual performance incentives encouraged 'creaming' and that few participants could access skills and education provision (Bryna Sanger, 2003: Youdelman and Getsus, 2005).

The 'Back to Work' programme, implemented in 2006, redesigned earlier incentives partly in response to such criticisms. Revisions were made to the outcome payment system, designed in part to improve access to skills training and place greater emphasis on employment retention and advancement (Egglestone, 2006). The contractor now, for example, must develop a 'Job Retention and Career Plan' for each participant and document their efforts to 'advance' the individual through skill development and financial planning. Contractors receive only a nominal administrative payment for clients who are not placed in jobs, and only partial payment for short term job placements. The contractual incentives continue to be targeted at sustained jobs and career pathways (see Table 1).

Table 1: New York City: 'Back to Work' Performance Milestones and Payments (US\$)

Employment Plans	
■ Pre-employment Plan	190
■ Job Retention and Career Plan	190
Unsubsidised Employment	
■ Job Placement for 30 days (minimum 20 hours a week)	1,139
■ Job Retention for 90 days after initial placement	1,219
■ Job Retention for 180 days	898
Supplements	
■ For case closure (no longer receiving cash assistance)	66
■ For Placement of Sanctioned Clients	351
■ Supplement for 10 per cent wage gain	99
Average rate per client	3,802

Source: Kasdan A. and Youdelman S. (2008) *Missing the Mark: An Examination of NYC's Back to Work Program and Its Effectiveness In Meeting Employment Goals for Welfare Recipients*, Community Voices Heard, New York, Table 4.

Initially, HRA had responsibility for delivering WIA training programmes but it failed to implement them effectively or integrate them with its welfare to work provision. Responsibility then was transferred to the city's Small Business Service, which established a separate network of seven 'Workforce 1 Centers'. These are delivered by contractors who provide employment and training advice with access to training vouchers for eligible participants. The performance incentives for these contractors are aligned with WIA requirements and payments are based on criteria such as job placements as a percentage of target placements, continuing employment after six months, and employer 'fulfilment' (Krauskopf, 2008).

A review of New York's employment placements and skills system highlighted the fragmentation of the system. In total the review found five different city agencies delivering over thirty separate programmes, albeit HRA and Workforce 1 Centers were the largest providers (Thompson, 2008). Whilst there was much innovation in 'advancement', sector based and targeted group training and employment programmes the review commented on the pervasive lack of coordination and collaboration throughout the system. This was exacerbated by federal requirements which meant that even where programmes were delivered by the same contractors they had to operate with different payment milestones and satisfy different requirements to verify performance. The report suggested that New York needed to develop a coherent strategy and pointed to the progress made in other cities and states in coordinating their systems.

Integration of welfare and workforce development systems and common performance measures

Different patterns of coordination and integration have emerged at state and local levels in response to the flexibility given by TANF and the one-stop systems established by WIBs. In contrast to New York City, several states, such as Utah and Texas, merged their welfare and workforce development programmes into a single agency at state level. Other states use a variety of contracts, financial agreements, memoranda of understanding, and other formal agreements to coordinate services and activities between state welfare and workforce development agencies. Such coordination may include co-location of or electronic linkages between welfare and workforce development services in 'one stops' (as in much of Wisconsin); blending of separate funding streams; and the development of more seamless service delivery through common application processes, integrated intake and case management (Ranghelli, *et al*, 2003; Noyes and Corbett, 2005).

The extent of such cooperation varies. Studies report that the logistical and bureaucratic barriers to effective collaboration are challenging. In particular, distinct funding streams and programme goals result in different eligibility requirements, programme definitions, reporting requirements, performance measures, and service priorities that make it difficult to achieve coordination or integration for service users (Ranghelli, *et al*, 2003). One evaluation reported that even though WIA legislation indicated that TANF recipients should have access to training programmes the legislative performance standards and work participation rules acted to restrict such access. Programme implementers suggested that relatively high expectations for post training job placements for WIA participants led to procedures to screen out individuals with low educational attainment and/or low work experience. At the same time TANF work participation rules restricted the extent to which TANF recipients could participate in vocational and other training.⁶ It also appears that work first policies which stressed immediate job placement over longer term training also affected the enrolment of TANF clients (Abt Associates, 2004).

⁶ Federal regulations specify that for all TANF recipients, other than teenagers, job skills training, education directly related to employment, and secondary school or equivalency classes can count towards the work rates only when combined with at least 20 hours per week (30 hours per week for two-parent families) of participation in a 'core' work activity, such as subsidised or unsubsidised employment or community service. Stand-alone 'vocational educational training' may count towards the work rate but is subject to a lifetime limit of twelve months per recipient.

The problem of ‘joining up’ federal employment and skills programmes led to an attempt to reduce administrative barriers and separate reporting requirements. This involved the design of ‘common measures’ of performance. These measures were intended to be applied to 31 employment and training programmes from 2004. There was, however, only limited effort in getting all the relevant federal agencies and state delivery bodies to ‘buy in’ to the new system and by 2009 they had still been implemented only within the Department of Labor (see Appendix B; CLASP, 2009). Nevertheless, the extent to which the design and implementation of such common measures facilitates integrated service delivery may merit further study in the context of proposed reforms to the British system.

Several states have taken their own approach to developing integrated performance standards which may also deserve consideration. These ‘return on investment’ standards seek more accurate measurement of the net costs, impacts and social returns of employment and skills programmes, which may be used to design contracts and steer provider behaviour. The most advanced system has been developed by Washington State which over a long period has required its WIB (and its predecessors) to undertake regular quasi-experimental outcome evaluations and cost benefit analyses of all its workforce programmes. The results have been used to develop a ‘return on investment’ system of performance measurement for all its state and federally funded workforce development programmes (Rubinstein and Mayo, 2007). On the basis of this experience Washington worked with a number of other ‘best practice’ states to propose a ‘next generation’ performance management system for US workforce development programmes (see Appendix C).

