NON-PROFIT ORGANISATIONS IN THE HUMAN SERVICES MARKETPLACE:

THE IMPACT OF QUASI VOUCHER-LICENSING SYSTEMS

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1. Introduction

The provision of human services relies substantially on government funding. Increasingly over the last 25 years, in Australia and elsewhere, that funding has been distributed using ‘competitive’ market mechanisms in the form of managed markets.¹ These markets are distinguished from conventional markets primarily by the fact that government is the source of much, if not all, of the purchasing power of the users of services.

There are many variants of managed markets, but we can identify three major forms that are fundamentally distinguished by who selects the service providers. Much has been written about competitive tendering and contracting (‘contracting’),² whereby a government agency decides which organisation will be the provider for a designated group of service users and pays the organisation to deliver the services. However, relatively little attention has been given to another major form of managed market, quasi voucher-licensing (QVL),³ whereby each eligible user⁴ of a service has an individualised subsidy from government and they (or their agent) can choose their own provider from a set of approved (or ‘licensed’) organisations. The nature and impact of QVL systems are commonly treated incidentally in studies of specific services or by examining one type of QVL,⁵ but there are important generic similarities among what at first glance may seem a disparate series of funding systems. There are also hybrids of these two mechanisms, whereby a tender process is used to limit the set of possible providers from which users can choose if they wish to receive the subsidy (Davidson 2009 in press).

The purpose of this paper is to examine the potential impact of QVL on non-profit organisations (NPOs) in mixed markets for human services, especially in terms of how this may differ from the impact of contracting. We are not here examining whether NPOs or for-profit organisations (FPOs) provide better services or outcomes under QVL, but rather simply seeking to identify the potential impact of QVL on the presence and behaviour of those NPOs that provide human services, including how the broader role of NPOs in developing social capital and civil society may be affected. The paper is essentially an initial exploration of the question, drawing on some established theory and Australian experience to identify and illustrate the key issues, rather than pretending to set out a completed theory. One key point to emerge, however, is that while QVL systems are likely to lead to a smaller share of the market for NPOs and more commercial behaviour by some NPOs than is the case under contracting,

¹ These are also known as quasi-markets (Le Grand & Bartlett 1993, Bartlett et al 1994, Bartlett et al 1998). In this paper, we use the term ‘conventional markets’ to refer to markets where there is no or minimal government funds to purchase the product; that is, the type of market assumed in standard economic theory.
³ This is the first use of the term ‘quasi-voucher licensing’ (QVL). These systems have also been described as quasi-vouchers (Lyons, 1995, 1998, 2001), licence-subsidy systems (Davidson 2009 in press), consumer-directed payments, and demand-side subsidies. Most previous terms centre on the demand element, but the term QVL acknowledges the importance of the supply-side licensing element that limits the organisations to which service users can present their subsidies, and requires providers to comply with regulations that are monitored and enforced.
⁴ The term user in this paper refers to the direct recipient of a service (eg. the child in child care), whereas an agent is a person who makes decisions on behalf of a user (eg. the parent of the child, although government may also be an agent for some users). The term client is used to refer to the user and/or agent where the relationship with a provider is discussed. The terms customer and consumer are also synonyms for client in this context, but those terms have strong connotations in commodifying people-oriented services and are only used to highlight parallels with other markets.
⁵ An exception is Lyons (1995, 1998, 2001), who appears to have coined the term ‘quasi-voucher’.

these systems can also potentially enable some NPOs (that would otherwise not be selected under contracting) to remain as a funded provider and to remain truer to their original social mission and objectives.

Section 2 provides some necessary background about human services, the marketisation of government functions, managed markets, and service providers. Sections 3-4 outline the major features of QVL and the way in which its impact on service providers may differ from contracting. The next three sections then discuss, in turn, how the impact of QVL may differ from contracting in terms of the presence of NPOs, the behaviour of NPOs, and the capacity of NPOs to contribute to broader social objectives. Section 8 presents some data from the Australian experience. We then make some concluding comments, including suggestions for how the propositions in the paper may be empirically tested.

