

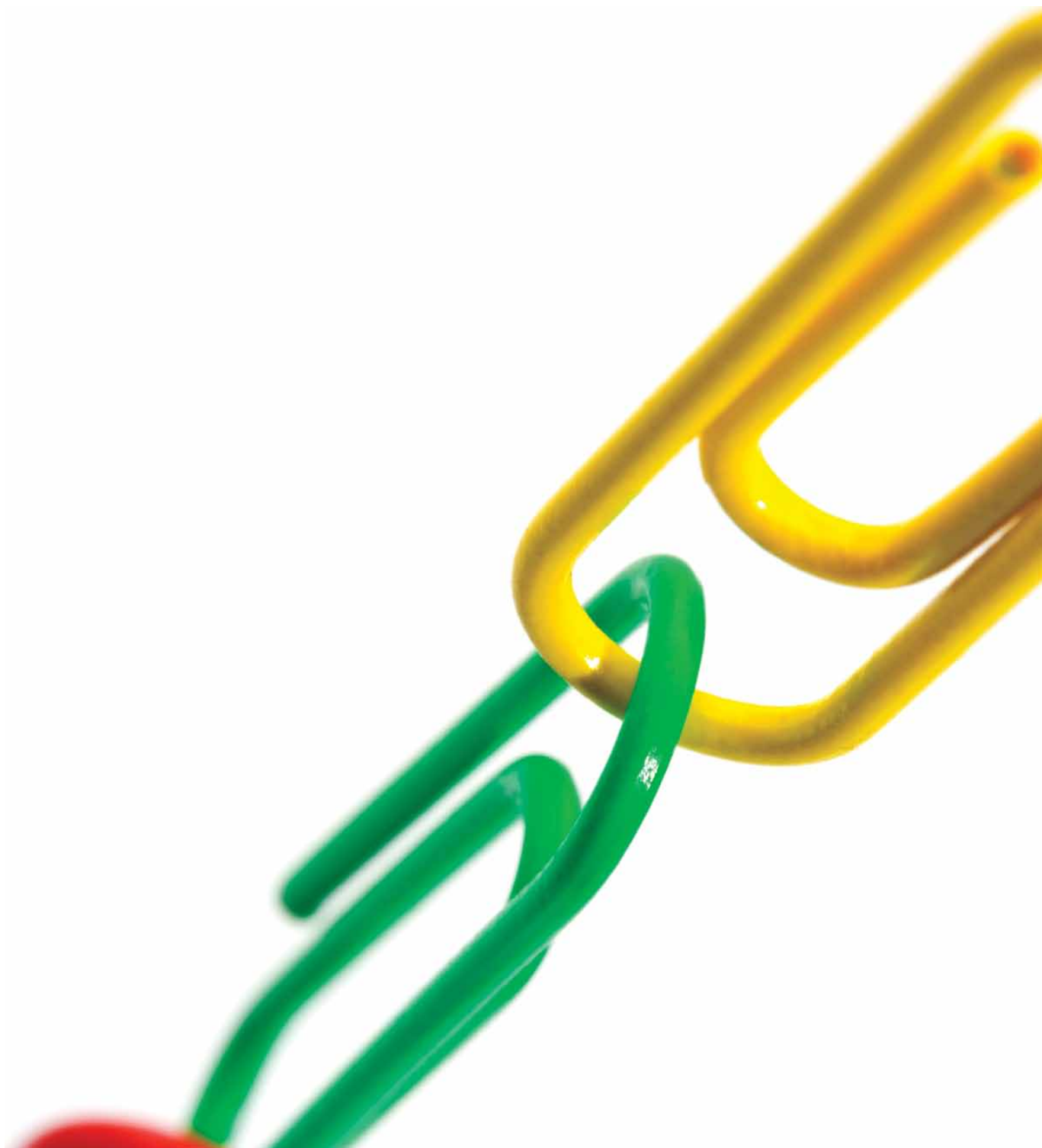
# Social Enterprise Schools



A potential profit-sharing model for  
the state-funded school system

Andrew Laird and Justin Wilson

Edited by James Groves



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# Executive Summary

## The challenge

- More good school places are needed to meet rising demographic demand.
- The shortage of good school places is particularly acute in areas such as London where the number of primary age pupils is rising fast.
- While there are surplus places overall in the system at present, half are in the worst-performing quarter of schools. Last year in England 17% of pupils did not get into their first preference school and 3.5% did not get any of their preferred schools. In London 34% did not get their first preference and 6% got no offer from any preferred school.
- The record deficit will constrain government spending for the foreseeable future.

## Why might allowing private provision help?

- The capacity of the voluntary sector is finite. Allowing for-profit provision would add additional capacity to create good new school places. The private sector could provide both additional capital and expertise.
- Successful private sector providers may have greater incentives to grow and replicate their models than voluntary providers.
- While on paper Academies and Free Schools have freedoms to vary from national pay and staffing policies, their ability to fully use these freedoms in practice may be limited until they reach critical mass. Union opposition to variation from national pay bargaining is entrenched, and there may be ‘safety in numbers’. The expansion of independently-run schools might be quicker if private sector involvement was allowed.

## ‘In-principle’ opposition to private provision ignores the fact that there is already substantial private provision within the state education system – the full extent of which is poorly understood

- Freedom of Information requests made to local authorities (LAs) during the course of research for this report revealed the extent to which private companies are already being paid to deliver state funded education.
- Ironically, despite opposition to for profit providers being allowed to run mainstream schools for 4–16 year olds, private companies already provide education to many of the most vulnerable children. There is profit making provision in nursery education, for children with special needs, and pupils in alternative provision and Pupil Referral Units.
- National data on such private provision is non-existent, and even local data is limited. But this report reveals for the first time the extent of for-profit provision in some of these fields. For example:

- Nationally, around 92% of three year olds receive some free nursery education, more than half of which is delivered by the private and voluntary sectors. Looking at local areas, 87% of Middlesbrough's 2010–11 spending on nursery education found its way into the hands of for-profit providers in that specific sector.
- Brent and Medway's LAs both spent 31% of their special educational needs 2010–11 budget on services provide by private companies
- 50% of Northumberland's alternative provision 2010–11 budget, including Pupil Referral Units, was spent on private for-profit providers. For-profit providers delivered 74% of North Lincolnshire's alternative provision during the same period.
- Furthermore, local authorities and state schools have been able to outsource school improvement programmes to private companies for a number of years. Such interventions have usually arisen when a particular LA has consistently failed to meet government threshold targets. Following direct intervention by the Secretary of State in 2000, Cambridge Education secured a £105 million contract to run education services in the London Borough of Islington from 2000-2007. The contract was extended to run through until 2013. Babcock International Group Plc. have been running school improvement services in Waltham Forest since 2008.
- School inspections are also contracted out to profit making providers in many instances. Ofsted deploys around 440 of its own school inspectors, augmented by almost 2,000 additional inspectors employed by Regional Inspection Service Providers. Prospects Services Ltd. covers a £71 million contract to deliver the Early Years inspection services for the North of England and the Midlands while Serco Plc. currently holds a 6 year contract worth £53million to provide school inspection services in the Midlands.
- The private sector provides all kinds of services in schools. In 2009–10 school spending on “Other professional services” was £572 million. The proportion of such spending that is spent outside the local authority is unclear, though it is likely to be rising as Academies are given control over budgets traditionally ‘top-sliced’ by their local authority. Even where the LA commission services like IT and facilities management this is often outsourced: for example, Birmingham, Devon and Sefton councils have all outsourced such roles to the private sector.
- Private providers play a growing role in higher education, and deliver much post-16 skills and training.
- Governors are able to commission private sector firms to manage, though not own, their schools. For example in 2007 Edmonton Council commissioned Edison Learning to manage Turin Grove school for three years. In January 2010 Priory special school in Taunton, Somerset also commissioned a private firm to run it. The Guardian noted that in both cases “The results were impressive and the schools improved.” More recently a new Free School, IES Breckland, has agreed a ten year management contract with the Swedish education firm IES.
- Private providers are already playing a large role in delivering state education. So it is unclear why private provision or private ownership should be ruled out ‘in-principle’ for mainstream schools or the 4–16 age bracket.

## Private provision is extensive in other countries, and appears to be working

- One hundred percent profit making companies are permitted to operate publicly funded schools in both Sweden and the USA. The most recent figures from 2008 indicate that 64% of Free Schools in Sweden are operated by for-profit companies. 56% of Charter Schools in the United States are managed by profit making providers.
- Most studies of independently-run state schools compare both voluntary and private providers with traditional state run schools. There is clear evidence that independently run schools are outperforming state run schools, based on 'gold standard' randomised control trials. Because for-profit providers provide such a large proportion of Charter Schools and Free Schools, this strongly suggests that on average they are outperforming traditional state-run schools.
- There are fewer studies that look specifically at the difference in performance between voluntary and for-profit independent providers. A recent report examining Charter Schools in Boston found that for-profit providers managed to raise mathematics scores by more than half a standard deviation per year in middle school, compared to non-profit provision.
- Private providers may have stronger incentives to grow and replicate effective models than voluntary groups.

## Social enterprise schools – ideally owned and run by teachers

- Despite the evidence above, ideological opposition to private provision of schools is strong. One poll for the think tank Reform found that 34% of voters disagreed with the statement that “In general, if private sector companies do a better job of running public services than the government, then they deserve to make a profit.”
- This report challenges the idea that there must be a binary choice between for-profit and not-for profit schools. If policy makers feel unable to introduce private provision, social enterprise schools may be a halfway house. John Lewis style mutuals are increasingly popular in other public services, including hospitals and social work practices.
- The government should launch social enterprise pilots to run a number of schools within 4–16 year old mainstream education. Such schools would be allowed to distribute 50% of any school surplus as a dividend to shareholders on an annual basis. The remaining 50% would have to be reinvested in the school.
- Teachers and other school employees should be given the option of holding shares in the parent company or in the school itself if it is an individual legal entity. Social enterprise schools could be owned and run by teachers creating strong incentives for improvement.

## Further assurances

- The operators of social enterprise schools could be subjected to a higher degree of scrutiny than not-for-profits, at least initially.
- **A reducing deprivation test:** This report argues that social enterprise pilots should operate within areas of greater deprivation and ensure that enrolment



initially includes at least 20% of students eligible for free school meals and hence the pupil premium.

- **A performance test:** A rule could be introduced such that the operators of a social enterprise secondary school would receive no share of any surplus unless a certain proportion of their pupils made the expected level of progress.
- **An 'asset lock':** Free School buildings and facilities procured by government could not be sold off for private gain. An exception to this principle would be made in those instances where the providers are prepared to invest their own capital to build a new school from scratch.

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# Introduction

Ever since the emergence of City Technology Colleges (CTCs) in the early 1990s, successive governments have argued that greater autonomy and freedom to innovate, plus improved accountability, will improve our schools. They have embraced the idea that greater choice for parents and competition between schools will drive up standards.

Reform has consequently gone some considerable way in shifting education policy in a more market orientated direction. However, while politicians have endorsed the idea of quasi-market forces, for-profit private providers remain controversial. The current Secretary of State for Education, Michael Gove, has made it clear he does not think for-profit involvement, as that seen in Swedish Free Schools, is currently necessary for the expansion of the Free Schools programme in Britain. Opposition from many in the education establishment, particularly the trade unions, is steadfast.

This report seeks to challenge opposition to any for-profit provision in our schools.

It does not present the case for a purely free market model, or argue that schooling in England should be transferred entirely to the private sector. Rather, it aims to outline some of the key benefits, including expertise and finance which the private sector could bring to our schools.

**Chapter 1** discusses current government policy on school autonomy, reviewing the extent to which choice and competition in the schools market has developed, potentially paving the way for an element of for-profit provision to enter the market.

**Chapter 2** details how, set against a backdrop of falling standards in recent years relative to international comparators, the English school system faces some considerable challenges. Significant numbers of Free Schools are needed to provide new school places to meet rising demographic demand, particularly in areas such as London. Many of our most deprived areas are held back by persistently failing schools; hence it is vital that we see the establishment of new secondary Free Schools as quickly as possible. The current purely not-for-profit approach to Free Schools will not enable us to meet such an ambitious target. Compounding these problems is the fact that our education system continues to be excessively inflexible on teachers' pay and conditions. This applies to Academies as well as maintained schools and, overall, is inhibiting a performance-driven culture. The potential innovation and flexibility that could be engendered by permitting even a degree of for-profit provision within the Free Schools system and which could help reverse these key challenges is also highlighted in this Chapter.

**Chapter 3** examines the role of for-profit providers in delivering public services more generally, and the public's attitude to such provision is also scrutinised. This chapter shows that the presence of for-profit provision is the norm, rather than the exception, in most other areas of public service provision and that education lags behind in this respect.

**Chapter 4** investigates some of the ways through which for-profit providers are already involved in state education, specifically in relation to early years education, pupils referral units (PRUs) as well as other aspects of alternative provision and special educational needs (SEN). It also discusses the extent to which private companies are currently providing school support services and outsourcing. The presence of these providers indicates that a significant degree of the public's suspicion of for-profit education stems from a lack of awareness of the extent to which private companies already deliver services to school age children.

**Chapter 5** investigates similar reforms which have been tried and tested in other countries. We look at Sweden and the USA, where there has been early experience of profit making provision of state funded schooling, examining the lessons that can be learned in relation to scale and performance in particular.

**Chapter 6** questions whether there really is a binary divide between for-profit and not-for-profit models. Given opposition from the educational establishment, we examine whether a social enterprise model might work. This would raise the possibility of employee ownership, a model which is now expanding in other public services. Teachers could become owners and shareholders in their own schools.

Finally, **Chapter 7** outlines some of the elements of an accountability framework within which social enterprise schools should operate, as well as pointing towards some areas where supporting reforms would assist the development of such a model.

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# 1

## School Choice and Competition

### Current government policy

Current government policy is, at least tacitly, encouraging a mixed market in the provision of schools designed to encourage choice and competition. With public opinion still somewhat suspicious of the private sector delivering public services, the current government has been reluctant to embrace the role which for-profit companies could play in the development and running of our schools. Nonetheless, there is undoubtedly an emerging, albeit limited, schools marketplace, characterised by increasing school autonomy and enabling more choice for pupils and parents.