Creaming and parking in US workforce development and welfare to work programmes

A number of detailed studies of workforce development and welfare to work programmes have sought to assess the impact of performance incentives and the extent to which such incentives have led to creaming and parking.

Evaluations of the earlier JTPA programmes found that state agencies responded to performance incentives and service delivery was organised to maximise measured performance, with federal incentives strongly reinforced in the performance based contracts given to providers (Heinrich and Marshke, 2008). Detailed econometric findings showed that strong performance incentives encouraged the selection of more job ready applicants and less willingness to use more intensive and expensive training provision. Even when case managers indicated a desire to help the most disadvantaged, analyses of their referrals to services showed that the “probability of meeting the standard was the most statistically significant and numerically influential factor in selecting applicants” (Heckman *et al*, 1997, p. 393).

Other econometric studies suggested that differences in participation reflected differences across groups in programme awareness as much as selection bias. Such differential access to knowledge about programmes had the effect of exacerbating the appearance of ‘cream-skimming’ in recruitment and the perceived influence of selection processes may have been exaggerated (Heckman and Smith, 2005). Another factor limiting creaming and parking was the ability, over time, for policy makers and programme administrators to redefine and improve performance standards. For example, JTPA initially included cost performance measures, based on how much was spent to produce a job placement. These were phased out eight years after their introduction in response to research and experience showing that the cost standards were limiting the provision of longer-term or more intensive programme services. Similarly federal officials changed technical enrolment and participation rules after it became evident that implementing agencies were manipulating start and termination dates to boost employment rates artificially (Grubb, 2006; Heinrich and Marscke, 2008).

A study of outsourced welfare to work provision reported that there was no evidence, at least at the time of the site visits, that creaming or parking were significant problems (McConnell *et al*, 2003, p. 42). Providers pointed out, for example, that it was difficult to favour participants who were more likely to become employed because they could not identify those people easily, and most of their participants faced significant employment barriers. Moreover, by typically including outcome and process measures in the contracts they designed, purchasers mitigated perverse selection incentives. The inclusion of measures related to job retention, wages and benefits, and earnings gains, for example, diminished the incentive to place participants quickly into poor quality jobs. Programme enrolment measures increased the providers’ incentive to engage all service users referred to them. Measures indicating completion of assessments and activities also limited the ability of providers to service participants differently. The challenge was to balance such process measures in ways that kept the provider focused on transitions into employment and allowed them some flexibility for innovation.

US performance standards and longer term outcomes

There is a trade-off between obtaining timely measures of performance and accurate ones. Programme managers and purchasers need shorter measurement periods than in more rigorous net impact evaluations, but the evidence from JTPA evaluations is that “short term measures are especially vulnerable to manipulation” (Courty and Marschke, 2003).

One significant finding from the JTPA evaluations was that the relatively short term employment related performance standards measured were “either uncorrelated with or negatively corroborated with net value added, especially in the long run” (Heckman *et al*, 1997, p. 392). In a review of the JTPA evidence, Barnow and Smith suggest that because performance standards now are negotiated with individual states rather than based on a standard model, with adjustments, as with JTPA, WIA took the delivery system “farther away from the evidence than it was before” (2004, p. 276). There was also evidence that the implementation of these

new standards had generated “inappropriate incentives for program[me] managers to improve measured performance rather than service access or quality” (Heinrich, 2004). Amongst other recommendations Barnow and Smith emphasise the necessity for longer term research to determine “short-term outcome measures that are reliably correlated with long-run programme impacts and cannot be gamed by local program[me]s” (2004, p. 275).

In terms of high quality welfare to work evaluations the evidence on the relationship between performance standards and longer term outcomes is mixed. One review of such evaluations suggested that many performance indicators “appear to work poorly for a wide range of people”. When the results from studies that measured three year effects were disaggregated for the most disadvantaged groups, average earnings levels were deemed “a fairly good, though not perfect, indicator of which programmes were most effective” and that the programmes involved “had among the largest impacts for the most disadvantaged” (Michalopoulos, 2004, p. 29, p. 30). This suggests that performance standards that measure levels of, and changes in earnings as well as employment and skills acquisition should play a role in outcome based commissioning.

3. Markets and outcome based contracting in vocational education and training and employment services in Australia

In Australia the federal government is responsible for the design and delivery of a national social security system, employment services and most employment programmes. Whilst the federal government has oversight of skills policies state and territory governments have constitutional responsibility for the vocational education and training (VET) system. Since the 1990s national policies and frameworks have been set up for the VET system but funding remains largely channelled through the states and territories which have also been responsible for accrediting and contracting with providers. At the front line employment and skills provision is delivered through two parallel systems with limited connections between them.

During the 1990s public sector delivery of employment and skills services in Australia changed in response to the combined impact of competition policy and the various forms of 'New Public Management' which sought to empower managers, improve efficiency and incorporate private agencies into the delivery of public services (Considine, 2001). Through successive reforms the Australian Government tried to create quasi markets in the delivery of VET and employment services. The changes were most extensive in the employment services system where the Commonwealth Employment Service was privatised and replaced by a 'Job Network' comprised of for-profit and non-profit agencies.

Federal responsibility for skills and employment provision and funding has moved between relevant Departments. In 1996 a combined Department for Education, Employment and Training was created, but in 2001 education and employment were separated. They were recombined in 2008 with the creation of the Department for Education, Employment and Workplace Relations (DEEWR). The recent reorganisation has been associated with a renewed Government commitment to reducing skill shortages and social exclusion. This has involved the creation of 'Skills Australia', a high-level independent advisory body with responsibility for providing guidance on the development of the VET system, as well as the imminent creation of a federal national regulatory authority. It has involved also measures to better integrate training provision within the outcome based contracting framework through which employment services are delivered and the targeting of over 300,000 'Productivity Programme'⁷ training places at the unemployed and those seeking to enter the labour market.