2. Background

2.1. Human Services

The paper is concerned with human services, defined by Zins (2001:6-7) as ‘institutionalised systematic services’ aimed at ‘meeting human needs…required for maintaining or promoting the overall quality of life’ of the service users. This encompasses ‘social services’ and covers a diverse range of fields and programs, including education, health, child care, residential and community care\(^6\) for the aged, disability support, family support, early intervention programs, homelessness, and job search assistance for the disadvantaged (Hasenfeld 1992). Most human services share common features that can make their provision via a ‘market’ somewhat problematic, given the substantial market failures that exist (Blank 2000) or even the lack of a market for some services where users lack financial resources. One aspect of these features is that they can limit the extent to which each user (or their family agent) can determine their provider. Davidson (2009) provides a detailed discussion of these features and their impact on human service providers.\(^7\)

2.2. The Marketisation of Human Services

The process of establishing managed markets in human services has been part of a broader movement by governments everywhere since the 1970s to use market approaches across the full range of their responsibilities. In the USA, the use of contracting in human services began in earnest in the 1960s and was well-established by the end of the 1980s (Smith & Lipsky 1993; Van Slyke 2002:3-4). The process occurred later in other nations such as the UK and Australia, where human services was one of the later targets of marketisation by government after action such as business and financial deregulation, the sale of government enterprises, corporatisation of government agencies, and the outsourcing of operational tasks. Thatcher did not seek to substantially change human services until 1988 in her third term (Le Grand & Bartlett 1993:1-3) and the Hawke Government in Australia (first elected in 1983) did not make many significant changes in its early period (McDermott 2008).

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\(^6\) Community care is a service that provides various forms of assistance to people who require some support because of frailty or disability, but who live at home rather than in a residential care facility (or nursing home).

\(^7\) However, it is also important not to overstate the distinct features of human services and to recognise that some of these features are ones that have traditionally been ascribed to all services, including services provided through conventional markets (Davidson 2009).
There were concerns that the push for ‘smaller government’ associated with marketisation would lead to a significant reduction in the funds available for human services. In fact, there has been a growing acknowledgement that governments must continue to substantially fund these services, coupled with significant increases in funding for a number of services and a recognition that in future years there will be an increasing demand for funds arising from demographic and other social changes (Smith & Lipsky, 1993:203-6; Saunders, 1998:11-12). What has changed substantially, however, is the way that these funds are distributed and the service are delivered. On the supply side, while governments do continue to directly provide services in some fields, there has been a much greater use of third party providers to deliver services in the name of the state, together with the introduction of market mechanisms to determine the providers for each service, leading to what has been described as the ‘hollow state’ (Milward & Provan, 2000). On the demand side, there has been a movement to enable the users of these services (or their agents) to have a greater say in who provides the services and the form in which they will be provided, through the use of both voice and exit mechanisms (Hirschmann 1970).

While the development of managed markets in human services has in part been aimed at reducing government expenditures, it has also been substantially about enhancing the quality and efficiency of services. However, the process has often been controversial, with questions not just about how it has been implemented or whether it has actually improved outcomes for users, but more fundamentally about whether it is appropriate to human services. As noted above, the nature of human services makes their provision via a ‘market’ problematic, and evaluating the actual impact of managed markets is complex given that their substantial growth has occurred alongside the introduction of other measures such as New Public Management and performance-based measures (which of course have also been driven in large part by the forces of marketisation).

### 2.3. Managed Markets

Managed markets are distinguished from conventional markets primarily by the fact that government is the source of much, if not all, of the purchasing power of the users of services. They are distinguished from most other forms of public funding because they require bodies that provide direct services for the public to directly compete against each other to obtain the funds. Introducing contestability for access to government funds aims to improve the quality of service providers both by encouraging new entrants and promoting change in existing providers.

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8 More broadly, the marketisation of public services has been justified by its advocates by three main arguments. First, the need to ‘reinvent government’ based on the claim that government can best achieve its objectives by focusing on strategy and policy rather than the detail of service delivery - that is, by ‘steering not rowing’ (Osborne & Gaebler 1993). Second, the claim that government has intrinsic deficiencies in delivering services and this is best done by the private and community sectors. Third, the claim that there are significant benefits in subjecting government funding to contestability and competition. In addition to these ostensible reasons, there have also at times been other unstated reasons, such as to weaken unions, or reward political supporters who have an interest in the fields being marketised.

9 We are focused on managed markets using non-government providers (FPO and NPO), but there are also ‘internal markets’ where government authorities use competitive processes to allocate funding between their ‘outlets’ (such as schools and hospitals).

10 Formally, contestability is about the ease of entry and exit to a market. In a perfectly contestable market, entry and exit are ‘costless’, in the sense that there are no additional costs for new entrants or ‘departees’ above the normal costs of establishing and operating the enterprise (Baumol 1982; Baumol et al. 1982).
Bartlett and Le Grand (1993:13-19) identify the core objectives that governments have in establishing managed markets in social policy, namely to promote greater effectiveness, efficiency, choice, responsiveness to client needs, and equity. There will be trade-offs in achieving these objectives; for example, increasing choice can mean a loss of efficiency. Bartlett and Le Grand (1993:19-34) also identify five key pre-requisites of managed markets if these objectives are to be achieved: some level of competition between providers; appropriate motivations and incentives for both buyer (whose focus should be the welfare of the users) and provider (who should in part be motivated by financial considerations so that they respond to market signals); symmetry in the information available to buyers and providers; minimal transaction costs; and avoidance of ‘creaming.’

