

THE PROCUREMENT OF WELFARE TO WORK SERVICES IN AUSTRALIA AND THE NETHERLANDS: LEARNING FROM COMPUTER SIMULATIONS

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ABSTRACT. The paper focuses on recent developments in the Australian Job Network and the Dutch reintegration services market - the latter with a particular focus on the role of UWV in the procurement of services. The two countries share a more or less similar labor market situation with a historically low unemployment record combined with a large inactive group in a very disadvantaged labor market situation. The tailoring of welfare to work services for these groups proves to be difficult and the public procurement agencies in both countries are looking at similar problems in this respect. Both the Australian government and UWV are in the process of introducing a new purchasing framework in 2008. The analytical framework in this paper lies in a novel instrument: Pre-Tender. This is a computer simulation of a social services market. Pre-Tender allows for the testing of various procurement and contract management approaches in terms of provider responses. In this perspective the paper discusses some of the avenues that the Australian government and the UVW pursue to focus their services towards the more disadvantaged groups. The conclusions in the paper have a broader relevance than just Welfare to Work and just Australia and the Netherlands.

INTRODUCTION

Is there scope for the private market in the provision of social services? From looking around, the answer would seem affirmative. In health care, public transport, public utilities and a number of other areas

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where government used to provide services in-house, countries across the world *have* shifted or *are* shifting to private providers. This shift has not remained unchallenged, however. Experiences with private provision in a number of areas have been less positive than anticipated. Governments for example have found it difficult to contain costs, issues have been raised with respect to the access of vulnerable groups to services, problems of parking certain groups have been brought to the fore (for example welfare-to-work in Australia) and service quality occasionally appears to have deteriorated. Therefore, it makes sense to ask: *is the market also catering for the most disadvantaged groups?*

Proper procurement and contract management are crucial for success in the contracting-out of services in the social area. This paper will elaborate this for the case of welfare-to-work services and it will take Australia and the Netherlands as benchmark countries. After a brief outline of the institutional framework in both countries and the policies over the past decade (section 2), the paper continues with the introduction of a new instrument that allows for the testing of various alternative procurement mechanisms, and the results from an experiment with professional bidders (section 3). Subsequently (section 4), the paper looks ahead: how will policies in Australia and the Netherlands evolve in the near future? and in particular, and are authorities successful in gearing the market more towards the most disadvantaged groups? The final part (section 5) contains some conclusions.

INSTITUTIONAL SETUP OF WELFARE TO WORK IN AUSTRALIA AND THE NETHERLANDS

Over the past decade an increasing number of countries have shifted from in-house provision to procurement of welfare-to-work services from private providers. Australia was the first with a full scale liberalization of the market for employment services in 1997. The Public Employment Service (PES) was privatized and the ground was leveled for competition in a large scale public tender for contracts for the period up to mid-2000. Currently the Australian government is preparing for the fourth employment services contract (ESC4) tender which is due at the end of 2008/beginning of 2009.¹ The Netherlands followed at the end of 2001 with a similar liberalization of the reintegration services market and privatization of the PES. Unlike Australia however, tenders are not organized on a national scale and central government is not acting as the

purchaser. The benefit agencies (UWV and municipalities) are responsible for the contracting of reintegration services on the private market.

At this point it might be instructive to explain a few things with respect to the institutional framework for the delivery of social services in both countries. For this purpose, Table 1 provides an overview.

TABLE 1
Institutional Structure for Employment Services in the Netherlands and Australia

Tasks	Netherlands	Australia
basic employment services	CWI	Centrelink
client intake and referral	CWI	Centrelink
benefits	UWV/municipalities	Centrelink
procurement and contract management	UWV/municipalities	DEEWR
case management	UWV/municipalities	private providers
specialized service provision	private providers	private providers

The Centers for Work and Income (CWIs) are the public agencies that are responsible for the basic employment services and the jobseeker classification ('profiling'). There are approximately 130 CWI sites across the Netherlands. The Social Insurance Organization (UWV) administers the unemployment insurance and disability insurance schemes. Municipalities administer social assistance for those who are not eligible for one of the other schemes. Both UWV and municipalities² are responsible for the reintegration of their beneficiaries into the labor market or into some alternative social inclusion program. These organizations, therefore, act as the purchasers of reintegration services from private providers, and this deviates from the situation in Australia (and for example, Britain, Flanders and a number of other countries) where the central government procures these services. This *decentralized purchaser-provider framework* that characterizes the Dutch model raises some governance issues³ - high transaction costs, limited transparency and difficulties with contract management are among the most compelling ones.