Successive governments have argued for increased choice in the schools system. New Labour's Academy programme, itself launched in 2000, built directly upon the City Technology Colleges (CTCs) created by the Conservatives in the late 1980s and early 1990s. While CTCs never grew to any great scale – just 15 were established with the last created in 1993 – they did prepare the ground for Academies, with close similarities in terms of the urban location, school specialism and sponsorship arrangements. New Labour saw the need for a new type of school, intended to either replace an existing failing school or to provide a new school in an area of sustained educational underachievement. Central to this was a belief that greater school autonomy would improve standards. In the foreword to the 2005 *Better Schools for All* white paper, Tony Blair gave a typically strong endorsement of the importance of choice and competition, in particular highlighting the experience of Sweden. Blair wrote:

*“Many other countries have successful experience with school choice. There is increasing international evidence that school choice systems can maintain high levels of equity and improve standards. Swedish parents can choose an alternative school to their local one, including a diverse range of state-funded independent schools. Studies have found that schools in areas where there is more choice have improved most rapidly.”<sup>1</sup>*

Current policy is rightly preoccupied with ensuring that this emerging schools market place should be built on the principles of fairness and equal opportunity. To achieve this, the government are approaching the extension of choice and competition as a means to improving access for the poorest children by ensuring good new schools are not just established in socio-economically advantaged areas. The market is being shaped to address this with the introduction of the pupil premium.<sup>2</sup> Introduced in September 2011, the premium allocates an additional £430 p.a. “to deprived children who are currently known to be eligible for free school meals in both

1 Department for Education, Higher Standards for All: More Choice for Parents and Pupils, 25 October 2005

2 A policy proposed by Policy Exchange in *School Funding and Social Justice* (2008)

mainstream and non-mainstream settings and to children who have been looked after for more than six months.” It was announced in December 2011 that the premium will increase to £600 from April 2012.<sup>3</sup> The aim is to “ensure those teaching the poorest children get the resources they need to deliver smaller class sizes, more one-to-one or small group tuition, longer school days and more extracurricular activities.”<sup>4</sup> While it will still be some time before the impact of the pupil premium can be fully assessed, it is an important step to introducing progressive financing in schools.

With this focus on the benefits of the reform for disadvantaged children, a broad consensus of political opinion, encompassing Conservative, Liberal Democrat and New Labour, has been built up. Combined with progress made under the last government, there is a growing acceptance of the benefits of school choice.

### A developing market

Significant parts of the state school education system continue to evolve on a course originally charted by previous governments, albeit with increased vigour and zeal. In addition to the original Academy model pioneered under Tony Blair, (“Sponsored Academies”) the coalition government has allowed good and outstanding schools to convert and gain the same freedoms as these academies (“Converter Academies”). In addition, it has allowed groups of parents to set up new schools (“Free Schools”). While the Academies programme is led by government and schools, the Free Schools programme is about enabling new schools to enter the system driven by parent demand.

As of 1st February 2012 there are 1580 academies open in England, including over 340 Sponsored Academies and 1240 Converter Academies.<sup>5</sup> By September 2012 there will be 96 open Free Schools.<sup>6</sup>

45% of secondary schools are either already open as Academies, or in the process of becoming one. The current government has also renewed the emphasis on using the Academy programme to turn around failing schools. In June 2011, the Secretary of State for Education, Michael Gove, announced that the weakest 200 primary schools in the country would become Sponsored Academies in 2012–13. In September 2011, almost 50 schools previously rated as no more than “satisfactory” by OFSTED, were sponsored by charitable bodies, existing school chains and universities to become Academies.<sup>7</sup>

In addition to Academies, both old and new, University Technical Colleges (UTCs) are adding further variation to the schools landscape. Intended to deliver a more focused vocational curriculum in close collaboration with specific businesses, 37 new such colleges are currently at proposal stage. Studio Schools, which operate under a blueprint developed by the Studio Schools Trust,<sup>8</sup> present another work-focused route opening up to the 14–19 age group. They aim to encourage employers to be involved in the running of the Studio School with the intention of offering guaranteed work placements and paid commissions to students during their studies.

As well as allowing new schools to enter the system, recent reforms have made it easier for successful schools to expand, strengthening the competitive forces in the system. The government’s new admissions code will allow schools to increase their admissions number regardless of the views of central or local government. This is a key flexibility if for-profit providers are to be attracted into the system.

<sup>3</sup> Department for Education, Pupil Premium – What you need to know, 12 December 2011

<sup>4</sup> Department for Education, Structural Reform plan, July 2010

<sup>5</sup> Department for Education, General Article: *Open academies and academy projects in development*, 3rd February 2012

<sup>6</sup> Information provided by the New Schools Network

<sup>7</sup> Education Secretary address to National College for School Leadership’s annual conference in Birmingham, 16 June 2011

<sup>8</sup> Studio Schools Trust, Whitworth Building, Ashton Old Road, Manchester M11 2WH

Generating a surplus through economies of scale, private providers would be quite reliant on the ability to grow and expand without bureaucratic hindrance. However, reform allowing at least some element of for-profit provision into the school system in the first place remains outstanding. Advancing the case for such reform occupies the rest of this report.

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# 2

## Addressing the Challenges – Harnessing the Private Sector

Public services face significant challenges as budgets tighten and the public's expectation of service quality continues to rise. Schools are not exempt from these pressures. This is particularly the case as schools are now operating in a considerably more restricted financial environment than was the case for the decade from 1997.

The pressure is magnified when we consider the significant task which the UK faces in striving to compete in the global skills market. In essence, there is a shortage of money and poor performance in many parts of the state system, just at the time when the UK urgently needs to increase its skill levels. International league tables make the challenge clear – the UK is ranked 25th for reading, 28th for maths and 16th for science in the PISA rankings.<sup>9</sup> In 2006, the UK was placed 17th, 24th and 14th respectively,<sup>10</sup> indicating a clear decline in relative achievement. Meanwhile employers regularly bemoan the 'quality' of school leavers and graduates. A survey conducted by the CBI in May 2011 revealed that 42% of employers were not satisfied with the basic use of English by school and college leavers and more than a third were concerned with the basic numeracy skills.<sup>11</sup>

According to the Office for National Statistics, between 1995 and 2009 the employment rate for people with low level or no qualifications fell from 60.1% to 55.8%, while for people with higher qualifications employment rates increased slightly from 77.2% to 77.4%.<sup>12</sup>

### What Problems Could Allowing Private Provision Help to Solve?

There are at least three fundamental areas where the private sector's involvement could go some way in helping our schools overcome major challenges.

#### **1. Education spending faces a funding squeeze. In some areas many new school places are needed to meet rising demographic demand. Additional investment from the private sector could help.**

Schools face a significant reduction in capital funding in coming years. Having wound down Labour's £55 billion Building Schools for the Future (BSF) secondary school rebuilding plan, the DfE received an "extremely tight" capital settlement with a reduction of 60% in 2014–15 compared to the historic high in 2010–11.<sup>13</sup> This is emerging in the context of rising primary school admissions yet a critical shortage of school places in the next five years.

9 OECD (2010), PISA 2009 Results: Executive Summary, "What Students Know and Can Do: Student Performance in Reading, Mathematics and Science", Figure 1, OECD Publishing. p.8

10 Shepherd, J. (7 December 2010), UK schools slip down world ranking. *The Guardian*. Retrieved from <http://www.guardian.co.uk/>

11 See CBI website, Education and Skills: <http://educationandskills.cbi.org.uk/reports/00360/>

12 Social Trends 41 – Labour Market

13 Department for Education, School funding announcement 2011–12, Written Ministerial Statement on Education Spending

An additional 540,000 primary school places will be required by 2018, with official figures projecting an increase in primary pupils of 14%, from 3.96 million to 4.5 million. The rise is steepest in London, where the population of five to 10-year-olds will rise by about 16%.<sup>14</sup> Funding has been pledged to deal with providing places, with £250 million being set aside for London alone.<sup>15</sup> Yet, questions about the sustainability of such funding arise especially when one considers that today's crisis in primary school places is tomorrow's dilemma for the secondary sector. The government has set aside an additional £1.3 billion for repairs in 2011–12 but this is viewed by some as nowhere near enough, with figures as high as £8.5 billion being quoted as the investment needed to meet the current backlog of repairs in English schools.<sup>16</sup> In addition, these repair cost estimates do not account for new problems caused by schools that had put off repairs in the expectation of being part of the BSF programme. July 2011 saw Michael Gove announce a new PFI programme, with an expected value of £2 billion in up-front construction costs, though this still remains modest when set against the new builds, refurbishment and repairs which are required.<sup>17</sup>

Severe cuts to capital grants come alongside restraints on day to day revenue. At the time of the 2010 Spending Review, a small real-terms increase in schools revenue spending was announced. Since then, forecasts for economy-wide inflation in 2011–12 have risen, meaning a 1.2% real-terms fall in 2011–12. Schools' spending is then expected to be frozen in real terms between 2011–12 and 2014–15.<sup>18</sup> The level of the Dedicated Schools Grant per pupil is set to be frozen in cash terms between 2010–11 and 2014–15 at around £5,300 per secondary school pupil<sup>19</sup> and £3,317 per primary school pupil.<sup>20</sup> To supplement the traditional per pupil funding, a pupil premium of £430 has been payable since September 2011, allocated to children who are eligible for free school meals. The premium will rise to £600 per child from April 2012 and funding will be widened to any child who had been registered for free school meals in the past six years. In addition, the pupil premium sits alongside a £200 premium for children who have a parent in the armed forces.<sup>21</sup> Total spending on the Pupil Premium will rise from £625 million in 2011–12 to £2.5 billion by 2014–15. However, despite this overall funding remains extremely tight.

These financial and capacity constraints are compounded by the inability of schools to attract external investment or take on debt to make up any funding shortfall. Schools are also hamstrung by a lack of flexibility to manage budgets across financial years, inhibiting their ability to make longer term investment decisions. Schools are severely constrained in terms of managing budgets flexibly, specifically when it comes to building up reserves from one year to the next. In the past, a large number of LA maintained schools were able to build up healthy balances but since 2008 councils have been required to claw back excessive surplus balances from schools. Surplus rules for Academies are slightly more flexible, though they remain limited to an annual carry-over of 12% (2% revenue and 10% capital) of their budgets. Hence, overall, successful schools are limited in the extent to which they can build up reserves to meet basic capital requirements or even to expand to meet increased demand. Combined with the fact that they are not allowed to take on debt, schools therefore find themselves currently dealing with a reduction in central government capital investment with neither the means nor the flexibility to adopt more innovative budgeting or draw upon private sources of finance.

14 Department for Education official figures, October 2011

15 Cecil, N. (3 November 2011), £250m to boost school places in the capital. *Evening Standard*. Retrieved from <http://www.thisislondon.co.uk/standard/>

16 Cook, C., A. Barker and E. Hammond (25 March 2011), Schools in England need £8.5bn repairs. *The Financial Times*. Retrieved from <http://www.ft.com/home/uk>

17 Michael Gove statement in House of Commons: Hansard, Debate 19 July 2011, c793

18 Chowdry, H. and L. Sibieta (October 2011), 'Trends in Education and School Spending', IFS

19 Department for Education, School funding announcement 2011–12, Executive Summary

20 Aggregation of Individual School Budgets (ISB) for primary and secondary 2010 and this national figure by the national number of primary and secondary pupils

21 Department for Education, School funding announcement 2011–12, Executive Summary



The injection of additional investment from the private sector could help, given that government resources will remain limited for some time to come. Allowing private providers to invest directly into schools would have a number of advantages over private investment through PFI: it would allow investment into non-capital spending, and allow companies to both build and operate schools, allowing better integration between builders and operators, and enabling schools with innovative pedagogies to enter the market with models.

## **2. We need more good school places. But there are limits to how much the voluntary sector alone can provide.**

As well as looming overall shortages of school places in some areas, there is a shortage of good school places in particular. 50% of all the current surplus secondary places are in the worst performing 25% of secondary schools.<sup>22</sup> Last year in England 17% of pupils did not get their first preference and 3.5% did not get any of their preferred schools. The data varies by region – in London 34% did not get their first preference with 6% not receiving an offer from any of their preferred schools.<sup>23</sup> Unless more good school places can be created, these figures will get worse. Policy Exchange analysis undertaken in 2011 found there to be 53 secondary schools running more than half empty. 225 schools (7% of the total) are more than a third empty. Almost all are poor GCSE performers.<sup>24</sup> In order to provide a viable alternative to these persistently failing schools, a considerable number of new Free Schools are required within a short time frame.

Yet, there are limits to the numbers of groups and individuals ready to sponsor an academy, or set up a new Free School. Setting up a new school is a significant capability challenge for most small groups who have to find pro-bono advice on programme and project management, business management, finance, architecture and engineering, not to mention cost-effective commissioning and procurement of infrastructure, goods and services. Free Schools face the challenge of finding a suitable building, acquiring it or negotiating a lease agreement and then delivering on planning consent and conversion. One of the key criteria for assessment of Free School proposals is the cost of buildings – both initial capital cost and ongoing revenue.

While it is remarkable that voluntary groups have achieved so much, the current development of Free Schools is excessively dependent on volunteerism and philanthropy.

Effectively harnessing the profit motive could really enhance capability and lead to the emergence of new Free Schools at faster rate. Private providers have, or can easily access, the expertise needed to deal with the management and logistical challenges set out above within a relatively short period of time. Furthermore, as will be discussed later on in this report, with proper incentives in place, the private sector can be steered towards opening schools in those areas which need them most. Private providers have strong incentives to expand and grow their business in a way that not-for-profit providers do not.

Some Free School groups are already appointing profit making companies to manage the process of setting up a school for them.<sup>25</sup> But, as this report will explore below, there are limits on the private sector's ability to provide new schools. This will limit the number of new good school places.

<sup>22</sup> Policy Exchange internal analysis using DfE figures on surplus capacity and GCSE pass rates, February 2011

<sup>23</sup> Policy Exchange internal analysis using most recent DfE figures on secondary applications and offers

<sup>24</sup> Policy Exchange internal analysis using DfE figures on surplus capacity and GCSE pass rates, February 2011

<sup>25</sup> Edison Learning, "Edison Learning wins a place as Project Manager and Educational Services provider on the DfE Academies and Free Schools Framework", 30 November 2011

**3. The labour market for teachers is inflexible, and doesn't reward high performers. But it will remain difficult for schools to vary from these national norms until there is a critical mass of independent state schools. Allowing private provision might allow more rapid progress for a number of reasons.**

While Academies and Free Schools have greater freedoms over pay and staffing on paper, in practice it can be difficult for them to take full advantage of these freedoms. Academy schools will retain staff from their predecessor school, and TUPE<sup>26</sup> rules lock in their current conditions. Even in the case of Free Schools, it is difficult to deviate from national pay and staffing norms when only a minority of schools have such freedoms, and there is often strong union opposition to doing so.