⁷ The A\$2 billion 'Productivity Places Programme' is intended to provide federal funding for over 711,000 training places over a five year period. The aim is to provide 392,000 places for workers wanting to improve their skills with a further 319,000 places targeted at the unemployed and those seeking to return to the labour market. The funding initially was channelled through DEEWR but has since been devolved to the states and territories.

Performance management and outcomes in the Australian VET system

In Australia national VET policy is negotiated and agreed by relevant Ministerial Committees operating within the framework of the Council of Australian Governments. Over 80 per cent of VET funding comes from federal and state governments, with the remainder from employer and student fees. Public funding is channelled mainly through state authorities with varying performance and reporting requirements (Knight and Mlotkowski, 2009, p. 31).

The detailed objectives for the Australian VET system have been largely driven through skill forecasts and planning assumptions, rather than being defined as meeting demand (Hoeckel *et al*, 2008). Overarching national strategies have been articulated by ‘peak’ advisory bodies, with the Australian National Training Authority (recently replaced by ‘Skills Australia’) outlining three distinct national strategies during its existence. These were intended to provide direction and a performance monitoring framework for the system.

The ‘key performance measures’ changed over the period but the common aim was that when considered together the results from the indicators would provide a comprehensive picture of the outputs, efficiency and effectiveness of the system. As the performance indicators evolved greater stress was placed on measuring outputs outcomes, with student learning and employment outcomes and employer experience of the VET system assessed through periodic surveys (Knight and Mlotkowski, 2009).

The most recent objectives and key performance measures agreed for the VET system are outlined in the ‘National Agreement for Skills and Workforce Development’ (COAG, 2008). The Agreement brought together, as far as possible, all federal government funding of skills and workforce development as part of a transition to a system where states would be accountable for securing the long term and ‘aspirational’ outcomes identified in the Agreement. The Agreement outlines key objectives and outcomes and identifies a range of outputs, progress measures and targets through which future performance is to be measured (see Appendix D). Karmel (2008) suggests that the approach marks a significant change from earlier strategies with states and territories now held accountable for strategically important outputs and outcomes whilst enjoying greater flexibility in how they secure them.

Skills Australia (2009) has proposed further changes to the ‘governance, architecture and market design’ of the VET system. Amongst other things, it envisages further extension of a ‘managed market’ that allows for ‘consumer led training’ but within constraints which allow VET to be aligned with economic and workforce development needs (2009, p. 15). It also recommends further contestability within the system, subject to appropriate regulatory reform, noting that some states are expanding competitive purchasing with “between 30 to 50 per cent of public VET funds contestable by 2012” (2009, p. 38).

Providers and performance accountability in the Australian VET market

The early market-based reforms of the Australian VET system made some funding contestable, allowing private providers to compete against the previous monopoly of 'Technical and Further Education' (TAFE) institutes. Subsequent reforms of the supply side included the implementation of 'user choice', a quasi-voucher scheme which enables employers and their apprentices and trainees to select a training provider and negotiate aspects of their 'off the job' training, such as its timing, content and delivery.

Public or private providers must be accredited as 'Registered Training Organisations' with relevant state or territory regulatory authorities in order to enter the VET market. This enables the provider to deliver employer recognised 'training packages' that meet standards determined through the 'Australian Quality Training Framework' (AQTF) – the basis for most of the programmes delivered in the VET system. Each provider wishing to gain recognition must comply with 'essential standards', including a requirement for an RTO to gather information on their performance against three quality indicators: 'employer satisfaction, learner engagement and competency completion' (Knight and Mlotkowski, 2009, p. 25).

Each public 'purchaser' sets the price it will pay for the training that it procures, and prices can differ substantially, depending on the specific nature of the training and a range of other factors, including delivery methods and local priorities. There are some differences between the states and territories but generally the basis for setting prices is a nominated dollar amount per hour of training (Ferrier *et al*, 2008, p.12). Each state or territory then manages the flow of contestable funds and desired outcomes in their training markets using a range of policy levers, such as pricing differentials, geographic restrictions, and capping of commencements (Skills Australia, 2009, p.57).

In general VET delivery bids from providers are evaluated by state training authorities on a number of criteria, including price and demonstrated capacity to deliver quality training. One review reports that payments to both public and private providers for contracted or tendered user choice and contestable delivery are progressive and depend upon evidence of performance. These requirements include "submission of training plans, evidence of commencement of training and evidence of completion of competencies or issue of qualifications" (Adams, 2005, p. 23).

A number of states have their own contract monitoring, compliance, expected performance and evidence standards in addition to those required by AQTF accrediting bodies. Skills Australia (2009) acknowledges that this leads to some duplication but stresses that the potential power of contract auditing compared to AQTF quality audit is the linkage of payment to satisfactory delivery of outputs and performance standards.

Following the introduction of contestability and 'user choice' the number of RTOs grew rapidly, increasing from 1,200 in 1994 to 4,500 in 2008 (Ferrier *et al*, 2008, p. 11). Nevertheless, the impact of contestability has been muted, with many RTOs being smaller, specialist providers, and much provision still controlled through large TAFE colleges. In some states the role of TAFE institutes has been redefined and they typically enter into service delivery contracts with their state or territory government where reporting and accountability requirements "provide for full or partial recovery of funding if contractual requirements are not met" (Knight and Mlotkowski, 2009, p. 31). By contrast other states and territories have sought to protect the viability of their TAFE institutes by not fully implementing a purchaser-provider model.

Skills Australia identifies what it considers to be another systemic weakness. Much of the performance and accountability framework for VET has been targeted at the whole system, with much less emphasis on transparency of performance at the provider level and "scant public insights into the outcomes realised by individual private providers" (2009, p. 64). Skills Australia proposed that individual providers should publish data on their outcomes – in terms of student and employer satisfaction, job outcomes, course completion – in "consistent, easily understood and accessible ways" (2009, p. 63). On receiving the report from Skills Australia the Deputy Prime Minister acknowledged that VET sector performance was 'opaque' indicating that later in 2010 the federal Government would be announcing 'steps' that will help "shine a light on the performance and effectiveness of the sector" (Gillard, 2010).