The challenging issues in this area of welfare-to-work focus on the targeting of the disadvantaged groups, creating more scope for training and intervention – for example: medical treatment – and tailoring combinations of services to those who are facing multiple problems – that is, the people who experience combinations of: bad housing conditions, financial problems, educational and medical deficiencies, et cetera.

So far, the private market has been able to deal well with the large number of clients with none or minor deficiencies. For rendering the market approach successful from a public interest point of view, however, the more difficult categories provide the ultimate test. This is currently the main issue in both Australia and the Netherlands – two countries that currently are experiencing similar labor market conditions: a tight labor market with a large number of unfilled vacancies on the one hand, and large pockets of disadvantaged groups on the other. Both countries face the problem how to gear the market more towards those disadvantaged groups.

Before proceeding, it may be instructive to point at one specific characteristic of welfare-to-work, one that poses a challenge on the contracting-out of these services. Unlike for most other services in welfare to work it is difficult to relate an outcome to the level of effort of the service provider. Outcomes can likewise be achieved due to favorable labor market circumstances and motivated clients – that is, to some extent independent from the performance of the provider. This problem is even enlarged in the bidding stage. It is difficult for procuring agencies to select the best provider and pre-commit this provider in the contract to some high expected outcome level. Afterwards, when the contract expires and results have been disappointing the provider can always claim that external circumstances were to blame. This renders the contracting-out of welfare to work services rather peculiar and this is most prevalent in contracting-out services for difficult to place groups. Two ways to tackle this ‘credible commitment’ problem are: outcome funding and performance benchmarking. The provider that exerts less effort will be less successful, other things equal, and this will be reflected in the stream of (future) revenues. These two approaches are both used to ensure that providers exert sufficient effort to place those categories of job seekers, where marginal placement costs may exceed marginal revenues.

Developments and Current Design of the Australian Job Network: 1997 - 2008

We will restrict ourselves to describing the current design and main developments over the past decade with respect to those four scheme parameters that are in particular relevant to the topic of this paper, these are: case management, tender design, the funding formula, and performance measurement.

Case Management

Centrelink refers clients to one of the contracted private providers. This provider then is responsible for all services including the case management. In theory this would give the provider a large scope to tailor the approach to the needs of the individual clients. However, the fee structure that has become increasingly detailed over time has generated a rather uniform approach across providers (DEWR2006).

Tender Design

The role of price in the award procedure has changed over time. In the first tender (ESC1) in 1997 the price (service fee) was the main factor in the awarding of the contracts to providers. In the second tender (ESC2) in 2000 more weight was attached to past performance and the prospective approach – price competition was reduced: price was weighted for 25 percent and, finally, from 2003 onwards (ESC3) the government sets the price unilaterally. This meets the criticism that competition on the lowest reward leads to inferior placement outcomes (OECD 2001, Productivity Commission 2002). The share of business that is offered for tender also has decreased substantially. In 2003 around 60 percent of the existing contracts was rolled-over, only 40 percent was open for tender. The share of contracts that was open for competition was limited even further in 2006 when more than 80 percent of the incumbent contract volume was rolled over.

Funding

In ESC1 and ESC2 there was an up-front fee and an outcome fee. The outcome component was 67 (ESC1) to 75 percent (ESC2) of the total contract fee. In ESC3 the fee structure has been revised. There is a fee for service with a detailed structure and an outcome fee – the outcome component is around 30 percent of the contract fee. In ESC3 also a new component was introduced: the Jobseeker Account (JSA).

This is an earmarked fund. Providers can draw resources from the JSA to tailor activities or instruments to jobseekers – in particular for long-term unemployed clients.

Performance Measurement

In 2000 the Australian government introduced *Star rating* – this is a sophisticated performance benchmark. In this benchmark the *actual* outcome of a provider is assessed against the *expected* performance, where the expected performance is adjusted to take account of variations in client characteristics and local labor market conditions. Scores are distributed on a scale from 1 to 5 stars such that 70 percent of providers in a region are rated 3 stars or more (Productivity Commission 2002). The Australian government uses Star rating to allocate contracts and to refer clients to providers within contracts. Hence, the performance benchmark is an important trigger for providers to achieve outcomes.

