



**GOVERNMENT
OUTCOMES
LAB**

NOTES FROM THE SESSION

Emergency Responses and Government
Outcomes peer learning group
Session I. COVID-19 and Outcomes Contracts

Wednesday 08th April 2020
15.30 - 17.00pm BST



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This session of the ERGO peer learning group will explore the implications of the current situation for those running outcomes contracts, focusing in particular on where and on what dimensions outcomes contracts are able to flex and adapt to the realities of the pandemic.

This online session will bring together legal experts and other practitioners to talk through the strengths and limitations of outcomes contracts in today's emergency context.

After this session, notes summarizing the conversation will be shared with participants. GO Lab will also endeavour to circulate these notes amongst relevant decision-makers in governments the world over. Any policy briefs or memoranda which stem from ERGO conversations will be shared with participants.

The focus of the session will be changes in projects that address complex social problems and primarily those based on outcomes, such as impact bonds. We are asking each speaker to address three questions:

1. What is guiding our responses - contract terms, laws & government emergency policies, or relationships?
2. What are our responses - pause, keep walking, run, new moves - in the immediate (emergency) term or short term (recovery)?
3. Do you see any promising practices emerging? Or, what is the one thing you want everyone to avoid, do, or know?

Agenda

15.30 Welcome

Clare FitzGerald, Research Fellow, Government Outcomes Lab

15:35 Comments from a UK central and local government outcome payer perspective:

James Magowan, Government Inclusive Unit, UK Department for Digital, Culture, Media and Sport

- In line with advice from the Cabinet Office we are relaxing payment terms for projects within the Life Chances Fund (LCF). This is in recognition of the fact that the outcomes as specified prior to COVID-19 may no longer be achievable. This is likely particularly the case where support services can no longer be delivered face-to-face.
 - LCF projects have received notice that over the next 6 months, they can elect to work on a fee-for-activity basis. This may be extended to 12 months. We are the minority funder here however, so this decision will also depend on local authority commissioners.
 - Our approach is to keep services in place as we can but we must acknowledge some projects will need to pause. Where this is the case, we will ensure that the money allocated to the project will stay in place.
- The organizations we support are working hard to ensure that vulnerable people are supported despite the current circumstances. They have moved to virtual contact swiftly and thinking behind adding additional support has begun. These and other adaptations may need to be in place in the longer term as well given that a return to normalcy is unlikely for some time.

15:45 Comments from UK provider, investor, and/or fund manager perspective:

Daniella Jammes, Freshfields

- A force majeure event excuses a provider from performing under a contract because the circumstances prevent them from doing so. In this situation, that provider might

also forgo payment. In an outcomes-contract, and in light of COVID-19, this is not a helpful conversation chiefly because these contracts are designed to deliver outcomes rather than specify services.

- Clearly, the rationale behind central government guidance is that we should be looking to change the services in order to continue providing support to vulnerable populations.
 - Outcomes contracts are uniquely positioned to do just this given that they tend to be less specific about service details meaning you can change services without changing the contract.
- Force majeure clauses usually only cover the period where the force majeure is occurring. Outcomes contracts are someone unique and vulnerable in the sense that inputs today give rise to outcomes tomorrow. Covering funding for 3 months is helpful, but what happens later on? Online services are great, but it is likely that these may be less effective. What this means for outcomes payments down the line - 6 months or 3 years - this is hard to know right now. COVID-19 will change the world and it will touch the most vulnerable, these contracts will need to be revisited.
- What has been most useful is not the contract here, it has been the relationships. Still, we must consider projects individually:
 - In a given project, is there a way that services can continue? how must they adapt?
 - Is there continuity of funding? Great to have the support from central government, but this is not something that all funders are taking up.
 - If the project must pause, there are existing termination clauses in the contract which can be used to cut costs.

David Hunter, *Bates Wells Braithwaite*

- Looking at the Central Government Guidance in the PPN02, the PbR element of this is probably the least helpful part as it is unclear whether the recommendation of looking to the last 3 months as a guide to determining future payments is a suggestion or an absolute.
 - There is not typical period in these contracts. if you look at the payment profiles in an outcomes contract, these are not linear. It can be slightly random as to what the payments have looked like over the past 3 months.
- A hierarchy as naturally evolved whereby people have started shaping their approaches by first looking at the contract and then government guidance, tailoring this to their particular project by leveraging their relationships.
 - The relevant parties should agree what is relevant rather than sticking to the letter of things. Talking is key right now as is shedding a zero-sum mentality.
 - It is helpful that both the contract and the relationships coalesce around a common aim - there is an objective that commissioner, provider, and investor are all aligned with. This should make it easier for flexibility to be employed.
 - Hopeful that the reliance on flexibilities and relationships at this time can give way to a new and better way of working together after the immediate threat has subsided.
- The force majeure provisions in these contracts were not envisioned to be used. Whether or not COVID-19 counts as one is an issue we can park. If you are in a situation where you are unable to deliver the outcomes, you have other tools at your disposal - extending the contract, revisiting the balance of risk related to shortening contracts.