To some extent the ability of schools to use the freedoms they have will depend on independently-run state schools attaining a critical mass in the system. Allowing for-profit providers to enter the market could help accelerate this process.

Furthermore, for-profit providers might be more likely to operate sizable chains of schools, rather than “one off” schools. This, plus expertise they might bring from outside the schools sector, might make them more confident in innovating in the face of union opposition than, say, a single school set up by a group of parents.

It is notable that some of the most interesting innovations in pay and staffing are occurring in the larger (not-for-profit) federations of schools. For example, the Harris Federation of Academies offers performance-related bonuses, as well as private medical insurance and a heavily subsidised Master's degree programme to its staff. ARK Academies also offer Master's bursaries as well as international development and other travel opportunities.<sup>27</sup>

## Summary

At least some element of for-profit provision within our state school system could therefore offer a means of radically addressing many of the key challenges facing 4–16 mainstream education. Outright opposition to the involvement of even a modest degree of private investment fails to recognise the potential benefits which it could bring, particularly in terms of improving educational outcomes for pupils from underprivileged backgrounds. It also ignores the fact that the profit motive has for some time been contributing to the improvement and reform of other key public services. Education still lags somewhat behind these other services, an issue which will be discussed in our next chapter.

26 Transfer of Undertakings (Protection of Employment) Regulations

27 Lipson, B. (2011). *Myths, evidence and innovation: a guide to making the most of Free Schools freedoms*. CfBT Education Trust p. 15

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# 3

## For-Profit Provision in Other Public Services

State school education in England remains some way off from operating in an open marketplace. However, the growth of Academies and the emergence of Free Schools, together with the growing number of non-state providers who are establishing strong bases within the schools market, has ensured a greater degree of choice and flexibility within the system than before. The emerging market in education is such that the role which profit making groups could play in running Free Schools has become the obvious next area of debate. Successive governments have shied away from allowing any form of profit making in the direct delivery of state funded schooling. The Coalition government has made it clear that all state funded schools must operate on a strictly non-profit basis.

### Attitudes towards profit making in the delivery of public services

The public's perception of for-profit provision of state services is worth considering carefully in any assessment of how the private sector might become more established in the delivery of state schooling. Public opinion remains cool to the idea of profit making schools. A 2011 survey for Reform found that 49% of people thought that state schools should be delivered by government alone. However, more people thought that government, charities and the private sector (31%) should deliver services than just government and charities (17%).<sup>28</sup> This suggests that public attitudes to profit making in schools are not as entrenched or dogmatic as many opponents suggest. Indeed, research carried out by the Parthenon Group showed that 60% of parents would be willing to consider sending their child to a for-profit private organisation that had experience of running schools.<sup>29</sup>

While these statistics give an indication of a degree of public reticence, they also highlight a willingness on the part of the public to accept that for-profit providers might have a role to play. In the Reform survey, the majority of people (52%) agreed that if private sector companies do a better job of running public services than the government, then they deserve to make a profit. By contrast, just 34% of people cared more about the fact that the service provider was making a profit than the quality of provision.<sup>30</sup>

In this regard, education still lags behind other key areas of public sector delivery. Comparing the schools sector to the prevalence of profit making in other public services, former Blair advisor Julian Le Grand recognises this as a

28 Reform, Quantitative poll – attitudes to private sector involvement in public services, May 2011

29 Parthenon Group (October 2010). Academies, what does the future hold?

30 Reform, Quantitative poll – attitudes to private sector involvement in public services, May 2011

“nettle that was not grasped.” Le Grand suggests that schools were viewed as a difficult sector to reform due to entrenched views and resistance to change within the education establishment.”<sup>31</sup> Connor Ryan, who advised David Blunkett and Tony Blair on Education policy, remarked that: “there is a strong public service ethos in the education system, which has always been resistant to profit making from the direct provision of education. The feeling is that if profits are made it can only be at the expense of educational inputs, such as teachers or equipment. There is a sense that it would be immoral to make profits from the direct provision of education, even though many educational services clearly generate profits.”<sup>32</sup>

Despite particular opposition and cultural aversion to ‘for-profit’ involvement in the delivery of 4–16 school education, the private sector has faced considerably less opposition in moving into other areas of public service delivery. The schools sector is now the exception rather than the norm.

### Profit making in other areas of public service delivery

The UK government has a long history of engagement with the private sector in the direct delivery of services. There is now considerable private sector involvement in areas as diverse as welfare to work, justice and health.

#### Involuntary services

The use of the private sector has been notably less controversial for involuntary services, such as welfare and prisons, which the general public do not expect or hope to use. Privately managed prisons were introduced to the UK in the 1990s.<sup>33</sup> Out of a total of 139 prisons in the UK, 14 prisons are now managed by private companies such as Sodexo Justice Services, Serco Group plc and G4S Justice Services LLC.<sup>34</sup> The management of a further nine prisons will be put out to competitive tender this year. In recent years, publicly funded welfare to work services have also been delivered by private sector providers. The Pathways to Work programme, which operated from 2008 to early 2011, aimed to get people off incapacity benefit and into work. 60% of providers were either from the private or charitable sector, with the remaining 40% operated by Job Centre Plus.<sup>35</sup> The main driver for the government was to transfer risk to the delivery organisation, so contracts included an element of payment by results based on the benefit payments saved from getting people into work.<sup>36</sup> In the more recent £5 billion Work Programme, almost all of the prime contractors are in the private sector, and the majority of the work is likely to be carried out by the private sector. The remainder is to be delivered mostly by the voluntary sector with only a small role for the public sector.<sup>37</sup>

Even in policing, which might be thought less amenable to private provision than other sectors, there is increasing outsourcing. Cleveland police, for example, have outsourced a wide range of back office functions, transferring 700 members of staff to the private sector, and saving £50 million in the process.<sup>38</sup>

#### Choice based services

Although at times controversial, profit making involvement in choice based public services has also become much more common. An estimated 5% of NHS services are delivered by the private and voluntary sector and it routinely buys operations from the private sector.<sup>39</sup> 200 GP surgeries are now operated by private companies.<sup>40</sup> The last government introduced Independent Sector Treatment

31 Interview with authors

32 Interview with authors

33 See Ministry of Justice website, <http://www.justice.gov.uk/about/hmps/contracted-out.htm>

34 See [politics.co.uk](http://www.politics.co.uk/reference/private-prisons): <http://www.politics.co.uk/reference/private-prisons>

35 Department for Work and Pensions, Pathways to Work – Jobcentre Plus support from April 2011

36 Department for Work and Pensions, The Work Programme

37 *Social Enterprise*, reporting DWP data, 6 April 2011

38 Policy Exchange, *The Cost of the Cops*, September 2011

39 Peston, R., (1 June 2011), How much private sector in NHS? *BBC News*. Retrieved from <http://www.bbc.co.uk/news/>

40 [http://www.pulsetoday.co.uk/newsarticle-content/-/article\\_display\\_list/11036525/private-companies-now-running-more-than-200-gp-surgeries](http://www.pulsetoday.co.uk/newsarticle-content/-/article_display_list/11036525/private-companies-now-running-more-than-200-gp-surgeries)

Centres (ISTCs), which are privately run providers of NHS acute services. The first contracts were signed in September 2003 and the first ISTC commenced services in October 2003 at Daventry.<sup>41</sup> These typically work on bulk contracts paid below the national tariff that NHS Hospitals can charge NHS Primary Care Trusts. The contracts allow for-profits to be paid out whether the agreed numbers of patients are treated or not and regardless of success rates.<sup>42</sup> Despite this, a Department of Health report in 2006 found that patient satisfaction was running at over 94%.

The 'Any Willing Provider' model specifically demands that NHS organisations compete on an equal footing against private companies and not-for-profit organisations for public money.<sup>43</sup> The procurement guide for commissioners of NHS-funded services clearly states that the procurement process should not favour any market sector (public, private, voluntary, charitable and social enterprise).<sup>44</sup> This includes ensuring that decisions are based on how well an organisation meets evaluation criteria, rather than decisions being made based on organisational type. The Principles and Rules for Cooperation and Competition "are intended to apply to all commissioners and providers of NHS services irrespective of whether they are public, private or third sector organisations."<sup>45</sup> The clear intention is for a level playing field for all providers.

Private sector provision is, therefore, slowly becoming more common in the health sector, culminating most recently in the award to a private company, Circle, of the right to deliver a full range of hospital services for the first time in the history of the NHS (see box below).

41 Department of Health, Independent Sector Treatment Centres – a report from Ken Anderson, Commercial Director, Department for Health, 16 February 2006

42 Department of Health, What patients say about Treatment Centres, 8 February 2007

43 Cooperation and Competition Panel, Review of the operation of 'Any Willing Provider' for the provision of routine elective care: Final Report, 28 July 2011

44 Department of Health, Procurement guide for commissioners of NHS-funded services, 30 July 2010

45 Department of Health, Principles and rules for cooperation and competition, 30 July 2010

46 See Circle Holdings PLC website: <http://www.circlepartnership.co.uk/about-circle>

47 Ramesh, R., (10 November 2011), Private firm to run NHS hospital. *The Guardian*. Retrieved from <http://www.guardian.co.uk/>

48 Jeffreys, B. and N. Trigg (10 November 2011), Circle in deal to run Hinchingbrooke NHS hospital. *BBC News*. Retrieved from <http://www.bbc.co.uk/news/>

49 See Circle Holdings PLC website: <http://www.circlepartnership.co.uk/about-circle/circle-story>

### Circle Holdings PLC Healthcare

Circle is an "employee co-owned partnership with a social mission to make healthcare simpler and better value for patients." Circle is co-founded, co-run and co-owned by clinicians, forming the largest partnership of healthcare professionals in Europe,<sup>46</sup> and is described as a "John Lewis-style partnership". Circle will manage the Hinchingbrooke hospital in Cambridgeshire from February 2012, after the government agreed to a decade-long contract.<sup>47</sup> The hospital had previously become burdened with substantial debts.

The consultants and healthcare professionals who work for Circle own the facilities they work in, with 49% of its ownership in staff hands and the other half of shares held by financial backers. It operates a scheme to allow more shares to be gained through a performance-related rewards system. Doctors may take a slice of the profits, though buildings will remain in public hands and the employees retain their pay and pension on existing terms, so Circle's takeover of Hinchingbrooke hospital does not amount to a full privatisation.

The firm will become the first non-state provider to manage a full range of NHS district general hospital services.<sup>48</sup>

Circle currently has four locations across Britain of varying size, in Bath, Nottingham, Stratford-upon-Avon and Windsor, with a further site under construction at Reading. The organisation claims an 18% productivity gain at Nottingham and extremely high levels of report customer satisfaction at their centre in Bath.<sup>49</sup>

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# 4

## The Extent of For-Profit Provision in Schools Today

Ideological, ‘in-principle’, opposition to private provision in schools ignores the fact that private companies already operate in our schools, and indeed are responsible with educating some of our most vulnerable students. There is lack of transparency, both at a local and central government level, about the proportion of education budgets are being routed towards for-profit providers.

During the course of our research, we used Freedom of Information requests to ask 39 LAs to disclose those percentages of their education budgets which they spend each year on for-profit providers of Special Educational Needs (SEN), alternative provision (including Pupil Referral Units – PRUs) and nursery education. The data is patchy. 20 of those LAs reported that they do not hold this information and currently make no distinction between for-profit and not-for-profit external providers. Nine failed to respond within the required time limits. The degree to which LAs are expected to break down their costs might help to explain this, particularly if one considers that in the s-52 financial returns which LAs must submit annually, the budget allocated to SEN pupils refers to independent, non-maintained and private providers all in the same budget line.

Despite these limitations, this chapter examines what available evidence there is on for-profit provision within our state-funded schools system, challenging the view that it has no role to play and identifying how private companies are already operating within the system.

### For-profit provision outside of mainstream schools

#### Pupil Referral Units and Alternative Provision

The 1996 Education Act imposes a duty on LAs to ensure that alternative provision is secured for pupils who are not in a position to attend a mainstream or special school. These pupils usually need additional support or have been excluded for discipline reasons so it is not appropriate to provide this service within the mainstream school system.<sup>50</sup> These students often have complex social and emotional needs as well and will require other LA services such as social services, the educational psychology service, courts and youth services. To meet this need LAs often set up Pupil Referral Units (PRUs) to accommodate these children on a temporary basis.

There is a lack of solid data around how and by which type of provider alternative provision is delivered. This problem was encountered by a number of groups and individuals we spoke to who also have an interest in this area.

There are around 450 PRUs in England, operated by LAs, the voluntary sector or, the private sector. They educate around 15,000 students per year at a cost

50 Department for Education, Exclusion Guidance for Schools, published 2008

of around £17,000 per pupil, which gives a national market of approximately £255 million. PRU provision is a clear example of where a market, which includes profit making private providers, is already opening up to provide direct specialist schooling to children of statutory school age.<sup>51</sup>

The majority of PRUs are still LA run. However, there are examples of LAs which have contracted out all of their PRU provision to private profit making providers. In Islington, Cambridge Education (CE@Islington) runs four PRUs for around 90 pupil placements. The value of the contract is approximately £22 million over a ten-year period. This ranges from Key Stage 2 provision to a behaviour unit and CE@Islington employs the head teachers, staff and controls the budgets.<sup>52</sup>

An Ofsted report on alternative provision (AP) published in June 2011 visited 61 providers of AP used by 23 schools and 16 PRUs. Forty of the placements for pupils were with private providers. Ofsted itself recognised this is still an unregulated area with only 17 of the providers subject to any inspection regime.<sup>53</sup> There was no identification of which of the private providers were for-profit. The costs of placements for students ranged from £20 to £123 per day in the providers visited with the most common cost at £50 per day. The schools and PRUs were spending between £5000 and £86,000 on alternative provision each year. One PRU was spending £1,055,666 for 206 students as it commissioned for schools throughout its LA area.<sup>54</sup>

Freedom of Information requests in relation to for-profit provision of alternative provision yielded interesting responses from two LAs in particular: Northumberland and North Lincolnshire. As Table 1 demonstrates, alternative provision is largely delivered by private for-profit providers in each of these areas.