UWV in the Netherlands: Evolution of Procurement of Reintegration Services 2001 - 2007

Like the Australian Job Network, the UWV purchasing model underwent some drastic changes in an even shorter time span.

Case Management

Before 2005, UWV purchased complete ‘trajectories’: all activities for a specific jobseeker, from the initial assessment of the job seekers to the final placement in a job, were contracted-out to the same provider. From 2005 onwards, the emphasis has shifted to a more tailored approach. This included the shift from complete trajectories to ‘modular’ purchasing and the retention of the case management role in-house (via public ‘reintegration coaches’). This implied a more central role for the clients and their reintegration coaches, whereas the role of the UWV purchasing department gradually became more like a back-office.

Tender Design

UWV has organized tenders, first on an annual basis: in 2001 and 2002, and from 2003 onwards three or four times per year for different categories of jobseekers. In the procurement of reintegration services UWV applies the open procedure. Selection and award criteria have changed over time. Table 2 gives the criteria and weighting for the 2005 tender round.

TABLE 2
Weighting of Award Criteria in UWV 2005 RFT

Criteria	Points
experience with a specific client group	150
method	150
fee	100
prospective placement outcome	50

Funding

Outcome fees are important in the contracts with private providers. For less difficult to place clients the fee is *100 per cent* outcome based, whereas for the more difficult categories a 50 percent up front and 50 percent outcome fee is common.

Performance Measurement

UWV also operates a performance benchmark. In the 2006/07 contracts UWV used the benchmark to roll over some of the contracts. This benchmark, however, is not as sophisticated as the Australian star rating benchmark. The benchmark incorporates placement scores of the various contracts but does not weigh the differences in JSC status into these placement results. In stead, separate performance benchmarks are published for each category of contracts.

Comparing the Job Network and the UWV Models

Comparing the Australian and Dutch (UWV) models, it appears that in the Australian model of contracting providers the performance benchmark has a far more crucial role than in the UWV model. The *reputation mechanism* therefore so far has been a more crucial governance instrument in Australia, whereas in the Netherlands the incentive for providers to achieve outcomes has been located primarily in the specification of the funding formula.

Another major difference is that the Netherlands allows for price competition: the service fee is set in the bidding process. In Australia, on the other hand, the government sets the service fee.

With a view to the challenge: *how to achieve outcomes for the most disadvantaged groups?*, it would be interesting to put both models to the test. Section 3 contains the preliminary results of such a test.

PRE-TENDER

Pre-Tender is a computer simulation of a market for social services, cast in a game format. It allows for the testing of procurement models during the design stage. The aim of Pre-Tender as a tool for policy makers is to facilitate a better understanding of strategic provider behavior, that is: the response from providers to alternative purchasing and contracting frameworks. This understanding enables the procuring agencies to tailor their requests for tender more specifically to their aims.

The game consists of a number of rounds. In each round the participants compete to obtain a contract. Participants are matched pair wise. This matching occurs at random. One participant of each pair obtains the contract (the other has to wait until the next round). The aim for participants in executing the contract is to make profit. The profit is a function of the achieved placement outcome, the fee for service, the effort and the costs of the effort. Apart from a profit (or loss), the outcome that is achieved earns the participants a reputation score. This reputation changes in the course of the game depending on the performance track-record of the participants. In some procurement models this reputation influences whether a contract is awarded to a specific participant. This is the case in two of the four models in Pre-Tender: the scoring auction and in the benchmark. In the latter, the contracts are awarded to the providers with the best performance ranking in the benchmark. The participants further dispose of several tools to help them in their decision making – for example a tool to calculate costs and revenues, and forecast tables. With these tools the participants can find which effort level will generate the highest profit, or the highest outcome given a certain profit target. The annex includes a few screen shots of Pre-Tender.

The model makes a distinction in two kinds of effort: placement and ‘intervention’. This distinction captures the idea of *multitasking* where one effort dimension produces outcomes that are better observable for the commissioner than the other. For example, a placement in a job is observable for the benefit organization, but the duration of the placement

(the job spell) is not known at the time when the provider receives the outcome fee. The aim in future releases of Pre-Tender is to elaborate this multitasking element further – for example, effort in *service quality* or effort that produces better outcomes in the long run (e.g. *training*) could be modeled to have an impact on the reputation in later rounds. In the current release the two effort dimensions are related to placement probabilities for different categories of jobseekers.⁴ The output is modeled as a (*marginally decreasing*) function of the effort in placement and the effort in intervention, and a function of the jobseeker category status and labor market situation as well. The latter (labor market situation) is modeled as a random variable with a mean that increases/decreases/remains constant each round in an upward/downward/neutral economic scenario.