There are many potential variants of managed markets, each emerging as the outcome of government decisions on a range of factors affecting the four core elements of a market - the product, buyers, sellers, and means of exchange (Davidson 2009). Governments, however, do not necessarily make explicit decisions about all of these factors. Indeed, in some cases, the ad hoc and implicit nature of some ‘decisions’ can mean that some elements of a program are inconsistent with other elements, or even with the overall objectives of the program. Further, ‘[i]n practice, the way a service is delivered … may be more a product of political dogma than of an assessment of relative efficiency or equity’ (Burchardt 1999:5).

As noted earlier, we can identify three major forms of managed markets that use non-government providers: contracting, quasi-voucher-licensing, and hybrids of these two. Contracting can take many forms, with variations along a number a number of dimensions, including the way the tender is conducted (eg. open or select, staged and EOIs, etc), how decisions are made as to who will win the tender (eg. possibility of rolling over contracts), and the form of the contract. Similarly, QVL systems can differ in a range of ways, including the way the subsidy is paid, the basis on which different users get different amounts, and the form of ‘licensing’. In the next section we will look in detail at the various forms of QVL systems and how they differ from contracting.

An important form are the hybrids of contracting and QVL, where there is a competitive tendering process that limits the numbers of providers who can ‘compete for customers’ and from whom users/agents can choose. There may be limits placed on the buyer-seller interaction or the frequency with which a user may change providers, and/or the use of mechanisms that ensure a minimum level of activity for all providers. The hybrid systems provide a valuable model. They aim to draw on the best aspects of both systems by limiting providers to the best ones, ensuring better planning of limited resources, and giving a greater guarantee of quality, while giving users greater choice and generating market signals. They can be structured to ensure that there is some stability for individual providers and thus for the overall supply of the services. The major disadvantage of hybrids is that they retain the complexities and costs of the CTC process.

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11 Bartlett & Le Grand (1993) (who use the term quasi-markets) only list four objectives, conflating effectiveness and efficiency into efficiency.
12 ‘Creaming’ involves limiting services to ‘less difficult’ clients rather than assisting those with more complex needs who require more resources and represent a greater operational risk.
13 For example, the New South Wales (NSW) Community Participation Program for people with a disability pays each contracted provider at least 75% of the agreed minimum intake during the first period of contracting even if a lesser number of clients choose any of the providers. This means that the government department is absorbing much of the risk, but it needs to be seen in the context of a rigorous process to determine the capacity of each applicant organisation prior to contracting them.
Given that it is substantially financing the services, government has the power to shape both the services and the markets in ways that go well beyond what governments can do in a conventional market (Davidson 2009). Three points are particularly important here. First, governments can directly control both who comes into the market (by its contracting or licensing decisions) and many aspects of how they operate, and thus substantially influence the costs and revenues of providers. Second, the design of each market creates a set of incentives and disincentives that will partially determine whether an organisation wishes to enter a particular market. Third, the greater capacity to influence the design and operation of the market via government opens the way for ‘politics’ to play a larger role in determining which providers actually get power within a managed market.

2.4. Service Providers in Human Services

The focus of this paper is on those services provided by third party organisations that access, directly or indirectly, government funds allocated for the services. Thus we begin from the point where government has already made the threshold decision to use external providers for a given service. While there is substantial theory and many practical tools to guide government in this decision 14 many such decisions over the last two decades appear to have been made on ideological or expedient grounds without adequate consideration of the theory or available evidence about the likely impact on the quality, effectiveness, efficiency, and cost of services. In addition, while third party providers are increasingly important in human services, they are not the total picture, even within a marketised environment. For some services, a government provider may be retained as one competitor in a managed market, 15 a process more likely to occur under contracting, with government providers relatively scarce under QVL. There are also situations where family or friends can be paid from government funds, 16 as well as services provided by FPOs and NPOs that are paid totally by the users and/or donor funds.

A common theme of theory and research about the participation of NPOs in markets and enterprise activities is that of institutional isomorphism, which brings with it the blurring of boundaries between NPOs and FPOs and mission drift as NPOs move away from their original purpose and are perceived to operate more like FPOs or their funders (Di Maggio & Powell 1983; Smith & Lipsky 1993). This will be a focus in Section 6 below regarding the behaviour of NPOs in QVL systems.