Other commentators conclude that the levers for holding states, territories and providers accountable for their performance and outcomes remain weak, with "little pressure on states and providers receiving public funds to improve their efficiency" (Knight and Mlotkowski, 2009, p. 9). Some analysts suggest that quasi market reform has had mixed impacts on choice, quality and service user responsiveness, and that high transaction costs associated with greater complexity and uncertainty in VET funding, "appear to have discounted or cancelled out any efficiency gains" (Anderson, 2006, p. 27). Another persistent criticism concerns the weak connections between the VET and employment services system – an issue of particular concern given the skill shortages that have characterised sectors of the Australian labour market over the past decade.

The employment services market: from the Job Network to Job Services Australia

In 1998 the Australian Government created a fully privatised employment placement market. Conventional labour market and training programmes for the long term unemployed were replaced by 'employment assistance', where 'black box' contracting gave providers flexibility to decide individual service provision within a system driven by job outcome related payments.

Between 1998 and 2009 the 'Job Network' (JN) moved from 'radical experiment' to established institution through three distinct periods, each marked by different 'Employment Service Contracts'. The design of the system, and the outcome incentives, changed as policy makers adapted the model to secure greater efficiencies, deal with unanticipated effects and, through successive 'welfare reforms', redefine services to 'activate' more working age benefit claimants. In 2009 a fourth contract came into force. The new 'Job Services Australia' model has been designed to provide greater flexibility in the system, to integrate generalist and specialist provision for the unemployed, and to create better linkages with skills provision.

The design of outcome based contracts and the Jobseeker Account

In the first contracting periods, JN employment assistance consisted of basic job placement activities and short 'Job Search Training' courses for people usually unemployed for three or six months. The most expensive provision was 'Intensive Assistance' (IA) targeted at those out of work for over a year or identified as being at risk of long term unemployment (determined through the use of a 'Jobseeker Classification Screening Instrument'). Providers were paid combinations of up-front service fees, job placement fees and outcome payments after 13 weeks (interim) and 26 weeks (final). The amount per participant varied with the payments designed to reflect the intensity of service provided and the risk involved in placing the jobseeker in work.

After the second contract period commenced published evaluations suggested that the purchaser-provider framework was working and that outcome payments and competition had created incentives for improved efficiency (OECD, 2001). Significant problems, however, had emerged. The Departmental evaluation reported that most intensive assistance was given in the first few months of participation, when most job entries were secured. Over time, client contact with providers lessened. The OECD reported that less than half of IA participants "had been sent to a job interview or to speak with an employer about a job"; nearly a quarter of those surveyed had "visited their provider only once or twice"; and "few providers appeared to be offering effective services to address the underlying barriers to employment" of the hardest to place (OECD 2001, p. 193 and p. 59). There was also minimal provider expenditure on employment subsidies or on vocational training.

The independent Productivity Commission reported that only 15 per cent of participants placed into employment by JN resulted in payment of a 13 week outcome payment. Providers were instead deriving 70 per cent of their income from the "high level of commencement fees" and had little incentive "to achieve additional outcomes" (PC, 2002, p. xxxiv). Critics argued that the funding incentives and the lack of regulation encouraged providers to take the up-front fee, work with the most job ready, 'park' the hardest to place, and fail to invest in expensive provision, including vocational skills.

The 2000-03 contracts involved changes designed to regulate the services given, and ensure improved provision for disadvantaged users. More radical change followed in the third contract, which operated between 2003 and 2009. This created an 'Active Participation Model' (APM) to deliver a 'service continuum' that would ensure job seekers were in regular contact with their provider and were actively engaged in job search and other authorised activities. The intention was to increase job search activity amongst the unemployed and to establish more process requirements for providers to meet.

The APM introduced other changes. Commencement fees were replaced by sequential service fees and a 'Job Seeker Account'. The Account comprised a restricted pool of funds earmarked for spending only on employment barrier reduction with the highest amounts allocated to the harder to help jobseekers. The Account was not an individual entitlement and a provider could use the account flexibly across their caseload. Crucially the provider was not allowed to retain any surplus Jobseeker Account funds as profit.

By 2009 the provider payment system comprised service and job placement fees, the Jobseeker Account, and outcome payments for 13 and 26 week job placements weighted towards difficult-to-place job seekers. The redesigned incentive system was intended to ensure that providers would put greater emphasis on income earned from outcomes rather than service fees. At the same time a more prescriptive delivery model combined with the Jobseeker Account sought to prevent 'parking', ensuring that all participants were more likely to receive services.

Star ratings and changes to the provider network

The JN was designed to promote competition for market share, through the tender process, and intra-market competition, by allowing unemployed people and employers to choose their preferred provider. The federal Department ensured that, in most areas, there was a choice of providers available and, when sufficient reliable job outcome performance data was available, it started to publish comparative star ratings to enable service users to make an informed choice between them (PC, 2002; ANAO, 2005).

The comparative rating formula gives most value to full time employment outcomes sustained for 13 weeks or more, secured as soon as possible after service users access assistance. The methodology includes regression adjustments for labour market conditions and participant characteristics. A speed of placement weighting was introduced in 2006 to serve as a counterweight to a fees system that gave relatively little incentive to providers to place people until they had actually become long term unemployed when they would attract higher job outcome payments. The Department estimated that within two years of introducing fully comparable star ratings 13 week job outcomes increased from 15 per cent to 35 per cent. In this context, star rating performance was used by the Department to further steer provider behaviour in that high performance could increase the amount of business a provider was allocated and enable them to secure future contracts. By contrast under-performance would result in loss of business and possible non-renewal of a contract.