**Table 1: Alternative providers by sector in Northumberland and North Lincolnshire<sup>55</sup>**

		Alternative provision					
		Private for-profit		Private non-profit		Public	
<b>Northumberland</b>	2007/08	£187,800	67%	£63	0%	£92,000	33%
	2008/09	£276,100	70%	£11,200	3%	£104,000	27%
	2009/10	£212,000	64%	£15,000	4%	£106,500	32%
	2010/11	£225,100	50%	£7,700	2%	£239,600	48%
<b>North Lincs</b>	2010/11	£247,002	74%	–	0%	£86,846	26%

51 Ofsted, Alternative Provision, 21 June 2011, No. 100233

52 Based on interviews with the authors

53 Ofsted, Alternative Provision, 21 June 2011, No. 100233

54 Ibid

55 Response to FOI requests (December 2011 and January 2012)

56 Under the Education Act 1996

57 Out of authority placements for special educational needs – Audit Commission, Local Authority Report, 2007

58 Using the total number of SEN pupils as 1,691,790 from SFR (Statistical First Release, 23 June 2011) it is possible to give a percentage of those pupils attending the different types of provision listed

### Special Educational Needs

SEN is another area where LAs have specific statutory responsibilities towards children with particular educational needs. Special schools admit children with statements of additional needs, detailing disabilities and illnesses ranging from medium learning disabilities to those children requiring support for Profound and Multiple Learning Disabilities.<sup>56</sup> In 2007/8 the total spend on SEN was almost £4.9 billion. An Audit Commission report in the same year estimated the total spend by LAs on out-of-authority SEN provision (i.e. voluntary and private) to be £500 million, or just over 10% of the total spend.<sup>57</sup> The national cohort of children in full time education with special needs in 2010 was 1,691,790, equating to 20.9% of the total school population.<sup>58</sup> Of these, 220,890 children had a statement of SEN and

93% of these were placed in mainstream schools (including Academies) or LA run special schools, with the remainder in either independent special schools (4.3%), non-maintained special schools (2%) or Pupil Referral Units (0.8%). Independent special schools are usually run for-profit whereas the non-maintained are usually defined as those run by charities or voluntary bodies. Under the Education Act 1996 the LA must pay all in respect of a child's education at a non-maintained school, although this is not necessarily the case for independent special schools.<sup>59</sup>

Students placed in independent special schools tend to have behavioural, emotional and social difficulties (BESD 30%) or a requirement for specialist services for those with Autistic Spectrum Disorders (ASD 23%). The Audit Commission suggests the average cost of a placement is over £57,000 and the proportion of these placements had been steadily increasing since 2003. In order to fulfill their obligations, LAs do spend public money buying places for children in independent special schools but the breakdown of provision is so varied that for most LAs there is no reliable data to provide an exact breakdown of spending.

Some of these schools are run by charities such as Action for Children, who have five special schools in England. However, there are private providers too: the Priory Group Ltd. and Cambian Healthcare Ltd. are two examples of private profit making companies who provide special school provision and have placements that are open to LAs.

### The Priory Group Ltd

Despite being best known for supporting celebrities through rehabilitation, 75% of the care provided by the Priory Group is publicly funded. This includes the Age Appropriate Inpatient Adolescent service for 8 PCTs across NW London under a three-year contract to deliver services for all adolescents with acute mental health problems.

The group was formed with the purchase of the Roehampton Hospital in 1980 by an American company and grew by acquisition of other hospitals and care facilities. In 1993 the group added a specialist education provider and now covers care homes, special schools, acute mental provision and specialist psychiatric facilities. In 2010 The Priory Tadley Horizon School was rated "Outstanding" by Ofsted for both its specialist education and care provision.

They have been owned by ABN AMRO Bank N.V and RBS and in January 2011 were acquired by private equity firm Advent International Corporation. They employ over 5,500 people across Europe and the UK. In Q1 2011 revenue for the group was £76 million with profit at £21 million.

### The Cambian Group

The Cambian Group works mainly in the Southwest and East Midlands supporting Aspergers Syndrome, Autism and Severe Learning Difficulties. It runs seven schools and between 2008 and 2010 their Ofsted reports have all been judged outstanding. The group started in 2003 with the development of an 18-bed rehabilitation centre. In 2005 it purchased seven special schools and started Cambian Education. It has since grown to become the largest independent provider of special needs services delivering care for over 1,100 individuals, in 60 facilities, employing over 3,500 staff and working with 140 public authorities.

Cambian Group is backed by the American company GI Partners that has approximately \$2 billion under management.

<sup>59</sup> Education Act 1996, S.348 (2)



Of the FOI responses we received, four LAs – Brent, Medway, Blackburn and North Lincolnshire – demonstrated a significant proportion of SEN provision being delivered by the for-profit sector. Table 2 summarises this information.

**Table 2: SEN provision by sector in Brent, Medway, Blackburn and North Lincolnshire<sup>60</sup>**

		Special Schools provision					
		Private for-profit		Private non-profit		Public	
<b>Brent</b>	2008/09	£3,463,154	21%	£1,335,563	11%	£3,655,427	68%
	2009/10	£3,885,381	26%	£2,312,269	10%	£4,114,642	64%
	2010/11	£5,276,832	31%	£2,435,530	10%	£5,839,573	59%
<b>Medway</b>	2005/06	£1,028,496	12%	£1,245,756	15%	£6,168,379	73%
	2006/07	£1,642,481	17%	£1,490,164	15%	£6,609,194	68%
	2007/08	£2,308,593	21%	£1,613,713	15%	£6,995,181	64%
	2008/09	£3,473,511	27%	£1,716,094	14%	£7,535,591	59%
	2009/10	£4,011,412	30%	£1,326,931	10%	£8,101,869	60%
	2010/11	£4,384,235	31%	£1,090,389	8%	£8,816,226	62%
<b>Blackburn</b>	2005/06	£1,322,195	19%	–	0%	£5,462,298	81%
	2006/07	£1,399,068	19%	–	0%	£5,921,158	81%
	2007/08	£1,321,299	18%	–	0%	£6,185,862	82%
	2008/09	£1,406,691	18%	–	0%	£6,223,593	82%
	2009/10	£1,684,504	23%	–	0%	£5,772,188	77%
	2010/11	£1,867,711	24%	–	0%	£5,900,239	76%
<b>North Lincs</b>	2010/11	£1,490,656	21%	£336,762	5%	£5,397,021	74%

This table shows that whilst public provision remains dominant there is clear evidence of increasing private for-profit provision in each of these areas. Between 2005/06 and 2010/11 the proportion of special school provision in Medway provided by for-profit providers increased by 326% which has resulted in an increase from 12% to 31% of overall provision. In Blackburn there has also been an increase over the same time period of 41% which is an increase from 19% to 24% of total provision.

#### Nursery and pre-school provision

Nursery and pre-school education is a sector where for-profit providers have become established to a considerable degree. This is due in large measure to the funding system that has developed around early years education, where an entitlement to 15 hours of free nursery provision for all three and four year olds as well as two year olds from less well off backgrounds has been available to claim since September 2010. This was an increase on the 12.5 hours previously available for all three and four years olds since 2004.

<sup>60</sup> Response to FOI requests (December 2011 and January 2012)

LAs have a duty to ensure that enough places are available. At a national level, pre-school support primarily provided in the form of Children's Centres, nursery classes in primary schools and nursery schools. However LAs also make arrangements with private and voluntary centres to ensure that there are enough places available to meet the demand. Research from the National Day Nursery Association found that a total of 584,200 (92%) three-year olds benefit from some free nursery provision. A lack of clear data means it is not possible to estimate with any accuracy the split between private nursery provision delivered by for-profit and not-for-profit organisations but an estimated 52% of these children receive nursery care from either a private or voluntary provider.<sup>61</sup>

Thus a mixed market of different types of pre-school providers has been allowed to evolve over the past ten years. To further encourage the development of a functioning market place, the Coalition government introduced changes in the way that funding for free places for three and four year olds is calculated. The new Early Years Single Funding Formula (EYSFF) is funded on the basis of places filled, rather than on places offered as was previously the case. This means that a nursery school's funding will be reduced if they offer places that are not filled and unpopular nurseries will not be supported to stay in business. There is also a requirement for LAs to include a deprivation supplement (similar to a pupil premium), which will encourage providers to set up in areas of most need. The deprivation supplement means that councils include an additional sum per pupils per hour often based around use of Free School Meals data and the deprivation indices of the councils involved. This ranges from 15p per pupil in Sheffield for example to £1.05 per pupil in the most deprived areas of Hertfordshire.<sup>62</sup>

It is, however, worth noting that the market continues to be regulated in a way that favours state providers. The funding formula allows for higher funding levels for state run nurseries than private provision, the former often being more expensive to run due to the requirement to have a head teacher and fully qualified teachers on their payroll. Private providers do not have this requirement and, as such, receive lower funding levels. The national average base rate paid by LAs for private nurseries was £3.51 per child per hour compared to £3.55 for voluntary settings and £3.96 for maintained settings.<sup>63</sup> For a 30 place nursery receiving public grants for those children for 15 hours a week this translates into a saving of over £10,000 a year with the private provision. Private providers are not allowed to charge any top-up for those first 15 hours of provision but can charge parents extra for any additional hours nursery care.<sup>64</sup>

The same accountability regime applies to all providers receiving state funding, with each being subject to regular Ofsted inspections. Complaints procedures are in place, and in 2009/10 Ofsted investigated around 7000 of these. The Early Years register includes all the providers operating from non-domestic premises and Ofsted does not distinguish between private (for-profit) providers and LA provision in this category. All providers are subject to the same standards for continued registration and where they fail to meet the criteria Ofsted has a range of statutory enforcement measures.

We received useful FOI responses from five LAs: Swindon, Leicester, Luton, Bristol and Middlesbrough. Table 3 summarises the information we received.

61 National Day Nurseries Association research with members, 2010. Presented at the NDNA Conference, June 2011. See NDNA website: <http://www.ndna.org.uk>

62 Children, Schools and Families Select Committee – Seventh Report: The Early Years Single Funding Formula, Should the Government proceed with the Single Funding Formula? 17 March 2010

63 National Day Nurseries Association research with members, 2010, presented at the NDNA Conference, June 2011

64 Department for Education, Code of Practice for Local Authorities on Delivery of Free Early Years Provision for 3 & 4 year olds, September 2010

**Table 3: Free nursery provision by sector in Swindon, Leicester, Luton, Bristol and Middlesbrough<sup>65</sup>**

		Free Nursery Provision					
		Private for-profit		Private non-profit		Public	
<b>Swindon</b>	2010/11	£2,266,000	41%	£1,832,000	36%	£1,572,000	23%
	2006/07	£1,605,097	18%	£553,001	6%	£10,834,819	76%
	2007/08	£1,712,226	19%	£606,979	7%	£11,648,965	74%
	2008/09	£2,671,082	21%	£789,813	6%	£10,953,584	73%
	2009/10	£2,520,484	22%	£675,201	6%	£11,224,257	72%
	2010/11	£3,068,130	22%	£815,493	6%	£11,575,153	72%
<b>Luton</b>	2005/06	£1,127,608	19%	£1,366,442	23%	£3,439,753	58%
	2006/07	£1,397,479	21%	£1,684,874	25%	£3,586,168	54%
	2007/08	£1,447,499	21%	£1,851,974	26%	£3,719,409	53%
	2008/09	£1,780,019	23%	£2,267,751	29%	£3,726,818	48%
	2009/10	£2,168,801	26%	£2,542,817	30%	£3,672,525	44%
	2010/11	£2,400,930	26%	£2,845,828	31%	£3,865,251	42%
<b>Bristol</b>	2009/10	£2,836,183	24%	£1,651,495	14%	£7,106,810	61%
	2010/11	£3,210,220	25%	£1,950,692	15%	£7,830,703	60%
<b>Middlesbrough</b>	2004/05	£185,238	84%	–	0%	£26,098	16%
	2005/06	£193,184	82%	–	0%	£39,418	18%
	2006/07	£202,990	82%	–	0%	£45,165	18%
	2007/08	£233,012	85%	–	0%	£50,154	15%
	2008/09	£296,031	85%	–	0%	£32,883	15%
	2009/10	£347,256	87%	–	0%	£98,623	13%
	2010/11	£371,067	87%	–	0%	£94,827	13%

This table shows that in all areas for-profit provision currently accounts for at least 20% of all free nursery provision. However in some areas notably Middlesbrough (with over 80% of provision since 2004/05) and Swindon (with 40% of provision last year), for-profit provision is the dominant form of provision. In Luton the spend on for-profit provision has increased by 113% since 2005/06 to a position where it accounts for 26% of total provision. It is also interesting to note that in Middlesbrough there is no independent non-profit provision at all and in Leicester it is significantly less than for-profit provision.

The debate around allowing for-profit provision within mainstream schooling would undoubtedly develop in a very different way if there was a more general appreciation of the existing involvement of for-profit providers in the PRU, special

<sup>65</sup> Response to FOI requests (December 2011 and January 2012)

schools and nurseries markets. There is a very obvious intellectual incoherence to arguing against allowing any element of profit making within the mainstream schools system when profit making companies are already successfully providing educational services to our most vulnerable children i.e. children with special needs and very young children.

### For-profit provision inside mainstream schools

So far we have examined how for-profit providers are permitted to deliver core education services outside of mainstream schools for 4–16 year olds. These are in areas where the pupils are some of our youngest and most vulnerable children. The next part of this chapter will focus on where for-profit making companies can operate in mainstream schools across the country, revealing that they too are involving the private sector, albeit in a more subtle manner.

#### School Improvement

LAs and state schools have been able to outsource school improvement programmes to private companies for a number of years. In 2007 Edmonton Council commissioned Edison Learning to manage Turin Grove school for three years. In January 2010 Priory special school in Taunton, Somerset also commissioned a private firm to run it. The Guardian noted that in both cases “the results were impressive and the schools improved.”<sup>66</sup> Such interventions have usually arisen when a particular LA has consistently failed to meet government threshold targets. Some examples of such programmes are discussed in the case studies below.