Julian Blake, *Stone King*

- We are talking about partnerships and collaboration here. These contracts are of a complex nature and what matters is how they are practically implemented rather than what shape their legal form takes.
- The emergency hasn't really created new things, it has put the focus on existing issues in an extreme way. Coming out of the crisis, we should be saying what these issues are, how they are being addressed in the moment, and how change needs to happen - capturing, consolidating and entrenching the need for change after the crisis.
 - We now know that low-skilled workers are key workers, the state can fund by reference to actual need, and the market mechanisms in public services don't work without proper regulation.
 - We must look at purpose over process, interpretation over literalness, creativity over risk-aversion, practical over technical, relational over transactional, and focus on partnerships rather than legal demands - collaboration towards the common purpose of providers and funders.
- The decades long shortcomings of public service contracts are being laid bare. Contract terms which relate to flexibility and working relationships are underdeveloped.
 - Fund organizations not in arrears
 - Revisit pricing (using the tools of open book accounting), short-termism, unilateral rights to vary.
 - Social value is not ancillary or additional, it is central to public service contracts.
 - We are seeing in real time what it means and what the requirements are with this emergency and it should be in deference to the social value standard.
- By doing the above, we get longer relationships, building public services over time with locally embedded providers

16:05 Comments from international development & impact finance perspective:

Ranajoy Basu, *McDermott, Will & Emery*

- We must examine the definition of force majeure. Outcomes contracts are meant to keep the deal together rather than dismantle or restructure the project. Force majeure is slightly broader in these outcomes contracts than in typical contracts because it looks to understand how an event could impact three interconnected things: cash flows, implementation and measurement.
 - It is important to understand who is the effected party in the force majeure event as you can have an event which impacts implementation but not cash flows. The important thing is that when you have an effected party, this triggers governance mechanisms to keep the deal together.
- We need (and are working on) a model force majeure clause with governance mechanisms aligned based on some misalignments we have observed:
 - Real difference in deliberation times between English law governed vs US contracts where the US provides longer durations.
 - In cross-border DIBs with aggregation of capital you have a number of contracts and funders behind an outcomes provider or risk investors. There are force majeure provisions at the outcome payor level, investor level, service provider level, but also on the back-to-back side.
 - From a financial perspective, you could have funders coming in operating in misalignment with what your actual impact bond stipulates. We are having conversations about how we hold everyone together in the meantime - now is not the time to talk about termination or restructuring.

- In blended funding arrangements - with grants and private sector capital - there is a tension where the private sector is looking to terminate or change more quickly.

16:20 Brief observations from legal scholars

Abby Semple

- I agree with the emphasis on focusing on relationships with existing providers, but there are unintended consequences to that including locking out new providers with long-term extensions to existing providers
- The PPNs are welcome and well-drafted, allowing for directly awarding contracts provided you publish an award notice and they are limited in time and scope in accordance with the emergency. The PPN also allows modifications of contracts.
 - People are modifying contracts - 20+/week (up from 2-3/week pre-COVID-19) - but these may go beyond what can be justified (e.g. extension of health services of 10 years; management consultancy services; PR services)
- PPN guidance on open book accounting and assurance of payment to subcontractors is salient, mindful that some subcontractors in outcomes contracts are not assured volume so may not be in line for payment.

Aris Georgopoulos, University of Nottingham

- Even at the EU level where we might see resistance on accepting flexibility of application of current rules around procurement, we see a significant change.
 - Either this is contained temporally to the crisis OR is already in existing systems.
 - We have the solutions here and all we are seeing manifested in these kinds of notices is a change in mindset in how we view rules:
 - Prior to COVID-19: rules were obstacles, what are we allowed to do?
 - Now: more interesting, how can the rules help us deal with the problem?
- Are we transitioning from transactional compliance-based interactions into relational forms? I see a change but this carries risk:
 - Opportunity of more loose application of existing rules may lead to contracting authorities moving towards creating set asides for particular providers for longer periods than the original contracts stipulated
 - This means monitoring organizations need to have a close look at awards and modifications post award
- We have looked at force majeure from the point of view from suppliers - but what about the reverse? For contracts that could be scaled back by the public authority, are there human rights implications we should be aware of?

Chris Stone, University of Oxford

- Everyone agrees that we want to keep services going, leaning on the relationships around contracts rather than being taken over by contractual assumptions. But we should not be moving to a fee-for-service basis. We should stick to outcomes by adapting those outcomes to the new circumstances. Don't retreat, adapt!
 - Analogy to Venture Capital: milestones en route to profits as basis of payments.
 - VCs with existing portfolio companies will make follow on investments - not just maintaining investments, increasing them but not making new deals
 - Be rigorous and specific about what has changed in relation to specific contracts. Don't just say - there is a crisis, outcomes won't happen so here is money - consider the case by case.

- Is the problem that the need is gone? Delayed? Or are their new demands, new outcomes we should be focussing on in the contract? What activities are critical, nice, or should be stopped?
- The danger is that we switch back to cost or performance-based contracting.
- Transparency is key - internally and externally - and re-evaluate what outcomes you should be principally pursuing.

Christopher Yukins, George Washington University

- Leadership behaviour - Trump has encouraged strategic behaviour meaning that lawyers and individuals are left to enunciate norms as these are not coming from the top.
- Force majeure in the US Federal system is quite mature, focussing more on delay than compensation. Compensation instead comes from the legislative branch.
 - Republicans agreed to the recent stimulus as a means to maintain their political power, but appropriations to contracts must come from open appropriation - it creates no new pool of money.
 - Politicians are setting the expectation of reimbursement for additional costs but no specific appropriations - creating strategic behaviour amongst agencies because they don't want project monies going to contractors for reimbursements at this time.
- A practical lesson from legal practice is that bringing in a third-party arbiter to help navigate these competing tensions across parties has been incredibly valuable

16:55 Close