Another factor that characterised the evolution of the JN was a reduction in the number of providers delivering services and seeking to enter the market. In 1997 over 1,000 organisations submitted tenders from which 306 core JN providers were selected. By 2008 the number of core providers had fallen to 99 with about 60 per cent of market share controlled by 13 larger generalist providers, five of whom held nearly 40 per cent of delivery. The market was shared almost equally between for-profit and non-profit agencies.

The performance of the Job Network

The Australian Government maintained that, from its inception the JN was much cheaper and consistently outperformed the former public sector delivery system (Thomas, 2007). There have been a number of official evaluations of outcomes from the system. The most recent reported that the net impact of intensive assistance targeted at the long term unemployed and most disadvantaged had increased from 0.6 per cent in 2001, to 6.2 per cent in 2002, to 10.1 per cent in 2005 (DEWR, 2006, p. 4). Another study, based on longitudinal survey data, found that job outcomes for intensive assistance improved ‘substantially’ between 3 and 18 months after leaving with respondents also reporting a movement from casual to permanent employment (DEEWR, 2008).

Departmental assessments attributed this success to the pressure generated by star ratings and the reinforcement of the pay-for-performance contracting regime following the reduction in commencement fee income. By 2005 services were being provided by a much reduced number of better managed agencies delivering service strategies that had been progressively refined on the basis of operational experience (Grubb, 2006). Other external factors also were significant, notably that in many areas JN providers now operated in conditions of near full employment.

The other much publicised success of the JN was to drive down costs. Officials frequently emphasised raw data on costs to indicate that between 1991 and 1994 the cost per employment outcome was around A\$8,000, rising to just under A\$16,000 in 1995-96. These costs fell to A\$6,500 in the first phase of the JN, and then to A\$3,500 by 2005, reflecting in part the falling real values of fees and outcome payments after 2003. One significant question was the extent to which JN cost efficiencies were, as many critics and JN providers suggested, secured at the price of weakened service quality (Finn, 2008).

Whilst the introduction of the APM had been designed to ensure more regular contact between providers and their participants the other performance incentives, especially star ratings, continued to shape provider behaviour in ways that disadvantaged the hardest to help and the providers who worked with them (Murray, 2006). Commentators were critical also of service quality, pointing out that low cost job search assistance and motivational strategies were unlikely to reduce the employment barriers of the hardest to help and that JN providers rarely used more costly employment subsidies or skills provision which could improve the employability and earnings potential of the longer term unemployed (ACOSS, 2008).

Other criticisms concerned the increasingly onerous compliance and contract management system to which the providers were subject. Some of these processes were designed to eradicate ‘imaginative practices’ where some providers had been able to secure outcome payments without placing participants in real employment. Others reflected new policy objectives where the Department sought to more directly ‘steer’ the actions of providers and enforce the job search activities of participants. This reduced the flexibility of the system with providers arguing that partnership based on collaborative relationships had been replaced by “command and control” which “shut down the innovation and flexibility that was sought from a new employment services system” (NESA, 2008, p. 13).

Job Services Australia and integrating skills provision within outcome based contracts

In November 2007 a new Commonwealth Government was elected with a commitment to both review the JN and to expand training opportunities. After a consultation period the new Job Services Australia (JSA) system was introduced, commencing in July 2009. The new model integrated JN provision with six smaller employment programmes with the aim of creating a single delivery system. It is budgeted to cost A\$4.9 billion over three years.

In the new system job seekers are categorised into one of four ‘streams’, with the most job ready referred to stream 1 and those with ‘severe barriers’ referred to stream 4. A provider must develop an individually tailored ‘Employment Pathway Plan’ which maps out any training, work experience or additional assistance the service user might need to find sustainable employment. On completion of a stream, usually after twelve months, the user may be reassessed and moved to another stream, or be required to participate in work experience activity. Jobseekers and employers are able to exercise a degree of choice over which provider they use.

The principles of the JSA market and outcome based funding system are similar to those which characterised the JN. Providers had to compete for fixed price tenders to deliver JSA, and were selected on the basis of several criteria, including their past performance and perceived capacity to deliver the revised employment assistance system.

The payment system comprises service fees paid during participation, access to an ‘Employment Pathway Fund’ (which replaced the Jobseeker Account), and job placement and outcome payments paid after evidence of 13 weeks or 26 weeks employment retention. The level of resource per participant, and outcome incentive for the provider, increases in relation to duration of unemployment and the severity of the barriers faced, as indicated by the service stream to which the participant is referred (see Table 2). Other refinements included financial recognition for securing limited ‘social’ outcomes for highly disadvantaged stream 4 job seekers and enhanced outcome payments for sustained jobs that JSA providers ‘broker’ with employers or which are preceded by participation in a ‘qualifying training course’.

Table 2: Job Services Australia: 2009-2012*

Work Ready		Disadvantaged Jobseekers	
Stream 1	Stream 2	Stream 3	Stream 4
53% of new job seekers	22% of new job seekers	10% of new job seekers	15% of new job seekers
* A\$11 in Employment Pathway Fund	* A\$550 in Employment Pathway Fund	* A\$1100 in Employment Pathway Fund	* A\$1650 in Employment Pathway Fund
* £385-A\$440 in Job Placement fees	* £385-A\$2800 in Outcome and Job Placement fees	* £385-A\$6600 in Outcome and Job Placement fees	* £385-A\$6600 in Outcome and Job Placement fees
* Up to A\$781 in service fees	* Up to A\$885 in service fees	* Up to A\$1120 in service fees	* Up to A\$2736 in service fees
Skills assessed after three months			
WORK EXPERIENCE			
* A\$330 work experience service fee			
* A\$500 in the Employment Pathway Fund			
* Up to A\$392 in service fees per year			

* Please note that some of these stream allocations and related fee payments have since been adjusted. Source: The Future of Employment Services in Australia: A Discussion Paper, (2008) Department of Education, Employment and Workplace Relations, Canberra, p. 3.

