

# Paper P2

## Performance Management

If, as the UK government intends, not-for-profit bodies are to play a bigger role in providing public services, many of them will need to improve both their efficiency and their effectiveness

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A flagship policy of the UK's coalition government is known as the Big Society. The idea behind it is to "take power away from politicians and give it to people" by promoting the development of social enterprise and local community groups to take on tasks formerly performed by central government. This implies a rearrangement and reinforcement of the not-for-profit sector.

The sector incorporates a wide range of not-for-profit operations (NFPs), including executive agencies, local authorities, charitable trusts and community-interest companies. The obvious central feature of such operations is that they are not primarily motivated by making a profit, whereas the ultimate goal of a commercial enterprise is to generate a profit for its owners. A business may take a short- or long-term view of how it wishes to achieve this, but it has a clear primary objective from which subsidiary objectives may be derived.

NFPs' objectives may be partly legislated for, partly constitutional and partly political. For example, the Driver and Vehicle Licensing Agency is legally required to keep vehicle registration records and to issue drivers with licences and road tax discs. Mencap, a leading UK charity, has the obligation to aid mentally disabled people written into its constitution. The education department of Sunderland City Council has a duty to run schools in the city, but has a wide measure of discretion over how it does this. It can spend money on salaries for teachers or it can switch some of that cash into acquiring IT systems and making greater use of computer-aided learning.

**'There is generally no market mechanism by which the users of an NFP's services can take their business elsewhere if they are dissatisfied'**

There is generally no market mechanism by which the users of an NFP's services can take their business elsewhere if they are dissatisfied with the quality or cost-effectiveness of what's provided. In an article in October 2010's *Harvard Business Review* ([www.snipurl.com/27ogwb](http://www.snipurl.com/27ogwb)) professors Robert Kaplan and Allen Grossman contend that the management of many NFPs involves a "black hole". The organisations operate without any clear measurement of how they are faring. Resources are tipped into this hole with little idea of what they might achieve, according to the authors, who argue that an NFP's financial report will reveal "virtually nothing about its effectiveness or efficiency in creating social value". They go on to advocate the use of a balanced scorecard approach for measuring performance and the introduction of a market mechanism to the funding system for NFPs.

Illustration: Denis Carrier/Dutch Uncle



Practical problems with resource management in the NFP sector include the following:

- Objectives may be unclear. For example, is the goal of a police service to provide foot patrols or is it to contain crime? The two are not the same.
- Objectives may change over time. For example, some NFPs involved in promoting the welfare of disabled children have recently switched their emphasis from providing segregated education facilities for their clients to aiding their integration into mainstream education.
- Different methods may be available to achieve a given objective. For example, a charity seeking to relieve starvation in a less-developed country may provide food to contain famine or it may promote economic development to make that country more resilient to the causes of famine.

A further consideration is that the relationship between objectives and means is often poorly

**'Experience suggests that the private finance initiative system has generally improved efficiency'**

understood. For example, one objective of policing would be "to contain street crime within limits considered to be acceptable". One means of doing that is to use traditional foot patrols. In fact, these are a relatively poor method of containing many forms of street crime; the use of patrol cars has proved far more cost-effective. Having said that, seeing police on the beat may make the public feel safer. But many local politicians advocate having more foot patrols in their manifestos, which reflects some lack of clarity: is the objective to contain crime or to make the public feel safer? Are foot patrols a means to an objective or are they an objective in themselves?

### Black holes and potholes

In recent years much of the debate on management in the NFP sector has concerned the twin concepts of efficiency and effectiveness. Efficiency concerns making the maximum possible use of resources. It involves a straight comparison of input and output – eg, the total cost per mile of road resurfaced. Many local authorities in the seventies were judged to be making inefficient use of resources. They performed most of their activities, such as road repairs, by using large numbers of directly employed staff. It was often found that this cost far more than comparable private-sector operations to achieve given outputs.