While ‘blurring’ is usually discussed in terms of NPOs becoming more commercial and business-like, there is some evidence of movement the other way. There is now considerable diversity among FPOs in human services, not merely in structure and size, but also in

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14 This ranges from the long tradition in broader economic theory about ‘make-or-buy’ decisions and transaction costs (eg. Coase 1937; Williamson 1975, 1998) through theory directly focused on this question (UK Treasury 2003, Blank 2000) and checklists to apply in specific cases (eg. Industry Commission (2000)).

15 There are two major reasons for this. First, and this is especially important in a nation with the geography and settlement patterns of Australia, there are likely to be communities and regions where no satisfactory NPO or FPO will be operating. Government providers tend to be more significant in less populous and more remote areas. Second, a government provider can potentially act as a market leader in driving best-practice in the industry by making explicit allowance for the positive externalities of its service in a way that is less likely in a totally commercial environment. These of course were the arguments for government business enterprises in Australia for much of the twentieth century, but which have largely been abandoned in the atomised world of the last quarter-century. A third reason for a government provider in conventional markets (eg. phones, utilities) is that a government business enterprise (GBE) can generate significant revenue for government.

16 This will vary by nation and service type, but it is especially likely in caring services (Evers et al 1994, Ungerson et al 2007, Fine 2007).
motivation and objectives (Davidson 2009). In particular, Marceau (1990) identified a group of FPOs in mainstream business (in manufacturing) that she describes as the ‘dwarves of capitalism’; these are people who own small operations, including many whose core objective is to be independent rather than wealthy. The ‘dwarves of capitalism’ have a strong presence in human services, and include people who have left employment with large NPOs or government because of their concern about the constraints of the bureaucratic and increasingly commercial culture in these organisations. Further, in an age of outsourcing, FPOs (including self-employment) ‘may offer the only alternative to professionals seeking to continue to practice their face-to-face-support skills’ (Taylor & Hoggett 1994:191). Some of these ‘dwarves’ represent a distinct and positive feature in service delivery, enabling experienced and capable people to provide services in ways, often very innovative, that focus on social and human objectives rather than organisational and commercial imperatives. Indeed, arguably the behaviour of quite a few of these small businesses is closer to the traditional view of NPOs than is perhaps now the case with some NPOs.

3. **Quasi-Voucher Licensing (QVL) Systems**

3.1. **Variants of QVLs - Design Issues**

There are two core features of quasi voucher-licensing (QVL) systems. First, on the demand side, government funding is distributed in the form of a subsidy for each individual approved user, and the user (or their agent) can choose their own provider. Second, however, the subsidy can only be used to obtain services from an approved provider (licence). Entry is possible for any provider who meets the set of minimum requirements and standards to obtain a licence, and licensed providers then ‘compete for customers’ with the government substantially meeting much, and possibly all, of the costs of service for approved users.

We now look at the different forms that subsidies and licences can take. This is not intended to be a comprehensive analysis of the design possibilities of systems, but rather in this context to give a sense of what is encompassed by these systems and to stimulate suggestions about the distinctive impact of QVL on NPOs.

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17 The variety of legal forms include public companies (ie. traded on the stock exchange), trans-national companies, large private equity firms, other incorporated firms with single owners or multiple shareholders, and unincorporated sole traders. With regard to motivation, many are profit-maximisers (eg. the board and management of public companies are required by law to ensure that the interests of shareholders are pre-eminent (Bakan 2004)) but some become involved in activities with altruistic or broader social aims as strategies to increase benefits in the long-term; others fundamentally want stability in the market as the basis for ensuring their continuing prosperity (Fligstein 2001); and others aim for some threshold of financial surplus but are then prepared to forsake extra profit in order to increase the social contribution of what they produce (Martin et al. 1998).

18 It perhaps need to be emphasised at this point that it is not being claimed that all, or even a large proportion of, small FPOs have this motivation. Clearly, many small FPOs in human services have owners who see them as cash cows and the first step to a commercial empire.

19 There is a substantial literature on the use of vouchers in human services, especially in education. Friedman (1962) presents the philosophical and economic arguments in what is considered a seminal work for proponents of vouchers. Lyons (1995) provides an outline of the core features of vouchers and their relationship to quasi-vouchers.
3.2. The Subsidy

3.2.1. Form of the Subsidy

We can identify three main categories of subsidy, two where the payments are made to users and one to providers.\textsuperscript{20} The first major category is \textit{direct payments to clients} in the form of cash, direct deposit, vouchers, etc, that the client (user or agent) can present to the supplier in full or partial payment of the service. The payment may be made before or after the service is provided. The second major category is \textit{tax-based mechanisms}, in the form of credits, rebates, or deductions.\textsuperscript{21} It is also important to note in this context that tax credits and tax deductions have a different distributional impact, with the latter providing a greater benefit to higher income clients in absolute dollars. The third major category is \textit{reimbursements to providers}, so that the price facing the client is lower. In some cases, the client may have an option to either sign over the direct payment to the supplier or obtain their own reimbursement for each transaction (eg. Medicare in Australia) or the reimbursement may be on the basis of a bulk report of all clients over a previous period (eg. residential aged care or private schools in Australia).