Although the previous JN was poorly integrated with the VET system there were a number of ways in which providers could facilitate access to training and be rewarded for doing so. A provider, for example, could use the Jobseeker Account to fund training. About a quarter of those in intensive support accessed such support but it mainly comprised low cost job search and motivation courses with participation typically lasting about three days and costing just A\$287 on average (Murray, 2006, p. 34). Providers also could refer participants to state financed VET programmes although participants had to remain actively seeking work and such participation might have impacted on the providers' performance in speed of placement (a key factor in the star ratings and business allocations). Finally JN providers were eligible for outcome payments, albeit paid at a lower rate, if they managed to place participants in full time education and training for at least one semester of a two semester course.⁸

⁸ This rule was supplemented by benefit rules for the means-tested common 'Youth Allowance' which is paid both to young unemployed people and those studying or training full time aged 16 to 20. The Youth Allowance, which pays the same as out-of-work benefit, is also available to 16 to 24 years old studying or undertaking a full time 'Australian Apprenticeship'.

These earlier rules have been retained and enhanced in the JSA service delivery model, creating stronger incentives for providers to both place people into designated skills courses, especially apprenticeships, and to place such participants in employment where they make use of any skills acquired. JSA providers are paid enhanced outcome payments for placing eligible participants into an apprenticeship in a 'skill in demand' or where the job is preceded by a 'qualifying training course', including those made available through the 'Productivity Places Programme'. During the time a participant is undertaking such approved training the individual may receive a financial incentive, of A\$46.60 per fortnight for up to six months, in addition to their benefit payment. For the provider the 'clock stops' in terms of their assessed 'speed to placement', designed to stop them 'parking' participants, and when assessing providers contract managers are now expected to assess how well they perform in connecting participants to appropriate skill opportunities. Finally, participants who enter stream 1 now are expected to undertake a skills assessment, and state and territory based language and basic skills provision which can be accessed by jobseekers has been allocated additional resources (Dacey, 2009).

A DEEWR Minister reported that by December 2009 the number of people receiving unemployment related benefits who reported they were participating in training programmes had doubled to over 13 per cent (Arbib, 2010). It is too early, however, to assess the extent to which the changes have facilitated a more integrated employment and skills offer to service users or improved outcomes.⁹ Anecdotal evidence from JSA providers suggests that there continue to be problems both with the timing, location and level of much VET provision, with few training providers offering the more basic or pre-entry provision needed by their service users. There is frustration too that delivery of the Productivity Places Programme has been devolved to states and territories, with the result that priorities and eligibility now vary, and JSA providers and their clients have to negotiate different delivery arrangements in each jurisdiction. Finally, there is some concern about the potential to 'game' the system whilst reduced outcome payments are paid for someone who enrolls on a full time education or training course rather than for their success in attaining a relevant qualification.¹⁰

⁹ Early data on the Productivity Places Programme found that between April 2008 and mid 2009 almost 90,000 people had commenced in 'job seeker' training places, with over 42,000 having been referred by JSA providers (Dacey, 2009). More than 6,000 of these JSA referrals, who completed, had achieved employment outcomes. Earlier destination evidence found that for 2008 PPP graduates only 19.7 per cent were employed in the same occupation group as their training course, with the match being highest, at 44.7 per cent, for those training as personal carers and assistants (NCVER, 2009).

¹⁰ Observations from interviews undertaken with JSA providers in Australia in November 2009 and March 2010.

4. Conclusion: policy implications

This review has considered the role of outcome measures, performance standards and related contracts in the management and delivery of the US and Australian skills and employment systems. The findings reveal that in each country respective federal Governments increasingly have set explicit performance and outcome targets within wider reform strategies designed to increase employment rates, reduce welfare dependency and increase skills attainment and utilisation. Performance management systems have been redesigned with public sector employment and skills delivery agencies subject to greater scrutiny and accountability and, where service delivery has been made contestable, challenged by the entry of other providers, including those from the private sector.

Public purchasers have made use of performance and outcome based contracting where skills and employment services have been contracted out. The terms of such contracts differ widely, with varying amounts of provider income dependent on securing agreed outcomes or performance standards. Only in some welfare to work and employment programmes is a major part of provider income dependent on securing sustained job outcomes. The contracts are not exclusively outcome based but have other performance and process requirements embedded within them.

Views on the success of such contracting systems are mixed and, even where the results may appear impressive, it is difficult to disaggregate the impact of the outcome based contracting system from that of other policy changes. Moreover, whilst the cost and efficiency gains claimed for US and Australian models appear significant, relatively little is known about how far these gains have been offset by high transaction costs or reduced service quality, especially for the most disadvantaged. Some of the cost reductions attributed to the Australian model, for example, stemmed from the withdrawal of more costly employment subsidies and training programmes that critics suggest were needed to tackle the employment barriers of the long term unemployed and enable participants to access better paid and more reliable jobs.

There is evidence that minimising cream-skimming, creaming and parking are significant challenges in both public and private sector incentive and target driven delivery systems. Such risks may be reduced through contract design and oversight with evidence that scope for 'gaming' outcome based systems diminishes as policy makers and contract managers develop expertise. The inclusion of measures related to job retention, wages and benefits, and earnings gains, for example, all help diminish any incentive to place participants into poor quality jobs. Measures indicating completion of assessments and activities and regular surveys of participant and employer experience all help limit the ability of providers to service clients differently. The challenge is to design such process and outcome measures in ways that allow providers flexibility in how they secure outcomes and do not create unnecessary administrative burdens.

The findings from the studies reviewed reveal that the implementation of performance and outcome based commissioning and contracting has been dynamic and that government agencies and 'purchasers' frequently have had to revise performance standards and contractual terms as problems have arisen and conditions have altered. In both countries there has been much 'learning by doing' and constant adaptation as officials have sought to establish performance management and payment structures that now aim to increase the duration of job outcomes, reduce creaming, integrate skills provision, improve service quality, and control any potential for perverse incentives or 'gaming' of systems.