Pre-Tender enables us to test whether the design of a procurement model or the specifications of the contract are in line with the objectives of the procuring organization. *To what extent does the design lead to the desired outcomes?* In the context of this paper for example, it would make sense to test whether the Australian and UWV contracting frames are sufficiently geared to obtain service providers that will achieve the best outcomes for disadvantaged categories. We have restricted ourselves, however, to just one aspect that is important in the two procurement models: the functioning of the reputation mechanism. We tested the Scoring Auction (SA) against the Benchmark (BM).⁵ The difference between the two mechanisms is that in SA reputation weighs for 25 percent in the awarding of the contracts and this weight remains constant during all rounds, whereas in BM the weight of reputation increases from 25 percent in round 1, to 100 percent in round 4 and onwards.

The Experiment

The experiment was conducted with professionals on April 21st 2008 at the Council for Work and Income in The Hague, Netherlands. The original plan was to have two groups of 3 participants competing in two separate clusters. The fourth competitor in each cluster or market would be pre-programmed: a ‘robot’. The idea was that this robot would perform different roles (i.e. play different strategies) in the two separate markets. In one market the robot would act like a ‘rat’ striving to maximize short-term profit, and in the other market the robot would act like a ‘pleaser’ striving for the best possible outcome for the procuring

organization. The idea was to test whether the two different strategies would have an impact on the strategies of the other participants and, eventually, the outcome for the procuring organization in one of the two mechanisms (SA or BM) more than in the other. Due to computer problems, however, the setting had to be changed into one group of three plus the robot, where each participant teamed up with a colleague to represent one provider and the robot played the ‘rat’ strategy. Given time restrictions the number of rounds in both mechanisms was limited to three.

The buildup of the two mechanisms was similar. The participants were given a case per round. Table 3 provides one example of such a case. The parameters that determine the bidding behavior and the group size are given in Table 4.

TABLE 3
Example of a Case Description

UWV is the largest purchaser of reintegration services in the Netherlands. UWV aims to contract service providers in one of its regional areas for elder jobseekers that have an employment track record in industries that have moved their operations overseas (ship yards, manufacturing industries, etc.). This group is highly motivated but faces severe problems to get back into the labor market. UWV envisages that a mix of training new skills and convincing employers that these jobseekers will be productive is required. The contract duration is 2 years.

TABLE 4
Round Parameters

Round	1	2	3
Group size	100	200	200
Placement probability	0.25	0.2	0.3
Outcome funding	0.6 (SA) 0.8 (BM)	0.6	1 (SA) 0.4 (BM)

Notes: placement probability refers to JSC status – the scale is from 0.2 (low) to 0.4 (high);

With respect to outcome funding the scale is from 1 (100 percent outcome fee) to 0 (fixed fee).

Results

Table 5 gives the main results. The placement score in BM (34.3 percent) is much higher than in SA (12.7 percent). The costs for the benefit organization per placement is a little lower in BM (€12,233) than in SA (€12,534). The total costs for the benefit organization, however, is much higher in BM than in SA. Hence, for the benefit organization there seems to be a tradeoff between the placement score and the costs of contracting.

TABLE 5
Main Results of the Experiment

	Placement score	Costs commissioner	Cost placement
Scoring Auction	12.7%	1,591,800	12,534
Benchmark	34.3%	4,195,800	12,233

A second observation relates to the average results per round. The average contract fee decreases in SA but not in BM. Table 6 illustrates this. At the same time, the placement score in SA more or less remains at its initial low level, whereas a substantial increase in the placement score can be observed in BM. It is tempting to conclude that this relates to the increased weight of *reputation* in the award formula in BM as compared to a constant weighting in SA. The other difference between the two rounds 3 was the degree of outcome funding. In SA a 100 percent outcome fee applied, whereas in BM this was 60/40 percent up-front/outcome.