#### Cambridge Education and the London Borough of Islington

In 2000, Cambridge Education won a contract to run education services in the London Borough of Islington, following direct intervention by the Secretary of State who directed the council to outsource a failing service. The contract was initially let for seven years at a reported value of £105 million with an extension in 2007 for a further six years by mutual agreement.<sup>67</sup>

The contract set out a range of Key Performance Indicators (KPIs), which were monitored on a termly and annual basis. These KPIs include pupil performance results, both at the end of Key Stage 2 and at GCSE, plus targets related to school exclusions, school attendance, statutory duties, strategic plans and policies, and surveys and customer feedback. There is a core contract price with a sizeable percentage of total revenue based on achievement of these KPIs.

The range of support includes: professional advice and support for head teachers; pre and post Ofsted support and advice including Self Evaluation and the writing of action plans; school improvement support focussed on the quality of teaching and learning; advice on developing and evaluating the curriculum; departmental review, data analysis, action planning, lesson observations; setting up school systems, e.g. examination systems, data warehousing, tracking systems; and coaching and team teaching with Newly Qualified Teachers (NQTs) and subject teachers.

The improvements in Islington schools and attainment were acknowledged by the LA and national league tables and the intervention led to Islington being the most improved London borough.<sup>68</sup> At the beginning of the contract, Ofsted judged almost 15% of the borough’s schools as inadequate or in need of special measures. Ten years later Ofsted

66 Guardian, 28th January, 2012

67 Tobin, L. (14 December 2010). London borough set to bring education back in-house. *The Guardian*. Retrieved from <http://www.guardian.co.uk/>

68 Department for Education, School and College Performance Tables

has judged all the schools as satisfactory, with 82% judged Good or better. More than one in five schools in the borough have been rated as outstanding for overall effectiveness. Government figures published in January 2010 confirm that Islington achieved its best ever GCSE results in 2010 with 72% of Islington students gaining five or more A\*– C grades in their GCSE exams.

### **Babcock and Waltham Forest**

In another example of for-profit companies providing school improvement services, Babcock has been providing school improvement services in Waltham Forest under a four-year contract that commenced on 1 April 2008. This involved the transfer of 121 staff to Babcock.

The focus has been on innovation and integration of services and key activities have included: the reorganisation of the school improvement service; more commercial resource management; highly targeted data-driven interventions with individual students; a reorganisation of the admissions service; and IT upgrades.

In the second year of the contract (2010), and for the first time, more than half of Waltham Forest's pupils (51%) achieved five or more A\*–C GCSEs including Maths and English, up from 46% the previous year. In the first year of the new admissions service the number of appeals successfully defended on behalf of the authority (evidencing that the process had been effectively managed) increased to 94%, compared with the national average of 69%.

During the same period, savings of £1.94 million (14%) over two years were achieved in addition to the 3% per annum efficiency saving and the return of additional efficiency savings through the gain-share mechanism.

### **New Free School approaches – for-profit at arm's length**

The Coalition government's insistence that all those who apply to open a new Free School must operate on a not-for-profit basis has in actual fact not prevented some private sector innovation from emerging. The recent Free School application from the Sabres Educational Trust in Brandon, Suffolk provides a case in point. While Free Schools cannot be established by for-profit companies, their Trusts can buy in services from private companies. The Sabres Education Trust have adopted this model in their application to open the Breckland Free School, having awarded a ten-year management contract to Swedish company, Internationella Engelska Skolan, (IES). The school remains at the proposal stage, though if successful it would see IES in theory being able to run the school and take a profit from the payments it receives from the Trust. With a proven track record of running its own Free Schools in Sweden, IES would be charged with operating the school, with responsibility for everything from IT services to the hiring of teachers and shaping of the curriculum.

As highlighted above, LAs have always been able to use private companies to help run state schools, whether that be in relation to back office functions or school improvement programmes. However, should the Breckland Free School be granted permission to open, it will be going further than before in terms of allowing a profit making company to manage and control all aspects of school life, right down to the teaching in the classrooms.

The model being proposed by Breckland is more like the Charter School approach adopted in the USA, rather than the Swedish model, where private companies are actually allowed to found their own Free Schools. The limitations of the Charter approach are worth considering and will be discussed at greater length in Chapter 5.

While it is good that private providers are able to operate schools on behalf of Free Schools, there are providers who will not enter the market on these terms. More providers would be able to enter the market if they were able to start their own schools, or operate on an own-and-operate basis.

## Back-office functions

A significant proportion of the schools budget is already being spent on private providers of education support services. Precise estimates are difficult to obtain but the 2009–10 Consistent Financial Reporting (CFR) data shows primary and secondary school spending on “other professional services” was £572 million.<sup>69</sup> On the one hand this figure does not include Academies, as they are not required to submit data. On the other hand not all of the money will be spent on private providers.

Even maintained schools are free to purchase services from private or for-profit providers. The range of these services will depend on the school but will generally include legal and HR services, surveys, and the annual requirements to remain within Health and Safety legislation e.g. Portable Appliance Testing.

Very few schools have the capacity to manage all of their back-office support requirements in-house and most require external support for many essential functions, such as HR and facilities management. These services have traditionally been provided by LAs, either through in-house provision or support commissioned from the private sector. The percentage of school budgets that have been retained by a LA to spend on these services has varied depending on the council and the range of services it provides but is widely estimated to average out at 10% of the total local schools budget.<sup>70</sup> LAs channel money to schools under various formulas and ‘top slice’ some of this money for centrally provided services. Schools also buy in services from their own funds.

The development of Academies and Free Schools has changed this landscape. Being independent of LA control Academies have much more autonomy in the procurement of these services. When schools convert to Academies the intention is to give them the LA top slice back through the Local Authority Central Spend Equivalent Grant (LACSEG). This then allows the Academy to fund all services for which it is responsible and gives it a choice to continue to receive some of its services from the LA or to look elsewhere.

Private providers are recognising this opportunity, with a growing amount of back-office provision for Academies being provided by profit making companies. A good example of this growth in private sector involvement is facilities management services, such as school meals and cleaning services, which have traditionally been delivered by LAs. Other councils already outsource many other services. In September 2011 it was reported that Birmingham City Council is considering outsourcing IT services abroad. A company called Service Birmingham set up in partnership with Capita plc. in 2006 had already outsourced 17 IT support roles to India by June 2011 with the intention of transferring up to 100 jobs. Devon Council

69 Department for Education, Consistent Financial Reporting data, 2009–2010

70 Calculated from the LA annual section 251 budget statement (filed under section 251 of the Apprenticeships, Skills, Children and Learning Act 2009)

has outsourced its school meals service to Devon Norse Ltd since September 2011 and Sefton Council outsources services to Arvato Ltd in a ten year public private sector contract started in 2008 to cover such services as finance, IT and HR. The DfE provides guidance on procurement of services and there are frameworks such as “Buying Solutions” in operation to support quality and reduce risk.

Many of the larger national providers work in the schools sector including Initial plc, Mouchel Group plc and Mitie Group plc. Mitie is the biggest facilities management provider to PFI schools in the country, currently contracted to 50 schools across the UK with another 40 under construction or refurbishment. Contract size is dependent on the size of the school but as an indicator one contract is in place to maintain three Kent based schools for £40 million over 31 years.<sup>71</sup>

### School Inspections

The UK has a highly regulated education system, with Ofsted setting the framework by which schools and LAs are judged. Ofsted deploys around 440 school inspectors. These inspectors are augmented by almost 2,000 additional inspectors employed by Regional Inspection Service Providers – private companies contracted to assist in the inspection of schools – and produce reports that are checked and signed off by HMI before publication.<sup>72</sup> There are three national inspections contracts let by Ofsted, covering the North where inspections are delivered by CfBT, the Midlands where Serco provide the services, and the South where Tribal Group PLC. is the provider. Prospects now covers a £71 million contract to deliver the Early Years inspection services for the North of England and the Midlands.<sup>73</sup>

**Table 4: Contracts held by private providers for inspection services**

Provider	Contract value	Length
Tribal PLC	£75 million	Six years
Serco PLC	£53 million	Six years
CfBT	£57 million	Six Years
Prospects	£71 million	Five Years
<b>Total Contract Value</b>	<b>£256 million</b>	

### Summary

This chapter goes some way to dispelling the myth that the private sector cannot be trusted to deliver education services in England. It has already been the case for some time that private companies invest in and draw profits from our schools and are charged with educating some of our youngest and most vulnerable students. This applies specifically to alternative education provision, SEN and nursery school provision. School improvement and back offices services have been delivered by private profit making companies for a number of years. Furthermore, it would seem that some Free School proposals, if granted, would even allow for-profits to operate all aspects of school delivery, from catering to staff recruitment and teaching. Expanding the role of private sector would not be venturing into entirely new territory.

71 See Department for Education, Consistent Financial Reporting

72 Ofsted, The Annual Report of Her Majesty’s Chief Inspector of Education, Children’s Services and Skills 2009/10

73 Prospects, News: Early Years Contract, 25 February 2010

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# 5

## International Experience

This chapter will look to other countries experience with for-profit school providers, and reflect on what lessons can be learned from them. In particular it will focus on the performance of private sector schools, and their role in enabling models which operate at scale. Furthermore, it will also examine issues of accountability with respect to profit making providers.

International experience of for-profit provision and management of schools is limited, and research concerning the performance of this provision is limited.<sup>74</sup> The overwhelming majority of the research on Charter Schools and Free Schools aims to compare the performance of all non-state run schools (both private and voluntary sector) with the existing state-run schools. There is less research looking at the differences between private and voluntary sectors. In both the US and Sweden the majority of Charter Schools and Free Schools are for-profit. The most recent figures from 2008 indicate that 64% of Free Schools in Sweden, and 56% of Charter Schools in the United States, are operated by for-profit companies. So the question about whether for-profit provision can be better than existing state provision strongly overlaps with whether Free Schools and Charter Schools work overall.

### Do Charter Schools work?

Unlike Free Schools in Sweden, much greater variation exists within Charter Schools across the USA. Application procedures and accountability varies widely across the states in which they operate, as does the quality of public schooling which we can compare Charter performance against. Nonetheless, increasing evidence points towards Charter Schools out-performing their municipal counterparts in more cases than not. A 2011 review of 40 studies of Charter School achievement and scientifically collated the results, concluded that children attending charter elementary schools do better in reading and maths on average than those in traditional public schools.<sup>75</sup>

The Center for Research on Education Outcomes (CREDO) at Stanford University has certainly found this to be the case in a number of States. An assessment of 49 New York Charter Schools for example, indicated that, in Maths, 51% of these schools showed academic growth statistically larger than that which students would have achieved in regular public schools, with 33% showing no significant difference. In reading, the numbers were not as strong, but still showed that 29% outperform their local alternatives, with 59% showing no significant difference.<sup>76</sup>

Charter School performance in Indiana and Indianapolis outpaced the traditional public schools in learning gains. Looking at the distribution of school performance, 98% of the Charter Schools had similar or superior academic growth than the traditional

74 Waslander, S., C. Pater and M. van der Weide (2010), "Markets in Education: An Analytical Review of Empirical Research on Market Mechanisms in Education", *OECD Education Working Papers*, No. 52, OECD Publishing. doi: 10.1787/5km4pskmkr27-en p.59

75 Julian Betts and Y. Emily Tang, 'The Effect of Charter Schools on Student Achievement', October 2011, University of Washington

76 The Center for Research on Education Outcomes (CREDO) at Stanford University, Charter School Performance in New York, Jan 2010



public schools in reading and 100% of Charter Schools had similar or superior academic growth in math compared to traditional public schools.<sup>77</sup>

Meanwhile, roughly half of 52 Charter Schools in New Orleans that have produced enough test scores to measure are improving student performance in reading or maths at a significantly faster rate than competing traditional schools.<sup>78</sup> In New Jersey, comparative data released by the Department of Education demonstrates that the majority of charters in urban areas in 2012 outperformed other public schools in their districts on required standardized testing. 69% of the secondary Charter Schools in one district scored higher than the public school average in maths for that same area. In Newark, all but two of the nine Charter Schools outperformed the district average for maths.<sup>79</sup>

In Sweden independent groups have substantial freedom to apply to set up new Free Schools which are allowed to make distribute 100% of a schools surplus as profit if they so wish. In 2010/11, there were 741 compulsory Free Schools and 489 upper-secondary Free Schools across Sweden.<sup>80</sup> The most recent figures from 2008 indicate that 64% were operated by for-profit companies. Free Schools take various forms, from small parental cooperatives to schools with a particular educational approach or subject specialism and those which are run by large companies. Providers receive funding on a per pupil basis, which includes a capital dimension. Selection is forbidden, with schools not being permitted to charge top-up fees.

With a growth rate of 15%<sup>81</sup> a year, the USA represents the largest growth area for government funded privately provided schools in the world. During 2008–09, 95 for-profit providers managed 733 schools compared to 103 non-profit organisations who managed 609 schools.<sup>82</sup> For-profit providers, generally known as Education Management Organisations (EMOs), can be contracted to run a school (or group of schools) directly by the District Education Board or they can be contracted by a Charter Board, which has been granted a license to set up a school. 95% of schools run by EMOs are commissioned by Charter Boards. As with Swedish Free Schools, they cannot charge fees and pupil selection is forbidden.

### Allowing private provision means more independent state-funded schools

The most immediate benefit from for-profit provision comes from having more independently run, but state funded, schools than would otherwise be the case. While it is possible that the not-for-profit sector would have expanded more rapidly in the absence of for-profit provision, this may not be the case. And with for-profit providers providing the majority of independent state schools in Sweden and the US, you might think that if private provision was banned that their independent state school programmes would be half the size they currently are.

By increasing the number of good schools places faster than the voluntary sector alone can provide, choice and competition are increased, driving up quality throughout the system.

Why are for-profit groups such a large part of the US and Swedish systems? Given that it is in the interests of successful private business to grow, for-profit providers are much more likely to grow to a large scale than their non-profit counterparts who may

77 The Center for Research on Education Outcomes (CREDO) at Stanford University, Charter School Performance in Indiana, March 2011

78 The Center for Research on Education Outcomes (CREDO) at Stanford University, press release on New Orleans Charter Schools September 2011

79 State of New Jersey, Department of Education, *Living Up to Expectations Charter Schools in New Jersey Outperforming District Schools*, Jan 2011

80 The Swedish National Agency for Education [http://www.skolverket.se/2.3894/in\\_english](http://www.skolverket.se/2.3894/in_english)

81 Lewis, L. and O. de Botton (2011), "Nurturing a thousand flowers: International approaches to government funded, privately provided schools", Research report, CfBT Education Trust

82 Miron, G. et al. (2010), "Schools without diversity: Education Management Organizations, Charter Schools, and the Demographic Stratification of the American School system", Boulder and Tempe: Education and the Public Interest Center & Education Policy Research Unit

be more content to run one good school in their local area. Private sector firms also have an incentive to grow reasonably sized chains or federations of schools so that they can take advantage of economies of scale and expertise. Anders Hultin, one of the architects of the Swedish system talked about the incentives of for-profit providers in an article in the *Spectator*:

### Profit is the key to success in ‘Swedish schools’<sup>83</sup>

The Swedish model that gets so much international attention today would not exist without the acceptance of profit making organisations. It is a simple matter of incentives. Why should an enterprising teacher set up on their own, and make a career out of innovating in education, when that could mean financial ruin? The solution to these problems is profit. Not a vast profit; some schools make no profit at all. But they behave like businesses, treating parents as customers — and this is what counts.