In this process much knowledge has been gained about different contracting models, the relationships between service delivery and performance incentives, and how to define relevant outcomes (see, for example, Smith and Grinker, 2004; OFM, 2005; Karmel, 2008; Ingeus, 2008; Heinrich and Marschke 2008). This knowledge, and that developed within the UK, must inform policy makers' efforts as they seek to operationalise employment and skills outcomes, such as those proposed by UKCES, into more effective performance management and contracting systems.

The review findings show that in both the USA and Australia there remain legitimate differences in the outcomes sought from 'work first' employment and welfare to work programmes and those sought from vocational education and training systems. Efforts to improve the connections and coordination between these 'work first' and skills development programmes are hampered by these differences and by the distinct funding streams and bureaucratic mechanisms through which such outcomes are sought. The result is fragmented eligibility requirements, different programme definitions, reporting requirements, performance measures, and service priorities, compounded also by variations in the precise definition of outcomes and their measurement and in how they are rewarded.

Such problems are common to the UK employment and skills system where variation in Government targets and incentives makes coordination and integration of services more difficult. This is particularly evident in the contrasts between the sustained job outcomes that DWP requires contracted employment providers to secure against the short term employment entries that enable Jobcentre Plus to meet its employment targets. It is also clear in the primacy given to qualification attainments in the skills system with less regard given to subsequent employment or whether the skills acquired are actually valued and utilised in the workplace.

In addition to more general findings from this study there are three particular proposals that, when tested, might augment current efforts to better coordinate and integrate employment and skills provision in the UK.

The first proposal concerns how to better integrate skills provision within DWP employment programmes for the unemployed. It concerns adapting the redesign of job focused outcome payments within the Job Services Australia payment system for use with FND and other contracted out DWP programmes. It would involve giving incentives to providers to broker training places and rewarding them when participants they have trained are placed in jobs that make use of the skills developed. Such differential payments could be adapted quickly rather than await the longer term DWP ambition that may eventually see job outcome payments paid over a much longer time frame.

The second proposal concerns enhancements in the assessment of employment outcomes from skills programmes and of the qualifications gained. This should involve the use of enrolment and destinations data, collected administratively or through leavers' surveys, to establish the employment and wage rates of participants. Such data could be used to establish whether individuals improved their employment position as a result of their participation and the extent to which they utilise any skills gained in their current employment. Such data could be combined into a measure of workforce quality, as suggested by Tom Karmel (2008) from the Australian National Centre for Vocational Education Research.

Finally there would be value in swiftly reviewing the many contrasting outcome requirements that exist within the British employment and skills system, and in how they are measured, with a view to developing 'common performance' or 'return on investment' measures, similar to those being developed in the USA. Such agreed common measures would help minimise different performance, outcome and reporting requirements and facilitate co-commissioning and the alignment of skills and employment funding. They also would help facilitate greater coherence in the performance and outcome standards that providers have to meet. At the same time such a review could critically audit the varying contracting and financial practices of the different public agencies involved in procuring skills and employment provision. The aim should be how to simplify such requirements and, if budgets cannot be integrated, to consider the extent to which 'master contracts' might reduce complexity in the system¹¹ and assess whether employment and skills purchasing might be better managed by a single professional procurement agency, as proposed by the Association of Learning Providers (2009).

¹¹ These are an administrative mechanism which involves a comprehensive agreement between a funding agency with responsibility for several categorical programmes, potentially a sub-regional partnership or an Employment and Skills Board, and a service delivery provider to deliver a more comprehensive, responsive, and coordinated set of services. The 'master contract' is designed to allow commissioner and provider to align their funding and service delivery goals by combining multiple, uncoordinated contracts into a single agreement (see, for example, Lepler *et al*, 2006).

Appendices

Appendix A: Training and Enterprise Councils, Local Enterprise Companies and Output Related Funding

Training and Enterprise Councils (England and Wales) and Local Enterprise Companies (Scotland) were introduced in the UK in 1987. These independent, employer-led companies were funded increasingly on the basis of achieved training or employment outcomes, in a system referred to as 'Output Related Funding' (ORF). The then Employment Service continued to separately purchase job search assistance programmes but it too placed greater emphasis on competitive bidding and rewarding providers for securing job outcomes.

TECs had considerable flexibility over their budgets including the capacity to generate surpluses, although these had to be spent in meeting wider TEC objectives. The TEC network delivered a wide range of training and enterprise programmes but most of the budget received was for the delivery of Youth Training (YT) and Training for Work (TfW). The Department for Education and Employment negotiated annual contracts with each TEC which agreed a contract price with targets for completed training weeks, volumes of participants and outputs. Young people were steered towards obtaining Level 2 National Vocational Qualifications (NVQs). In the case of unemployed adult trainees there was greater emphasis on job outcomes, measured 13 weeks after a person completed training. Individual TECs had annual budgets of between £15 and £50 million (Bennett *et al*, 1994).

There was no variation in training week payments but ORF was introduced in 1990/91 when it comprised 10 per cent of TEC budgets. It was assessed in relation to a point score weighted to reflect the policy value placed on qualification levels and job outcomes. The proportion of ORF funding increased to between 25 per cent and 40 per cent in 1993/94. At this point seven TECS moved to a 25 per cent/75 per cent 'starts and outcomes' model for their TfW provision that was subsequently extended. By 1997 output payments accounted for between 25 per cent and 35 per cent of the YT budget and 75 per cent of the TfW budget. ORF funding was introduced to Scottish LECs from 1992/93.