TABLE 6
Breakdown of the Results per Round

		Round 1	Round 2	Round 3
Scoring Auction	Contract fee	4,500	5,250	3,250
	Placements	20	28	17
Benchmark	Contract fee	5,000	6,750	7,000
	Placements	21	56	96

The third observation relates to the individual strategies. The pre-programmed 'rat' managed to win all three rounds in SA. His strategy was to promise high levels of effort – which, in fact, he didn't deliver after the contract had been awarded to him. In BM however, with a similar bid strategy he only won a contract in the first round. After this first round his deteriorating reputation prevented him from winning any further contracts. Hence, the conclusion appears to be that SA still leaves some scope for providers who are in the market only to achieve short-term gains. These providers do not act in the public interest. In BM these providers are driven out the market after just one or two tender rounds.

The overall conclusion from the experiment is that the reputation mechanism appears to be a powerful tool in procurement design.

The design of the reputation mechanism in this experiment was still rather crude. For example, no account was given of the JSC status – that is, differences in outcomes over the various rounds that are due to differences in job seeker characteristics. The impact of the placement score in rounds 2 and 3 on the reputation therefore was similar, whereas the placement probabilities of the clients in both rounds were different. Another issue is that providers could renege on their bid with respect to effort levels. In the real world commissioners will somehow monitor provider effort levels – for example, through client satisfaction scores. Moreover, given the limited number of participants and the limited number of rounds these results are to be conceived as just an illustration of the potential of Pre-Tender as an instrument for procurement design. Despite these caveats, however, the results are challenging enough to warrant further research and in our view illustrate the added value of Pre-Tender as a procurement design tool.

NEW AVENUES: MAKING THE MARKET WORK FOR THE DISADVANTAGED JOBSEEKERS

The UWV Purchasing Framework 2008-10

UWV has revised its procurement framework in 2008. The new approach puts more emphasis on contract compliance, a more client oriented service provision and further tailoring of services to individual client needs. In the new framework UWV organizes a tender to select service providers that meet certain quality standards. These service providers will be licensed for a two year period to provide services to

UWV clients. The actual contracting will be done by the reintegration coach in close collaboration with the individual clients. Hence, the licensed service providers still will have to compete for the actual business within the general contracting framework and their reputation will be an important factor in this respect.

Open Windows in Australia

Australia also is in the process of revising its contracting framework. The new cabinet has been canvassing organizations and professionals to forward their views and this had led to a wide criticism and a number of proposals to improve the Job Network model. Criticism, among other things, points to ill targeted assistance and high dead weight losses (where the groups that receive assistance are those that would have found jobs anyway), low levels of training and an insufficiently transparent performance benchmarking system (Star rating). The government is seeking to increase service levels for disadvantaged jobseekers and improve outcomes for this group. Therefore, amending the funding mechanism and the performance benchmark – both in a direction so as to make it more rewarding to achieve outcomes for the disadvantaged clients – are priority areas in the government's reform agenda (DEEWR 2008).

CONCLUSIONS

Both UWV and the Australian government are looking at new avenues to tailor reintegration services to the more disadvantaged groups. For the Australian Job Network this would include a revision of the funding structure, including the securing of resources for training purposes, and a further improved process of allocating the contracts with the Star Rating benchmark. For UWV the main challenge lies in the reconciling of the role of the professional case manager and individual client choice on the one hand, versus principles of transparency and open competition on the other. In particular this would require the design of a more sophisticated benchmark that can be used for the referral of clients to service providers.

In this paper a central issue in both models: the functioning of the reputation mechanism in the allocation of contracts, has been tested with Pre-Tender – albeit still in a rather crude manner. Future research could test other features of both procurement models. For example the role of

the funding structure in the provision of training and other services that benefit the disadvantaged groups, or the allocation of clients to service providers in view of the balancing of risk for providers.

The design of the procurement mechanism that generates the best results for disadvantaged jobseekers is a difficult task. Both the Australian government and UWV have found themselves in a long process of piece meal engineering to get the procurement and contracting framework right. Our contention is that procuring agencies can benefit from an instrument like Pre-Tender. Pre-Tender allows for the testing of alternative procurement models, or parameters within one specific model before the actual implementation takes place. An example of the latter could be the impact of different scoring options for award criteria. In this respect, Pre-Tender could aid procurement agencies in designing the most effective framework in the most efficient manner – that is, avoiding the trial and error approach that is common in real life practice.

This paper has provided a preliminary illustration of the possibilities. Depending on the demand of the procuring organization and the characteristics of the specific service market, the model can be adapted. Therefore, Pre-Tender could be relevant for a broader area of social services procurement – for example health care, household services, occupational health and safety, education services (e.g. for immigrants), and public transport. In all these areas governments – often local level governments – find it difficult to tailor their procurement process to meet their demands. We think that computer simulation models – like Pre-Tender – can be useful in those areas as a design tool.