Take, for example, Carlsson school in Stockholm: an excellent institution, but one run as a not-for-profit charitable trust. Because it lacks proper incentives to expand, it deals with surplus demand by asking parents to form a queue. And it is a very long queue. Parents who are considering Carlsson for their child must send in an application when their child is born. Many miss the cut. And thanks to the school’s strict first-come-first-served policy, along with the academic calendar, many of those children who do make it are benefiting from the time of year in which they were born. It is best to have a birthday between January and April if you want to get into Carlsson.

If Carlsson School was run by a profit making organisation, its natural response to the waiting list would be to expand, not become more selective. Nor would it show off about the length of its waiting list. Instead, Carlsson School would be not one school, it would be an entire group of Carlsson Schools. That is how all successful businesses work. It is how Kunskapsskolan, the school chain which I founded after I left government, works. Profit-seeking schools respond to greater demand with extra supply: this is in the best interests of children, parents and society.

While Free Schools in Sweden failed to grow at any rapid pace in the years immediately after their introduction in the early 1990s, the number of new schools increased rapidly – by 71% – between 2003–2008, despite the fact that overall student numbers in the country fell during the same period.<sup>84</sup> With 2/3 of Free Schools operating under a for-profit model, this demonstrates the willingness of for-profit providers to create scale and choice even in a shrinking marketplace.<sup>85</sup>

A profit motive provides the incentive to overcome risks associated with expansion, allowing providers to expand into new, often deprived, areas where the demand for new good schools is greater. Sweden does not have a national pupil premium type payment for pupils from lower socio-economic groups. Thus it cannot be maintained that for-profit providers are merely motivated by the availability of extra money in more deprived areas. Rather, for-profit providers seek to expand into such areas because they perceive a gap in the market, with fewer good schools in those areas than elsewhere. By contrast, it could be argued that non-profit providers have less incentive to operate outside their comfort zone. Both Anders Hultin, advisor to the Swedish government in the initial years of its Free Schools policy, and Mikael Sandstrom, current State Secretary in the Swedish Prime Minister’s office and co-author of a study into Free Schools in 2002, pick upon this as an important

<sup>83</sup> Extract from *Spectator* article, September 2009

<sup>84</sup> Waslander, S., C. Pater and M. van der Weide (2010), “Markets in Education: An Analytical Review of Empirical Research on Market Mechanisms in Education”, *OECD Education Working Papers*, No. 52, OECD Publishing. doi: 10.1787/5km4pskmlkr27-en p.59

<sup>85</sup> The Swedish National Agency for Education [http://www.skolverket.se/2.3894/in\\_english](http://www.skolverket.se/2.3894/in_english)

point. Hultin maintains that a reliance on the not-for-profit sector alone would not have delivered the necessary scale to allow a sustainable Free School sector to flourish in Sweden.<sup>86</sup> Sandstrom concurs, arguing that state and non-profit providers in Sweden do not have the same motivation to grow.<sup>87</sup> The idealism and drive of those running non-profit schools does not serve as a motive for many people otherwise perfectly capable of setting up a school to meet market demand.<sup>88</sup> There are limits to voluntarism alone.

### Case study: Kunskapsskolan<sup>89</sup>

Kunskapsskolan was established in 1999 and runs 32 schools in Sweden making it the largest Free School provider in the country. They have a very individual identity founded on encouraging a student-centered approach to learning, where students typically work by themselves with support from teachers in forming their own educational plans and weekly timetables to suit their own individual needs, they provide an alternative to traditional teacher-led schooling. Internal surveys show that 84% of children enjoy attending school, and 83% of the adults are satisfied with their child's learning.

A central team fulfills all the back-office functions that drive economies of scale across the group of schools. KKS will generally start a school with a 10/15 year contract which will require a substantial upfront investment from the company resulting in negative return for the first few years. They prefer not to put investment into bricks and mortar as they view their intellectual property as their principle product, so Kunskapsskolan will usually make an arrangement with a landlord who will convert a building which they will then lease for the 10/15 year contract. A key area of cost saving for Kunskapsskolan is that they utilize buildings where it is possible to use up to 2/3 less space than a traditional school setting. Through this and general efficiencies their business model requires around a minimum of 20 schools in order to generate an operating margin of 5%.

Andrew Coulson, Director of Educational Freedom at the Cato Institute in Washington, has analysed Charter Schools business models in the USA and agrees that a profit motive is more likely to generate expansion. Coulson maintains that for-profit businesses in competitive markets should have an incentive to specialise and to differentiate themselves from their competitors. One of the easiest ways to do this is to identify audiences underserved by existing providers, and to cater specifically to them. Coulson points out that the segment of the population most often underserved by traditional state school systems around the world is the poor, and hence finding better ways to serve low income families may be relatively easier – and relatively more commercially viable – than serving middle and upper income families who are more likely to already enjoy adequate services from the existing providers.

The experience of the for-profit US provider Edison Learning Ltd would seem to bear this out. As the company has grown, it has expanded into lower socio economic areas. The percentage of Edison students from low-income families grew from 57% in 1998–99 to 78% in 2003–04. In 2003–04 African American children made up 66% of Edison pupils, Hispanic 19% and only 13% were Caucasian.<sup>90</sup>

86 Curtis, P. (2 October 2009), Swedish Free Schools creator rejects 'flawed' Tory version. *The Guardian*. Retrieved from <http://www.guardian.co.uk/>

87 Bergström, F. and F. M. Sandström (2002), "School Choice Works! The Case of Sweden", *School Choice Issues in Thought*. Indianapolis: Milton & Rose D. Friedman Foundation

88 Sahlgren, G. H. (December 2010), "Schooling for Money: Swedish Education Reform and the Role of the Profit Motive", *IEA Discussion Paper*, No. 33. p.21

89 See New Schools Network website: <http://newschoolsnetwork.org/assets/files/Kunskapsskolan.pdf>

90 Wilson, S. F. (2006). *Learning on the Job*, Harvard, p.104

### Case study: Edison Education

Edison is the oldest EMO in the USA, opening its first four schools in 1995 having spent three years developing their school design. It has since become one of the USA's largest Charter School management organisations and was running more than 3,600 schools by 2006.<sup>91</sup>

The company sought contracts with school districts, charter authorising agencies and charter holders to manage new and existing schools. Edison receives per pupil funding from local districts but *“invests its capital up front on all new instructional materials, technology and training to give the school a fresh start”*.<sup>92</sup> Edison Education operates on a 5% margin.

### Replicating effective models

A key problem confronting education systems around the world lies not in a lack of the right ideas or models of delivery but rather in the inability to replicate these approaches. Providers driven by a profit motive are not just more likely to expand and create a chain of schools in order to create efficiencies but are also more inclined to facilitate the spread of best practice.<sup>93</sup>

In the USA, non-profit providers have struggled with scale. One study showed that to date, many non-profit providers in the US have had difficulty meeting their original growth targets, and many are struggling to create the necessary economies of scale to sustain their central offices without heavy reliance on philanthropy. The study's survey reveals that the average non-profit provider relies on philanthropy for approximately 13% of its total operating revenues.<sup>94</sup> Research undertaken in Arizona demonstrates that for-profit provision can operate on a more sustainable basis. Its findings demonstrated that for-profit organisations operating as a chain are likely to generate efficiencies by pooling together resources, research and development, best practice and information processing.<sup>95</sup> In the case of Edison, they translate their principles to all elements within the schools, with incentives reinforcing this. Longitudinal case studies of 25 Edison schools indicate that schools which succeeded in sufficiently implementing all of the Edison principles also show the highest level of student performance.<sup>96</sup> This can also lead to increased value for money. A survey on Charter Schools in Arizona, Michigan, Pennsylvania and the District of Columbia found that for-profit providers achieve economies of scale within chains and that these are often twice of those operated by non-profits.<sup>97</sup> They achieve this partly through centralised support services and administration and the increased benefit (due to the increased number of schools) of standardised teaching methods, practices and materials.

### Expansion at its best – the Swedish vs the American model

One key feature sets the USA and Sweden apart when it comes to the role of profit making companies running state schools. The USA adopts a charter model, whereby profit making Education Management Organisations (EMOs) can only be contracted to run a school by a non-profit organisation, a Charter Board. EMOs are not able to initiate the set up of schools themselves but rather must react to opportunities as they arise. The same constraints do not apply in Sweden,

91 Coulson, A. J. (2011), “The Other Lottery – Are Philanthropists Backing the best Charter Schools?” Cato Institute, Policy Analysis No. 677

92 Marsh, J., L. Hamilton and B. Gill. (2008). “Assistance and Accountability in Externally Managed Schools: The Case of Edison Schools, Inc.” *Mathematica Policy Research* (Chubb, 2004 p.488)

93 Coulson, A. J. (2011), “The Other Lottery – Are Philanthropists Backing the best Charter Schools?” Cato Institute, Policy Analysis No. 677

94 Centre on Reinventing Public Education, *Charter Management Organizations: Innovations, Opportunities, and Challenges – Research Brief*, June 2010

95 King, K.A. (2007), “Charter schools in Arizona: does being a for-profit institution make a difference?” *Journal of Economic Issues*, 41 (3)

96 Waslander, S., C. Pater and M. van der Weide. (2010), “Markets in Education: An Analytical Review of Empirical Research on Market Mechanisms in Education”, *OECD Education Working Papers*, No. 52, OECD Publishing, Marsh et al., 2008

97 Guilbert C., et al. (2002), “Education Management Organizations: Growing a For-profit Education Industry with Choice, Competition, and Innovation”

where for-profit companies can directly make an application to set up a new Free School, thereby creating their own opportunities for expansion. Given that the Breckland Free School in Suffolk – discussed in Chapter 4 – would emulate the charter approach should its application be successful, this distinction between the Swedish and American model is worth consideration, particularly since it has a direct impact on the how scale can be achieved without quality being jeopardised.

Given that they must be established on a non-profit basis, Charter Boards in the USA are usually heavily dependent on individual philanthropists or local institutions such as universities to partner with them and drive forward expansion. In some instances, this approach has been highly effective. The Knowledge is Power Program (KIPP) was originally established with a gift of \$15 million from the Fisher Foundation to cover the first three years of operation. Successful outcomes have ensured that KIPP has received a further \$70 million of donations from the Foundation over the last ten years, thus indicating that successful expansion of non-profit school Charter Boards is very reliant on well judged philanthropy.

Evidence would indicate that examples such as KIPP prove the exception rather than the rule. Recent research focusing on California which has more Charter Schools than any other single state, found that there is no correlation between the level of philanthropic funding that schools receive and their performance.<sup>98</sup> As an example, out of the 68 Charter networks analysed, the one which ranked top in terms of performance, American Indian Public Charters, was only ranked 21st in terms of the amount of philanthropic funding received. By comparison, the Aspire network, which received the most funding (£36 million compared to £1.2 million donated to American Indian Public Charters) was ranked 23rd in terms of pupil achievement. Crucially therefore, a disjuncture can emerge between those investing financially in a school and those charged with running it, thereby running the risk that neither feels entirely accountable. While it is the case that Charter networks are growing, the risk lies in the fact that they are all growing – the average and poorly performing as well as the outstanding. This suggests that the philanthropic model simply lacks the scale and management to drive forward the relatively rapid expansion of outstanding Charter Schools. This is a critical weakness and an area where the Swedish model has a significant advantage. The Swedish approach is simpler and more transparent, with all potential providers, whether for-profit or not applying to the Swedish Inspectorate for permission to set up a Free School. The emphasis of the application is on financial viability, competence of the organisation and demand, with success depending wholly on the number of pupils attracted. For-profit companies such as Kunskapsskolan and IES are therefore better able to identify potential sites for new Free Schools, directly establish them and then run them as their own, rather than having to work through a trust. Thus expansion becomes a more streamlined process and accountability more transparent.<sup>99</sup>

## Performance

### Student performance

For-profit provision of schooling in both Sweden and the USA has become widespread, enjoying a large measure of political confidence. This is despite the fact that research examining the comparative performance of for-profit, not-for-profit and state provision in Sweden and the USA remains at a relatively early

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98 Coulson, A. J. (2011). "The Other Lottery – Are Philanthropists Backing the best Charter Schools?" Cato Institute, Policy Analysis No. 677

99 Evans, N. and D. Meyland (2009). *A Guide to School Choice Reforms*, Policy Exchange 2009, p.31

stage. However the frequency of such studies is increasing and those which have already been carried out give us an indication of the effect these reforms have had on the education system in each country.

There are standout examples of where the performance of schools operated by for-profit providers has proven to be better than other schools. It has recently been demonstrated that Charter Schools in Boston have managed to raise mathematics scores by more than half a standard deviation per year in middle school.<sup>100</sup> Research carried out by Peterson and Chingos in Philadelphia measured the comparative performance of non-profit providers (such as local universities) and for-profit providers (such as Edison).<sup>101</sup> The research covered 30 elementary and middle schools which were contracted out to for-profit providers and 16 of which were contracted out to non-profit providers. The performance of these schools was also measured against that of over 70 state run schools. This research found that the performance of the non-profit providers was substantially worse than that of the state schools. With regard to Maths, the research found that students were approximately 50% of a year's worth of learning worse off annually than they would have been in a state run school. For reading ability, the figure was 32% of a year's worth of learning worse off.

The findings for schools run by profit making organisations were much more positive with students approximately 60% of a year's worth of maths learning better off and 36% of a year's worth of reading learning better off than in a state school. Students attending independent schools under for-profit management were thus found to be a year's worth of maths learning better off than their non-profit counterparts every year.<sup>102</sup> Although this research is limited to one educational subject area, the results clearly show the potential positive impact of a model which allows an element of profit. Permitting profit making providers to fully operate schools can therefore have a powerful positive impact on educational outcomes.