There are mixed reviews of the performance of TECs and the impact of their programmes (for example see: HoC EC SC, 1996). There was controversy about the impact of ORF and additional incentives in the TEC funding system for 'special needs' trainees were weak compared with the greater outcome and funding pressures on mainstream budgets that were transmitted to providers through contracts. Over time the funding system shifted the focus of YT and TfW activity towards lower cost provision that marginalised provision for higher cost trainees in general and special needs groups in particular (Meager, 1995).

Other problems emerged about TEC-related payment systems with critical National Audit Office and Parliamentary reports (NAO, 1995, 1996). These highlighted poor audit practices and ‘gaming’ in the system with duplicated and incorrect payments, inadequate supporting evidence for claims from some providers, and high level TEC reserves (Bennett *et al*, 1994). There were high profile cases of providers registering and claiming NVQs for non-existent trainees and placing trainees in temporary employment for a short time to trigger job outcome payments (Jones, 1999). There were also criticisms of the governance of particular TECs and in 1999 a White Paper criticised the complex funding, administration and contracting system for TECs and their providers which at its worst “absorb[s] resources which would otherwise benefit the trainee” (DfEE, 1999, p. 19). The White Paper led to creation of the Learning and Skills Council and the decision to end TEC operating licences in April 2001.

Appendix B: Workforce Investment Act Common Measures of Performance

Adult Program

1. Entry into unsubsidized employment;
2. Retention in unsubsidized employment six months after entry into the employment;
3. Earnings received in unsubsidized employment six months after entry into the employment; and
4. Attainment of a recognized credential relating to achievement of educational skills, which may include attainment of a secondary school diploma or its recognized equivalent, or occupational skills, by participants who enter unsubsidized employment.

Dislocated (Redundant) Worker Program

5. Entry into unsubsidized employment;
6. Retention in unsubsidized employment six months after entry into the employment;
7. Earnings received in unsubsidized employment six months after entry into the employment relative to earnings of job of dislocation; and
8. Attainment of a recognized credential relating to achievement of educational skills, which may include attainment of a secondary school diploma or its recognized equivalent, or occupational skills, by participants who enter unsubsidized employment.

Youth Program

Older Youth (aged 19-21)

9. Entry into unsubsidized employment;
10. Retention in unsubsidized employment six months after entry into the employment;
11. Earnings received in unsubsidized employment six months after entry into the employment; and
12. Attainment of a recognized credential relating to achievement of educational skills, which may include attainment of a secondary school diploma or its recognized equivalent, or occupational skills, by participants who enter unsubsidized employment or who enter postsecondary education, advanced training or unsubsidized employment.

Younger Youth (aged 14-18)

- 13.** Attainment of basic skills and, as appropriate, work readiness or occupational skills;
- 14.** Attainment of secondary school diplomas and their recognized equivalents; and
- 15.** Placement and retention in postsecondary education, advanced training, military service, employment, or qualified apprenticeships.

Across Funding Streams

- 16.** Customer satisfaction for participants; and
- 17.** Customer satisfaction for employers.

Source: <http://www.doleta.gov/Performance/quickview/WIAPMeasures.cfm>

Created: March 27, 2004; Updated: December 17, 2009

Appendix C: Integrated Performance Information for Workforce Development

Labor Market Results for Participants:

- Short-term Employment Rate: The percentage of participants who are employed during second quarter after exit. (For youth, enrolment in education counts as well as employment.)
- Long-term Employment Rate: The percentage of participants who are employed during the fourth quarter after exit. (For youth, enrolment in education counts as well as employment.)
- Earnings Level: Median earnings during the 2nd quarter after exit among all exiters with earnings
- Skill Gains: The percentage of exiters who have completed a certificate, degree, diploma, licensure, or industry-recognized credential during participation or within one year of exit.

Results for Employers and the Economy:

The percentage of employers who are served who return to the same program for service within one year; and employer market penetration.

Return on Investment:

Taxpayer Return on Investment: The net impact on tax revenue and social welfare payments compared to the cost of the services.

Participant Return on Investment: The net impact on participant earnings and employer-provided benefits compared to the cost of the services.

Source: WSWTECB (2005) *Integrated Performance Information for Workforce Development: A Blueprint for the States, Washington State*, pp. iii-iv

Appendix D: VET Objectives and Outcomes National Agreement for Skills and Workforce Development: Council of Australian Governments

Objectives

- All working aged Australians have the opportunity to develop the skills and qualifications needed, including through a responsive training system, to enable them to be effective participants in and contributors to the modern labour market.
- Individuals are assisted to overcome barriers to education, training and employment, and are motivated to acquire and utilise new skills.
- Australian industry and businesses develop, harness and utilise the skills and abilities of the workforce.

Outcomes

- The working age population has gaps in foundation skills levels reduced to enable effective educational, labour market and social participation.
- The working age population has the depth and breadth of skills and capabilities required for the 21st century labour market.
- The supply of skills provided by the national training system responds to meet changing labour market demand.
- Skills are used effectively to increase labour market efficiency, productivity, innovation, and ensure increased utilisation of human capital.

Outputs

The following outputs will act as a proxy to measure progress towards the above outcomes.

- (a) Number of enrolments in vocational education and training.
- (b) Number of course completions in vocational education and training.
- (c) Number of unit/module completions in vocational education and training.
- (d) Number of course completions by Indigenous Australians in vocational education and training.
- (e) Number of enrolments by Indigenous Australians in higher level vocational education and training qualifications.

Progress measures

- (a) Proportion of the working age population at literacy level 1, 2 and 3.
- (b) Proportion of 20-64 year olds who do not have qualifications at or above a Certificate III.
- (c) Proportion of graduates employed after completing training, by previous employment status.
- (d) The percentage of graduates with improved employment status after training.
- (e) The number of hard to fill vacancies.
- (f) Proportion of people employed at or above the level of their qualification, by field of study

Targets

- (a) Halve the proportion of Australians ages 20-64 without qualifications at Certificate III level and above between 2009 and 2020.
- (b) Double the number of higher qualification completions (diploma and advanced diploma) between 2009 and 2020.

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