3.2.2. Level of subsidy

The level of subsidies under QVL can vary in terms of the level of the \textit{proportion of the total cost of the service} that the subsidy represents. For some services the subsidy is set at a level that enables a provider to operate with only this income;\textsuperscript{22} where the subsidy covers or almost covers the total cost, there is much greater scope for an agency to support disadvantaged or marginal users without requiring significant additional funds. More generally, however, there needs to a co-payment from the client (see below) or some further private subsidy.\textsuperscript{23}

The \textit{absolute dollar value of the subsidy} is also important in that, properly calculated, the price of a service will contain an element for overhead for the overall operation of the organisation. Unless this amount is sufficiently high, it may not be possible for an organisation to reach the critical mass to develop the organisational infrastructure necessary to support the service.

A third source of variation in the level of subsidy will be how \textit{variations between individual users} are determined. The subsidy for a given service type will generally not be a single fixed dollar sum, but vary on the basis of differences in the \textit{service} provided (eg. Medicare has a large array of prices linked to length of consultation, type of surgery, etc); the extent of each individual client’s \textit{need} for the service, which may be determined by independent government assessors (as with residential and community care in Australia) or by the provider; or the

\textsuperscript{20} Within each of these categories there are further variations. We will not explore these taxonomically, but it is important to bear in mind that the analysis below may need to be qualified in specific cases because of these variations.

\textsuperscript{21} These mechanisms have two major benefits for government. First, they can effectively defer the actual payment by government, perhaps for 1-2 years, thereby reducing public borrowing costs (although in Australia it is also possible for employees to lodge a declaration that they are eligible for the subsidy and have the tax taken out of their regular pay reduced). Second, they mask the total expenditure by government on any service. In Australia, there has been an increasing use of tax expenditures to fund the welfare state; between 1992-3 and 2005-06, they increased from 10% to 16% of public spending (Spies-Butcher & Stebbing 2008).

\textsuperscript{22} For example, with Medicare in Australia, in 2006-07, 73% of all services were bulk-billed (ie. no co-payment, with the provider being reimbursed), and a significant number of providers only bulk bill. (Medicare Australia 2007/Table 12).

\textsuperscript{23} These additional private subsidies could include donations to NPOs, or education scholarships given by FPOs in what is often essentially a marketing activity.
income of the client (which may include parental income as in child care).\textsuperscript{24} With programs such as community care, a common hourly subsidy rate may be charged for all clients and service types, but some will have been assessed as requiring more (subsidised) hours. There can also be cross-subsidies within QVL systems between clients with different needs. A provider may charge some clients for higher quality or more service with the profits going to meet the cost of the services for other clients; or all clients may be charged the same price but some require more staff time or other resources.

3.2.3. Co-payments

An important aspect in determining the entry of FPOs into human service markets using QVL is the extent to which a co-payment can be obtained from the client in addition to the subsidy from government. Where there is no limit on the amount of co-payment and the client basis is not restricted via a means test, the market is potentially very lucrative since providers can offer a substantially subsidised product to a more affluent sub-group of clients and be more able to ask for higher fees or provide additional (unsubsidised) service, as occurs in Australia, for example, with private schools, child care, and residential aged care.\textsuperscript{25}

3.3. Licensing Arrangements

Just as there is a variety of quasi-vouchers under QVL, there is also a variety of quasi-licences and licensing systems. These may be based on extensive regulatory machinery focused on initial accreditation and regular monitoring of the provider organisation; or on less rigorous processes to assess the capacity of an organisation; or on the professional qualifications of the staff directly providing the service.

Will service standards required of providers be higher or lower under QVL than contracting? On the one hand, they may be lower because only the best providers are selected under contracting. On the other hand, the standards under QVL may be deliberately set higher than under contracting because the government agency knows it will not be able to exercise control over performance, while the existence of a formal regulatory machinery may ensure that under QVL, service standards are actually enforced.