Other research has indicated that in the vast majority of instances, for-profit provision makes no material difference, either positively or negatively, to school performance. Research by Sass found that Charter Schools in Florida managed by for-profit firms performed the same as regards student achievement as charters operated by non-profit entities, though competition from Charter Schools in general was found to induce an increase in maths test scores in nearby state schools.<sup>103</sup> Research undertaken by Hill and Welsch compared Charter Schools operated by for-profit and non-profit providers in Michigan over a four year period (between 2002 and 2005).<sup>104</sup> The model was controlled for student and district characteristics and the results concluded that the type of ownership of a school (profit or non-profit) does not affect the delivery of education services in either a positive or negative way.<sup>105</sup> In an earlier study on some of the first Edison schools in Michigan, Miron and Nelson found similar test score patterns in Edison schools and state public schools matched on similar characteristics.<sup>106</sup> Some Charter Schools have been forced to close due to poor academic performance, though recent research indicates that of the 15% of Charter Schools which have been forced to close since 1992, only 18% of these were as a result of such failure. This equates to around 3% of overall Charter Schools opened in the USA over the past two decades. The vast majority of closures were attributed to financial and operational mismanagement.<sup>107</sup> Failures of this kind must not be overlooked particularly given the recent failure in the UK of Southern Cross,

100 Abdulkadiroglu, A., J. D. Angrist, S. M. Dynarski, T. J. Kane and P. A. Pathak (2011), 'Accountability and Flexibility in Public Schools: Evidence from Boston's Charters and Pilots', *Quarterly Journal of Economics*, 126(2)

101 Peterson, P. E. and M. M. Chingos (2009), 'Impact of for-profit and non-profit management on student achievement: The Philadelphia Intervention, 2002–08', *Program on Education Policy and Governance Working Papers Series PEPG 09–02*

102 Waslander, S., C. Pater and M. van der Weide (2010), 'Markets in Education: An Analytical Review of Empirical Research on Market Mechanisms in Education', *OECD Education Working Papers*, No. 52, OECD Publishing

103 Sass, T. R. (2006), 'Charter schools and student achievement in Florida.' *Education Finance and Policy*

104 Hill, C.D. and D.M. Welsch (2009), 'For-profit versus not-for-profit charter schools: an examination of Michigan student test scores.' *Education Economics*, Vol. 17

105 Miron G. and C. Nelson (2002), *What's Public About Charter Schools*. Thousand Oaks, CA: Corwin Press.

106 Miron, G. and B. Applegate (2000), 'An Evaluation of Student Achievement in Edison Schools Opened in 1995 and 1996.' Kalamazoo, MI: The Evaluation Center, Western Michigan University

107 Consoletti, A., *The State of Charter Schools What We Know – and What We Do Not – About Performance and Accountability*, The Centre for Education Reform, December 2011

which put essential elderly care services at risk and sparked a national debate on the appropriateness of private provision of such services.

Evidence from Sweden also indicates that for-profit Free Schools have neither a dramatic advantage nor disadvantage in terms of on performance when compared to not-for-profits, though both out-performed municipal schools. Research undertaken by the Institute of Economic Affairs (IEA) in 2010 focused on Sweden and assessed the comparative performance of municipal schools, non-profit Free Schools and for-profit Free Schools.<sup>108</sup> The research, which took a number of variables into consideration including estimates of parental education levels and income, showed that both profit and non-profit Free Schools outperformed municipal schools by around 6 Grade Point Average points. Interestingly, the findings indicated that the for-profit providers have a bigger beneficial impact on lower socio-economic groups with average GPA scores increasing by 11.6 compared to only 4.4 in non-profit Free Schools. Overall, the research concluded that for-profit and not-for-profit providers had similar positive effects with for-profit raising GPA by 5.6 compared to 6.2 for non-profit, i.e. allowing some element of profit making does not have a detrimental effect on students.

In a later follow-up study utilising more sophisticated statistical methods Sahlgren found that the influence of both for-profit and non-profit Free Schools was found to be much stronger, increasing the GPA by 33.74 and 33.86 points respectively and representing an increase of 16.3% in comparison with municipal schools.<sup>109</sup>

### Staff Performance

The introduction of the profit motive as a guiding concern naturally entails a greater focus by providers on organisational performance and the monitoring of inputs, specifically staff inputs. In addition to any regulatory framework and sanctions regime there is evidence of private profit making companies striving to hold their staff to account internally, a process which requires some flexibility if staff are underperforming. Edison has its own star rating system for its schools, which determines whether or not an individual school is performing adequately.<sup>110</sup> The system is intended to be “an objective measure from which [Edison] can celebrate success or set targets for improvement” and covers:

- Operational excellence – teacher turnover, pupil attendance etc
- Customer satisfaction
- School design – measures the implementation of Edison’s fundamentals
- Financial management – fiscal health of school
- Student achievement<sup>111</sup>

Schools are awarded a one to four star rating for each of these areas, the intention being that these internal checks give prior warning of any problems before they lead to a drop in school performance.<sup>112</sup>

A key aspect of Edison’s operational authority is flexibility over staffing and high expectations are set, for head teachers in particular. On at least one occasion Edison have set a target of removing or improving the bottom quartile of headteachers and followed through by removing 80% of the worst performing quartile group. The for-profit motive also encourages greater flexibility on pay and promotion, with a career ladder which allows teachers to advance to greater

108 Sahlgren, G. H. (December 2010), “Schooling for Money: Swedish Education Reform and the Role of the Profit Motive”. IEA Discussion Paper, No. 33

109 The follow-up study employed Instrumental-Variable techniques in an attempt to account for potential endogeneity in the original study: see Croft. (2010), “Profit making Free Schools: Unlocking the potential of England’s Proprietorial Schools Sector”. Adam Smith Institute

110 Marsh, J., L. Hamilton and B. Gill. (2008), “Assistance and Accountability in Externally Managed Schools: The Case of Edison Schools, Inc.” *Mathematica Policy Research*

111 Gill, B., et al. (2005), *Inspiration, Perspiration and Time: Operations and Achievement in Edison Schools*, Rand Education

112 Marsh, J., L. Hamilton and B. Gill. (2008), “Assistance and Accountability in Externally Managed Schools: The Case of Edison Schools, Inc.” *Mathematica Policy Research*

levels of responsibility and remuneration in shorter periods of time than is the case in state schools.<sup>113</sup> Many EMOs including Edison and Advantage Education Ltd, also offer front line staff an equity share in the company, which brings with it many advantages in terms of commitment and motivation.<sup>114</sup> The possibilities of encompassing employee ownership with a social enterprise model will be discussed at greater length in the next chapter.

## Summary

The number of quality international studies of for-profit provision of schools is limited, though increasing. Of those which do exist and focus on Sweden and the USA we can detect evidence of improved performance outcomes in instances where for-profit providers are allowed to operate schools.

However, both for-profit and voluntary providers appear to be improving results relative to state run schools. The introduction of for-profits as well as voluntary providers would allow faster growth in the number of independently-run but state funded schools, and would allow failing schools to be replaced more quickly. While there are exceptions, in general not-for-profit providers have less incentive to grow to scale.

113 Marsh, J., L. Hamilton and B. Gill. (2008), "Assistance and Accountability in Externally Managed Schools: The Case of Edison Schools, Inc." *Mathematica Policy Research*

114 Sahlgren, G. H. (December 2010), "Schooling for Money: Swedish Education Reform and the Role of the Profit Motive". *IEA Discussion Paper*, No. 33.p.110



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# 6

## The Social Enterprise Model

### The next step

Addressing the challenges faced by our schools demands us to seek out more innovative solutions. This report has so far highlighted how at least some element of private investment and profit making in our state school system could enable us to do just this. The flexibility to take greater financial risk could allow private provision to help address a funding and capacity shortfall in our schools; the expertise and capability of the private sector could bring scale to the Free Schools programme, generating more good school places and driving up standards; and the innovation of private providers could provide a much needed spur to further reform on staff pay and conditions.

### Politics

However, while for-profit provision is already operating in other areas of the public sector, and many areas of education provision, there is political opposition to allowing for further for-profit provision in state schools.

But is there really a binary choice between for-profit and not-for-profit? In other public services the number of mutual and social businesses is growing. Could this model work for schools too?

### A new model for schools

As demonstrated in earlier chapters, there is much more flexibility in other areas of public service delivery than education. Providers tend to operate along a sliding scale of independent delivery models stretching from non-profit (often charitable) provision to full for-profit provision. Along this scale there are more nuanced approaches which bring together the benefits of both non-profit provision and for-profit provision. This is the essence of a “social enterprise.” Though “social enterprise” is not a legal entity in its own right, the term is generally recognised as representative of an ethical and socially focused approach to running a business. As defined by the Business Link, social enterprises have “*primarily social objectives with surpluses principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners.*”<sup>115</sup>

This study is primarily interested in the distribution of profit/surplus which a Free School operator might make on an annual basis. Hence we will present a range of defined models which move along the profit scale from the totally non-profit charity model, through examples of a social enterprise model which allow limited distributable profit, to the completely for-profit private company.

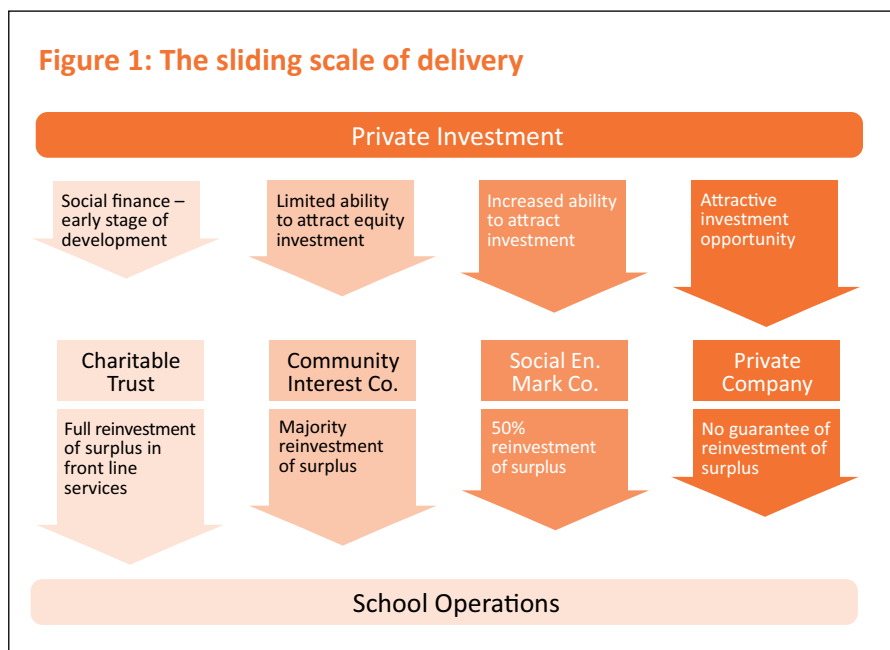
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115 Definition taken from the Business Link website guidance on how to set up a social enterprise

In each instance we will identify how the models match up to a set of seven key principles which we present as the building blocks of a new approach to delivering schools. The seven principles are:

- Financial transparency
- A duty to reinvest all or all or a portion of surplus
- Financial freedom: Ability to pay a portion of any surplus as a return to shareholders
- Asset lock on publicly procured buildings and facilities
- Financial freedom: Debt financing possible
- Potential for greater flexibility on staff terms and conditions
- Employee ability to give staff a share of ownership

The diagram below demonstrates where these models sit along a sliding scale between non-profit and purely for-profit delivery. Having presented the various features inherent to these models we will analyse them and demonstrate why a variant of social enterprise provides us with the best way forward.



The diagram above demonstrates that as the level of external investment increases, the requirement to allow a return to investors also increases and the commitment to reinvest surpluses in the front line decreases.

The key features of each model along the sliding scale are described below.

### 1. Charity (limited by guarantee)

Charities are non-profit making with 100% of any surplus being reinvested to further the organisation's purposes. The Charities Act 2006 requires all charities to have aims which are demonstrably for the public benefit. There are a number of advantages to being a charity, including tax breaks on gifts given, corporation tax, stamp duty, VAT, Rates and capital gains tax. Charities can borrow and take on debt and receive donations but they are not an appropriate model for attracting

external equity investment as there is no way of extracting a return. Consequently, as indicated in Chapter 5 they can easily become reliant on philanthropy and donations to fund their operations and/or expand.

Beyond state schooling, the charitable sector in the UK currently plays a significant role in the provision of schools. This is borne out by the wide range of individual independent schools or Federations registered as charities, such as the Girls Day School Trust. Under current UK legislation, Free Schools must be governed by a Trust which is registered as a charity.

## 2. Community Interest Company

Community Interest Companies (CIC) are the only recognised legal form of social enterprise. They are limited companies created for the use of people who want to run their organisation for community benefit and not purely for private advantage. New CICs are approved by the CIC Regulator who also has a continuing monitoring and enforcement role.<sup>116</sup>

The “Asset Lock” is a fundamental feature of a CIC which ensures that the assets of the CIC are used for the benefit of the community. Application of this “lock” in this context would ensure that Free School buildings which had been procured by government could not be sold off by a for-profit operator for private gain. An exception to this principle could be made in those instances where the providers is prepared to invest their own capital to build a new school from scratch, as is sometimes the case with EMOs in the USA. In these circumstances it would be unrealistic to expect the provider to accept an asset lock, which might endure if they lost the contract to run the school. There is also a cap on distributable profits/surplus. This is currently set at 35%. This cap is reinforced by a maximum dividend per share. Between 1st July 2005 and 6th April 2010 the limit was 5% above the bank of England base rate of the value of a share. To allow CICs to attract additional investment, the maximum dividend was raised to 20% of paid up value for shares issued after 6th April 2011.

The CIC is a very popular delivery model in other areas of public service particularly healthcare, where often valuable public assets, such as medical equipment are transferred and as such an asset lock is required.