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NOTES

1. The third contract ESC3 – originally planned from 2003 to 2006 – was extended in 2006.

2. According to the Work and Social Assistance Act (2004), municipalities are for 100 per cent responsible for their social assistance benefit expenditure. Surpluses over the received budget may be retained but deficits need to be recovered from local tax revenues. This provides municipalities with a strong incentive to reduce (or at least: contain) their case load.
3. Tergeist and Grubb (2006) have listed the main issues. Tergeist and Grubb have labeled the Dutch municipalities market segment a two-tier quasi market.
4. The idea is that for different categories of clients with a different jobseeker classification (JSC) status the optimum placement/intervention effort mix is different. For example: more disadvantaged groups would require more training effort in addition to placement effort, whereas for less disadvantaged groups good placement outcomes are feasible with no training effort at all.
5. The Scoring Auction resembles to some extent the UWV procurement model, whereas the Benchmark has some features of the Australian model. In SA the contracts are awarded according to four criteria that have an equal 25 percent weight: promised effort on placement, promised effort on intervention, service fee and reputation. BM starts in round 1 as a Scoring Auction but reputation is weighted in round 2 for 50 percent and in round 3 for 75 percent. From round 4 onwards contracts are awarded for 100 percent on reputation.

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ANNEX Screen Shots of Pre-Tender



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[Log out](#)

Scoring Auction

<p>Round 2</p> <p>Costs per hour 94</p> <p>My reputation 7.0</p> <p>Accumulated profit 8300</p>	<p>Bid</p> <p>• UWV</p> <p>JSC (category): <i>Benefit Claimants JSC medium/difficult, Service: Intervention and Placement, Group size: 125</i></p> <p>UWV is the largest purchaser of reintegration services in the Netherlands. UWV aims to contract service providers in one of its regional areas for elder jobseekers that have an employment track record in industries that have moved their operations overseas (ship yards, mining, etc.). This group is highly motivated but faces severe problems to get back into the labor market. UWV envisages that a mix of training new skills and convincing employers that these jobseekers can be productive is required. Probably service providers have to offer some post-placement support and wage subsidies to be successful in achieving longer-term outcomes with this group. The contract duration is 2 years. UWV will offer business to 3 providers each on a 33 percent share. At the end of the period contracts of the 2 best performing providers will be rolled over.</p> <p>Fee Structure: 80% Outcome, 20% Commencement</p> <p>No. hours intervention per client: <input type="text" value="5"/></p> <p>No. hours placement services per client: <input type="text" value="10"/></p> <p>Required fee per unit outcome (placement): <input type="text" value="4500"/></p> <p style="text-align: right;"><input type="button" value="Bid"/></p>	<p>Bid Tender document</p> <p>Procedure How the contract is awarded</p> <p>My company Explanation of the level of my costs per hour</p> <p>Calculator Calculates costs and revenue</p> <p>Forecast Mid-term labour market forecast</p>
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Log out

Benchmark

Round 3

Costs per hour
62

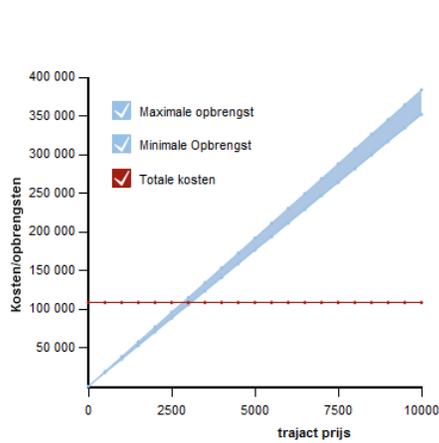
My reputation
-7.0

Accumulated profit
-128250

Calculator

With this calculator you can vary the no. hours placement and intervention and the contract fee. This will help you to determine your effort level and your bid.

Fee Structure: 40% Outcome, 60% Commencement



intervention (hours per client)
0 20

placement (hours per client)
0 40

assessment

Estimated Outcome: 18

Execute
Contract conditions

Outcome
How the outcome is calculated

My company
Explanation of the level of my costs per hour

Calculator
Calculates costs and revenue

Forecast
Mid-term labour market forecast