3.4. Distinctiveness of QVL Systems

For both the users and providers of services, markets using QVL systems operate much more like a conventional market. However, while regulation and small subsidies exist in many conventional markets, QVL systems are distinguished by the combination of regulation of providers that is directly linked to the nature of the service with a level of subsidy that represents a significant proportion of provider revenue. In QVL systems, there are usually other sources of revenue beside government and there is no clear-cut boundary in terms of the proportion of revenue obtained from government, but even where a majority of the revenue of providers comes from user co-payments, the government involvement (via funding and

\textsuperscript{24} This process was subverted by the Howard Government in Australia in relation to private school funding, with the level of subsidy depending on the average level of income of the student’s home locality. Thus a child from a rich family living in a poor region draws a higher subsidy than a child from a poorer family living in a rich region.

\textsuperscript{25} In some cases, the co-payment may be fully covered by other government payments (eg. in Australia, the old age pension is sufficient to meet the co-payment for many nursing home residents in Australia).
licensing) will be a key driver in determining the entry and operation of major providers in the market.  

QVL systems are distinguished from contracting in that any organisation that meets the minimum licensing requirements can provide services that attract government funds, whereas under contracting an organisation may meet the minimum service standards required of all tenderers, but still not be able to service approved users if it is not selected in the tender process. Under contracting, the competition between providers is to gain entry to the market and the user typically has no direct say about who the providers will be; under QVL, the competition between providers is to attract customers. In other words, under contracting, providers compete for markets, while under QVL they compete within markets. Both forms of competition exist under hybrid systems. Under both contracting and hybrids, generally no new provider can enter in the shorter term to respond to emerging client needs.

The other major difference from contracting is on the demand side. Under contracting, the buyer (ie. government) commits to buy from a provider for a guaranteed period, which in human services is usually at least a year and may be 3 or even 5 years. Typically, payments are made on a regular quarterly or six-monthly basis, and the provider has to meet performance indicators set and assessed by a single government agency. Under QVL, however, commitments and payments by buyers to providers are much more atomised (or less ‘bulky’), and the assessment of performance by buyers is less formal. There are many more buyers, obligations to use the provider in the future are far more limited, payments are more likely to be made on a weekly or monthly basis - or even by spot purchase - and performance is judged by a multitude of customers, few (if any) of whom will have formal performance indicators. In later sections, we consider how these differences impact on the presence and behaviour of providers, especially NPOs.

We will not explore it further in this paper, but we can identify a number of criteria to determine whether QVL should be used in preference to contracting. Three of these are drawn from the analysis by Blank (2000) that focuses on the type of market failure present in the service, namely the public policy purpose of the government funding (especially externalities and distribution issues), and the extent to which agency and measurability of outputs are problems. In addition we also need to consider the capacity of a QVL system to maximise the quality of providers, maximise efficiency,\(^2^7\) and constrain total cost. A further reason that governments use QVL systems is that these systems allow better targeting of benefits to particular individuals and groups (Lyons 1995).

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\(^{26}\) For example, the Australian corporate FPO, ABC Learning Centres, claimed that a key element of its ‘successful child care model’ was to ‘maximise government funding [to] underwrite income sources’ (ABC Learning Centres 2005).

\(^{27}\) This should include consideration of allocative, productive, and dynamic efficiencies (Maddala & Miller 1989:Chapter 9; Hilmer 1993:3-4).
4. Service Providers and QVL Systems

4.1. General Considerations

We now investigate the ways in which QVL systems differ from contracting in their effect upon providers, in terms of seven sets of factors: dependence on users; risk; flexibility, diversity, and growth; asymmetries of information; distributional effects; quality assurance of providers; and market structure. Some of these factors are intrinsic to all QVL, others are dependent on the particular design of each QVL. In later sections, we will draw on these factors to help explain how QVL systems impact on the presence, behaviour and broader social role of NPOs in managed markets for human services.

Dependence on Users

First, and most fundamentally, compared to contracting, QVL makes the viability of provider organisations much more dependent on the assessment of users than of government. While entry to these markets requires providers to respond to government regulations and standards, once these (usually relatively objective and transparent) criteria are met, the viability and success of providers depends on winning ‘customers’. Under contracting, ultimately it is the government agency’s perception of the user’s response that is important. Under QVL, however, a provider has to directly respond to the ‘consumer preferences’ of individual users who are free, to varying extents depending on the program, to simply take their custom elsewhere.

Risk

Second, the nature and level of risk is different for providers under QVL. It is a moot point and case-dependent - as to whether the overall risk for a provider including in the intermediate and longer-term, is more or less under QVL, but clearly the nature of the risk is different. QVL systems give providers less certainty but greater opportunity in the short-term. Winning a contract from a government agency will ensure that providers obtain a relatively fixed level of revenue and stability over the contract period, but in general they will be locked into an agreed level of activity and return. On the other hand, providers in QVL markets can continuously expand their business, but they also face the prospect of earning nothing if they cannot appeal to users. In the intermediate term, the risk of failure is less precipitous under QVL, since organisations are less likely to face the suddenness of losing a contract, but their long-term viability is dependent on continuing to attract users to their service and maintaining a clear channel of supply to users. Customer commitments and payments to providers are more atomised - and thus less secure - under QVL. Of course, some crisis may lead to a provider under QVL having the worst of both worlds with a sudden and unexpected large fall in clients and revenue, for example from a single well-publicised case of food poisoning or carer abuse at a residential aged care or child care facility that by itself would not have led to a loss of their contract.