## 3. Social Enterprise Mark Company (limited by shares)

Whilst the CIC is the only separate legal structure for social enterprise it is not the only way a company can be recognised as a social enterprise. Adherence to a slightly less stringent set of conditions allows a limited company to receive a Social Enterprise Mark. Such companies must demonstrate they have social and/or environmental aims as well as having their own constitution and governing body – it cannot therefore be a department within an LA. At least 50% of company profits must be spent on socially beneficial purposes (e.g. re-investment in front line services), the remaining 50% being distributable to investors. The company must also demonstrate that social/environmental aims are being achieved, and if it ceases trading, the remaining assets must be distributed for those aims. This model is therefore less heavily regulated than the CIC model but it does allow companies with a substantial social or environmental focus to achieve recognition for this. As there is no specific legal entity for this type of social enterprise, these companies tend to be limited by guarantee or shares.

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<sup>116</sup> Community Interest Company (CIC) Regulator Guidance (May 2005)

#### 4. Private Profit Making Company (limited by shares)

These form of the vast majority of businesses in the UK, with individuals or groups holding shares in a company and any surplus generated by the company being either reinvested or distributed to the shareholders as the company board sees fit. These can be public limited companies (i.e. external investors can buy shares) or private companies limited by guarantee. They are governed by a board of directors and are required to submit accounts each year to Companies House. Unlike charities and the various types of social enterprise, no rules apply on how much surplus can be distributed to external shareholders.

There are wide range of private profit making companies which deliver front line public services and support services in the UK such as Tribal, Capita, Edison Learning, Serco and A4E.

### Comparing different models

Table 5 briefly assesses the four delivery models outlined above on eight different dimensions.

**Table 5: Comparison of different delivery models for new Free Schools**

	<b>Financial transparency</b>	<b>Duty to reinvest all or a proportion of surplus</b>	<b>Financial freedom: ability to pay a proportion of any surplus as a return to shareholders</b>	<b>Asset Lock on publicly procured buildings and facilities</b>	<b>Financial freedom: debt financing possible</b>	<b>Potential for flexibility on staff terms and conditions</b>	<b>Employee ability to give staff a share of ownership</b>
<b>Charity</b>	Yes (accounts presented to Companies House and Charities Commission)	Yes	No	Yes (on all assets)	Yes	Yes	No
<b>Community interest company</b>	Yes (accounts presented to CIC regulator)	Yes	Yes (limited to 35% of surplus plus individual limits)	Yes (on all assets)	Yes	Yes	Yes
<b>SE Mark company (limited by shares)</b>	Yes (accounts presented to Companies House)	Yes	Yes (limited to 50% of surplus)	No	Yes	Yes	Yes
<b>Private company (limited by shares)</b>	Yes (accounts presented to Companies House)	No	Yes	No	Yes	Yes	Yes

These different models would need to be adapted for the schools sector. The level of investor return which would be permitted would need careful consideration. Like the Charity model, the CIC has a universal asset lock, which would be a concern for private providers who have invested their own capital in premises, whilst the Social Enterprise Mark Company has no explicit asset lock at all.

If politicians are not prepared to embrace for-profit provision, is there a potential halfway house? We suggest that an interesting model would combine

- Social enterprise with a flexible asset lock
- 50% of any surplus to be distributed as dividend to shareholders
- Remaining 50% of any surplus would have to be reinvested in the service

Due to the substantial initial external investment that will be required, it should be permissible for 50% of any school's surplus to be extracted as a reasonable return on that initial investment. As we will explore below, it would be desirable to encourage teacher ownership, and be able to offer staff a personal financial stake in the school they work in (or in the broader provider company).

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# 7

## Accountability, Sanctions and Supporting Reforms

In a speech to Policy Exchange in June 2011 Michael Gove stressed the importance of ongoing accountability, commenting that “autonomy works best when it’s paired with sharp, smart accountability.”<sup>117</sup> It is important, to ensure as level a playing field as possible is in place for all types of providers. However, if a degree of profit making is to be acceptable in state funded schools, a more robust accountability and sanctions framework for those types of providers should be considered. Further investigation into holding social enterprise schools to greater account than other schools is therefore warranted.

It does not lie within the remit of this report to provide a detailed outline of what any impact evaluation of social enterprise schools might look like. Nonetheless, it is clear that any pilot programmes, and ultimately any social enterprise schools which are rolled out across the country, must be prepared to be subjected to a rigorous impact evaluation process from their inception. Private providers have already been shown to have the capacity to improve the learning outcomes for students, however, as highlighted in a recent World Bank/CfBT report, our knowledge base is informed by relatively few randomised control trials.<sup>118</sup> In order to close this research gap, more needs to be invested in the collation and assessment of performance outputs from schools which are operated by non-state providers of all types.

### Application and the monitoring of financial health

As far as initial school applications are concerned there is already a rigorous process in place for Free Schools and social enterprise applications could fall within this. This could easily be applied to private providers with the addition of aspects such as financial plans detailing the use of any expected surplus in terms of reinvestment and distribution to shareholders. The application process would also have to take account of commercially acceptable levels of debt and planned carry over within financial plans.

Whilst society at large finds it acceptable for a private company to fail, any disruption to the operation of a schools provider due to financial failure will have a huge impact on the pupils. This has particular significance in the aftermath of the Southern Cross social care crisis in 2011. The government would have an operational obligation as well as a political imperative to assess (and continue to assess) the financial stability of publicly funded schools. It would be politically very

117 Michael Gove’s speech to The Policy Exchange on Free Schools, 20 June 2011

118 Lewis, L.A. and H. A. Patrinos (2012), “Impact evaluation of private sector participation in education”, CfBT Education Trust

difficult to let a group of schools fail due to the financial position of their parent company. Consequently, aside from an initial assessment through the standard PQQ process, it would be reasonable to have a process in place which monitored the ongoing financial health of for-profit providers ongoing financial monitoring of social enterprise schools would be critical. Financial transparency could be ensured through the appropriate regulators e.g. Companies House and the CIC Regulator.

### **Monitor: safeguarding continuity of health services**

In 2013, Monitor, which is currently the independent regulator of Foundation Trusts, is set to become a powerful regulator of all providers of NHS care, including privately owned providers.<sup>119</sup> Its powers, which include the safeguarding of continuity of services, will particularly apply to providers who deliver state funded services. As part of this it will have powers to levy providers for contributions to a risk pool; and intervening directly in the event of failure and will have power to trigger a special administration and regime. Monitor will be able to investigate complaints of anti-competitive behaviour and to act as an arbiter.

### **Recommendation**

The Education Funding Agency, which already performs a light touch regulatory role for Academies and Free Schools, should have its remit expanded to be more in line with the health regulator, Monitor. Such a regulator would have the ability to monitor anti-competitive behaviour and would also guard against any one provider becoming too dominant and allow the risk of failure to be spread more widely. In addition, in the event that for-profit provision went beyond the social enterprise model at some future stage, the regulator could also have responsibility for an insurance scheme whereby a levy was raised from for-profit providers, contributing towards a risk pool to guard against failure.

### **Payment and performance**

To a great extent, any schools provider will be held accountable through pupils and parents exercising their choice to attend and remain at a school – if standards decline and pupils leave, revenue falls. If one school in a chain of schools operated by a single provider gets a poor record, the goodwill value of that provider in each of its schools declines. Yet a process whereby the market wholly regulates itself in this manner cannot be totally relied upon. Swedish and American for-profit and non-profit Free and Charter Schools are subject to the same regulatory framework with no special sanction applying to their performance. However, with the educational establishment in Britain showing reluctance to readily accept idea of profit making in Free Schools, social enterprise providers may have to, initially at least, accept a greater burden of proof.

Special accountability measures for for-profit providers are attractive given the cultural aversion to profit making in the schools system and the allaying of concerns that such special measures might bring. Perhaps the ultimate safeguard against any suggestion those providers were “creaming” off profit at the expense of pupils educational experience would be a financial sanction on dividends if performance drops below a certain level or if agreed contractual KPIs in terms of pupil outcomes are not met.

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<sup>119</sup> Department of Health, Equity and Excellence: Liberating the NHS, 12 July 2010

Payment by results as a method of payment within UK public services is still in its infancy but one of the most well known and pure examples is the DWP's Work programme where providers (often profit making) are paid upon getting a workless person into work and keeping them there. The payments are based on the saving the state makes from not having to pay that person out of work benefits and are made over a period of up to two years.

### Recommendation

For-profit operators of schools should be subjected to a higher degree of scrutiny than not-for-profits. The most effect means of doing this would be by some element of financial sanction based on performance being in place. The exact nature of such a payment mechanism needs further development and a range of Key Performance Indicators would have to be identified. A rule where operators of a social enterprise secondary school would receive no share of any surplus unless a certain percentage of all students achieve expected levels of progress might be a sensible starting point.

This would not affect the spending on pupils and would go some way to allaying the concerns of the schools establishment that profits could be taken at the expense of education quality.

In addition any social enterprise pilots must operate within areas of greater deprivation and ensure that enrolment initially includes at least 20% of students eligible for free school meals and hence the pupil premium.<sup>120</sup> The pupil premium in itself will be an incentive for private providers to seek to attract these students.

### Supporting reforms

Beyond a framework of sanctions and accountability there remain a number of factors which could be regarded as critical to the future success of for-profit provision in schooling and social enterprise schools in particular. It should be taken as a given, for example, that any school which receives state funding should be free at the point of delivery for all pupils and should not be allowed to charge top-up fees. Nor should academic selection be an option for any new social enterprise schools, thus safe-guarding against the potential for cherry picking on the part of private investors. Rather the standard admissions code should continue to apply.

A number of education reforms should be pursued concurrent to the running of social enterprise school pilots. While these would assist specifically in the development of such newly operated schools, they would also have a significantly positive impact on the shape of school provision across all schools, regardless of how they are run.

- **Financial freedom with regard to surplus, debt and external investment.**

Private companies, charities and various forms of social enterprise which deliver front line services in areas such as health and welfare to work have much greater flexibility over their budgets than both maintained schools and academies. Academies are restricted to a surplus carryover of 2% from their revenue budget and 10% on their capital budget and are not permitted to take on any debt. To allow social enterprise schools (and indeed this would be beneficial for any school) to build up capital and contingency

<sup>120</sup> The national average number of school children registered for free school meals and hence eligible for the pupil premium is 16.7%. Data is drawn from School Census 2011 which can be found on the DfE website



reserves there must be a much greater ability to carry over surpluses from one year to the next.

- **Ability to give staff a share of ownership.** It could be very beneficial for the school provider, staff and subsequently for the pupils if providers were able to offer staff a personal financial stake in the school they worked in (or in the broader provider company). This would fit with the mutualisation reforms in other areas of public service. Public service staff in other areas including nurses, doctors, social workers and Sure Start centre staff are all setting up social enterprises with employee ownership shares – why not teachers?

Public Service delivery organisations which are owned by front line staff are starting to become more widespread and there are some encouraging examples of early success. See the Evolve YP case study below:

#### **Employee ownership: EVOLVE YP Ltd Social Care Services**

Evolve YP is an independent social enterprise based in Staffordshire which delivers social care services for Looked After Children. The organisation was formed by staff “spinning out” of the LA in 2009, and is jointly owned by the social workers and personal advisors who deliver the services. Each of the original members of staff holds a share in the company and sits on the board. Evolve has the freedom and motivation to develop new and innovative services (which would not be possible or encouraged in a LA setting) and high staff satisfaction levels based largely on the feeling of empowerment staff enjoy through having a share in the business.

Teachers often take the lead in setting up Free Schools – of the groups that the New Schools Network has worked with who aim to open in September 2012, 31% of these were teacher groups.<sup>121</sup> The government’s open public services white paper makes clear the government’s intention to give front line staff the opportunity to own their own services. Employee ownership would bring with it the potential for greater productivity, further commitment and an increased propensity to innovate.<sup>122</sup> These are valuable attributes to have in any public service, and would be particularly valuable in a school environment. In the USA, many EMOs including Edison and Advantage, offer front line staff an equity share in the parent company.<sup>123</sup> As part of a “social enterprise” school model it would make sense to give school employees the option of holding shares in the parent company or in the school itself if it is an individual legal entity.

121 New Schools Network data

122 Employee Ownership Association, *The Employee Ownership Effect: a review of the evidence*, Matrix Evidence, March 2010

123 Wilson, S., (2006), *Learning on the Job: When Business Takes on Public Schools*, Harvard University Press, p. 110

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## Conclusion

In September 2011, Deputy Prime Minister Nick Clegg delivered a speech firmly ruling out the Coalition government giving sanction to free schools making a profit: “Yes to greater diversity; yes to more choice for parents. But no to running schools for a profit, not in our state-funded education sector.”

However, private companies have been delivering education to some of the youngest and most vulnerable children for years. Local authorities pay considerable sums to private companies each year to provide nursery care. The private sector provides alternative provision like Pupil Referral Units and special educational needs provision. Companies are also providing “school improvement services”, which make it their job to turn around failing schools. Profit making firms already manage school facilities and operate their IT systems. We already have lots of profit making companies operating in the state education sector. So it is not clear why there should be any ‘in-principle’ objection to them running schools.

Nor is there a simple binary choice between not-for-profit and pure for-profit providers. This report advocates the roll-out of a series of social enterprise schools which could be owned and run by teachers.

With fiscal restraint set to limit state education spending for the foreseeable future, the report argues that private investment could be harnessed and put to greater effect providing excellent schools and delivering exceptional teaching within them.

Education reform over the past two decades, and more notably during the past two years, has seen the emergence of a limited schools market place, characterised by increasing school autonomy, enabling more choice for pupils and parents. However, with public opinion still wary of the private sector being involved in 4–16 mainstream education, the current government has been reluctant to embrace the role which for-profit companies could play in the development and running of our schools.

Ironically, however, private companies have been delivering education to some of the youngest and most vulnerable children for years. Local authorities pay considerable sums to private companies each year to provide nursery care. The private sector provides alternative provision like pupil referral units and special educational needs provision. Companies are also providing ‘school improvement services’, which make it their job to turn around failing schools. Profit making firms already manage school facilities and operate their IT systems. We already have lots of profit making companies operating in the state education sector. So it is not clear why there should be any ‘in-principle’ objection to them running schools.

This report demonstrates that failure to take further reforming steps in the direction of for-profit would be a missed opportunity. It argues that this policy debate need not be a simple binary choice between not-for-profit and pure for-profit providers. Rather, it contends that the roll-out of a series of social enterprise schools which could be owned and run by teachers provides a progressive step forward. Such a model would allow some element of distributable profit, enabling external investment, whilst ensuring a minimum level of reinvestment. Though not in itself a panacea to solving all the problems faced in our classrooms, if properly managed social enterprise schools hold the potential to play an important role alongside the public and voluntary sectors in meeting the challenges facing education in England today.

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