Financial management initiatives in the eighties required local authorities to put many of their works programmes out to tender, allowing businesses to bid for contracts. The current private finance initiative system involves continuing private-sector participation in the running of facilities such as schools and prisons. For example, in the past a contractor would probably have built a school and simply handed it over to the council. In a public-private partnership the contractor might build the school and then lease it to the council. The contractor therefore remains responsible for aspects of the school's management after its construction. It has an incentive to consider the trade-off between construction costs and operating costs: possible economies in the construction phase may lead to higher operating costs – and the contractor has an interest in both. Experience over the past 20 years suggests that this system has generally improved efficiency and value for money, although the concept does have its critics. ▶

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The concept of effectiveness is a little harder to handle than efficiency. It concerns finding the cheapest combination of methods of achieving an objective. NFPs will normally have a number of objectives. For example, a public authority may have “containing youth crime within acceptable levels” as one of its objectives. It has several means of achieving this, including:

- Providing school attendance officers to ensure that children are not regularly absent from school (education department)
- Providing leisure facilities – eg, sports grounds and youth clubs (recreation department)
- Providing help for disadvantaged or problem families (social services department)
- Providing police patrols to tackle young criminals (police department)
- Providing young offenders’ institutions at which criminals can be detained (prisons department).

All these departmental activities play a part in achieving the objective. The problem is to find the optimum combination of spending for all of them together. Practical solutions to this problem are the core of planning techniques such as zero-based budgeting systems.

A policy of detaining young felons may achieve the objective, but at a high cost. Imprisonment is an expensive last resort and it may turn a marginal criminal into a habitual one. Experience suggests that much crime can be prevented by using less extreme methods. A high proportion of crime is committed by males aged 13 to 18. Ensuring that all children attend school regularly and that adequate recreational facilities are available to them may tackle the causes. An insensitive cutback in one area – eg, making an attendance officer redundant – can have a high cost impact in other areas when truant schoolchildren commit petty crimes. The key to effectiveness is to find an optimum pattern of spending to achieve the objective. Finding that pattern will usually involve determining a programme of activities that cuts across traditional departmental boundaries.

The emphasis in modern public-sector planning tends to be on outputs rather than inputs. A council’s departments may be efficient, but the organisation as a whole may be ineffective if the overall pattern of departmental activity has not been

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planned carefully. Conversely, an organisation may have detailed inefficiencies in its operations, yet still be effective.

The charity Oxfam operates in crisis relief, development and advocacy in the developing world. In a December 2010 interview on the BBC World Service’s *Global Business* programme, Oxfam’s chief executive, Barbara Stocking, stated that the effectiveness of its development projects could be measured using seven metrics including: the rise in household incomes in affected areas; the perception of increased “resilience” among people in affected areas; and the improvement in Oxfam’s perceived standing among its local partners.

### Market mechanisms for the NFP sector

A conceptual underpinning of the Big Society is the introduction of an element of competition among NFPs in order to promote efficiency and effectiveness. One feature is the proposed Big Society Bank, from which NFPs will be invited to bid for funding. This corresponds to the US Social Innovation Fund (established in 2009), which allocated \$50m to 11 NFPs in July 2010 alone.

Let’s imagine that a local community decides to act in order to improve the prospects of young people in a deprived area. Various means are available for achieving this objective, including devoting resources to housing, childcare, recreation, education and training. Rival NFPs might be invited to submit competing proposals for funding. Their alternative programmes may offer widely differing spending patterns and they will be required to submit performance metrics relating to their past operations. The funding authority will then be able to choose a proposal based on which seems to offer the best value for money in terms of both efficiency and effectiveness.

As Kaplan and Grossman state in *Harvard Business Review*: “The ultimate prize is a social capital market that delivers real impact for the dollars donors contribute. The discipline of such a marketplace would motivate non-profit leaders to: adopt clear models for creating social impact, provide a solid framework for measuring and reporting performance, and help non-profits to develop the leadership and management capabilities they need to achieve their missions.”