28 Subject to cost escalation provisions and trigger mechanisms in the contract if circumstances change.
29 Of course they may have their accreditation (‘licence’) withdrawn, but maintaining their standards is something that is far more within their control than decisions about contracts.
Flexibility, Diversity, and Growth

A third set of factors involves greater possibilities for flexibility, diversity, and growth for service providers under QVL. Providers are likely to have greater flexibility as to whom they service and how they operate (although this may be less so if the licensing standards are very prescriptive). To the extent this is true, there should be greater diversity among providers under QVL and greater opportunity for providers to respond to market niches; by catering to only a segment of the total target population, a provider can focus on its particular mission and play to its organisational strengths. This also makes it more possible for existing providers to adapt their services or for new providers to enter the market, in response to emerging needs. QVL systems are also less of a zero sum game than contracting, given that there is likely to be greater marketing activity by providers, which in turn may generate new demand; and, as noted in Section 5 below, new entrants are more likely under QVL and these may include powerful corporates whose political influence and lobbying power are used to increase the total or per capita government funding available for the service.

Asymmetry of Information

Fourth, buyers under QVL (ie. individual users and their agents) are much more diverse than the buyers under contracting (ie. a government agency), with most not having access to, nor the time and other resources to consider, comprehensive and detailed information about the operation and performance of each provider. Thus providers have more scope to exploit information asymmetries. Ideally, the diversity of buyers should mean that providers are more responsive to client needs, but it also mean that providers have a greater opportunity to use clever marketing techniques and attractions that may be only superficially linked to quality service as means of attracting ‘customers’.

Target Group and Distributional Factors

A fifth set of factors concern potential distributional effects between different individuals and sub-groups of the population, which may arise depending on the design of each QVL. In turn this will affect the type and behaviour of providers wishing to enter each market. An important example is how QVL can affect whether creaming may occur. It is likely that QVL will reduce creaming where higher need clients attract higher payments that reflect their real costs, but will exacerbate it where there is no difference in payment according to need. While a contract may require a provider to service a certain number of higher need users, there is an intrinsic pressure to minimise the number of such users to that of contracted performance levels. Under QVL, providers may be either required under their licence to service higher need users or have an incentive to target them where payments are high; but where there are no licence conditions or higher payment for higher need users, then QVL may result in more creaming.

Each form of subsidy payment also has its own particular effects on the presence and behaviour of providers in QVL. For example, there are at least two potential impacts from the use of tax expenditures. First, this method of payment requires the individual to pay up front and then wait (for possibly 1-2 years) for reimbursement; this makes it less likely that people of limited means can pay. Second, if the subsidy is in the form of a deduction, there will be the usual equity effects of deductions favouring higher income earners by giving greater benefits in

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30 This could occur either under more open-ended automatic eligibility programs (eg. childcare and Medicare in Australia) or by generating more applicants to be tested where individual client eligibility has to be determined (eg. community and residential aged care).
terms of absolute dollars saved; this is less of an issue if it is paid as a tax credit or rebate, but lower income people still have to earn enough to pay the tax. Together, these two forces act to reduce demand for a service, especially for higher priced FPOs. On the other hand the use of direct payments or reimbursements may have the opposite effect stimulating demand among lower income groups, given that price signals are hidden and the service is virtually a ‘free good’ for users; this can be an issue with Medicare where lonely people may go to a bulk-billing doctor simply for company.

The level of the subsidy and the possibility of co-payments have distributional effects that impact on who becomes a provider. A key issue is the extent to which a co-payment is allowed, encouraged, or required.\(^3\) The more a co-payment is allowed, the more likely it is that higher income groups will pay for more or a higher quality of service. Thus the universality of a scheme will accentuate this effect, given that the more universal a scheme, the wider the range of consumer preferences and more high-income users/agents. Further, the more universal a scheme and the more potential for co-payments, the more likely it is that there will be stratified markets with profit-maximising providers having a strong incentive to seek more affluent clients and give a higher level of service to these sub-groups in the target population (Marwell & McLerney 2005).\(^3\)

**Formal requirements for licensing of providers**

*Sixth*, the processes by which providers are licensed will affect the profile of providers for any services using QVL. It is well established that contracting favours larger organisations given that significant resources are usually required to develop a successful tender and tendering agencies often look to the security blanket of selecting a larger organisation to ensure delivery. The second factor is less important with QVL, but the first is simply replaced by the greater capacity of large organisations to prepare for accreditation and may be accentuated where a government agency sets high and detailed service standards because it will have limited scope to exert control over performance in the future. A further potential impact is where the accreditation process for QVL piggybacks on the accreditation of the professionals who provide the service, as will often occur in medical-linked services (eg. payments under Medicare in Australia are based on a system of individual practitioners with ‘provider numbers’).\(^3\) We would also expect that where a QVL system provides scope for family or friends to be a paid provider, (eg. this is a major variable around which funding schemes for personal care are constructed (Ungerson et al 2007)), the demand for organisational providers would be reduced, although in some such programs, there is a requirement that any carer paid with government funds receive some formal training and this has opened up a new ‘business arm’ for provider organisations.

**Market Structure**

*Finally*, QVL will have a major impact on the structure of the markets. On the one hand, the market is likely to take the form of differentiated (or monopolistic) competition (Chamberlin

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31 For example, in Australia, a co-payment is allowed under Medicare but often not charged (ie. by providers who bulk bill); it is allowed under child care and generally charged; and it is required under HACC (community care) where a provider must have a policy for user charges although this can include procedures for granting total exemption.

32 For reasons noted above, this possibility is accentuated if the subsidy is paid via a tax deduction since the dollar value of the subsidy will be higher for higher income people.

33 Smith & Lipsky (1993) also point out that this can have the effect of ‘medicalising’ the delivery model of services that are intended to have more of a social focus.
1933; Robinson 1933), where there are a number of providers with similar, but distinctive, products. Such markets are characterised by an excess number of suppliers compared to what efficiency would dictate. This suggests that there could be viability issues for some providers, less incentive for profit-maximising FPOs to enter the market (although markets based on differentiated competition are often the life-blood of small business), less stability for providers, and a greater turnover of organisations in the market. On the other hand, the Productivity Commission in Australia (2002) suggested that the replacement of the current contracting system for Job Network providers by QVL would ‘lead to some consolidation in the industry’. As we see later, such consolidation has occurred in child care in the wake of the movement to QVL.

4.2. Application to NPOs

In the next three sections, we draw the earlier discussion together to examine three different effects - first, the presence of NPOs in QVL markets; second, the behaviour of NPOs in QVL markets; and third, the impact of QVL markets on the role of NPOs in building social capital and civil society. As we have noted earlier, the final outcomes with regard to each of these three effects in any specific case will depend very much on the specific form that each QVL market takes.

In what follows, we are essentially examining what would change in both the short-term and the longer term if, for a given service, a contracting system was changed to a QVL system, with no change to the fundamental service standards, resourcing, or client eligibility for the subsidy. That is, if the program funds were cashed (or ‘vouchered’) out, and the government maintained the same total dollars, the same dollar cost per individual client (including variations by need), the same eligibility requirements for the service, and the same minimum level of service quality that providers have to give to gain entry to the market. Our major interest is in the comparative static effects, but we also note some dynamic effects, especially in the way in which QVL systems may attract more FPOs which can then generate changes in the parameters of a system.

This is essentially an initial exploration of the issues. In examining the three effects, we identify the implications of the factors set out above and draw on some existing theory and on the Australian experience to illustrate what may happen and how existing theory on NPOs involved in contracting and other mixed markets can be used to analyse the subject of this paper. There are many other such possibilities to use existing theory to explore this question.

As noted earlier, there are FPOs whose principals are primarily driven by social concerns and the desire to maximise quality of service and who are prepared to sacrifice profit to achieve these aims. Thus, in what follows, the discussion of NPOs implicitly includes these more socially-conscious non-profit maximising FPOs in many respects.

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34 This national program providing job search assistance to disadvantaged people via a network of contracted providers was established in 1998 to replace a service system formerly provided directly by the national government through its Commonwealth Employment Service (CES).
5. Presence of NPOs

What are the implications from the earlier discussion for whether NPOs are more or less likely to be present as providers under QVL than under contracting?

The first conclusion is that the impact of QVL on the presence of NPOs will vary by sector, dependent on the nature of the service and the particular form of QVL that is adopted, especially in terms of the nature and size of the target group eligible for the subsidy, the way the subsidy is paid, the level of subsidy and the capacity to obtain a co-payment from clients. Some sectors will be particularly attractive to profit-maximising FPOs, because of higher subsidies, higher income users, lower costs, and/or lower service standards to meet. Some sectors will also be relatively more attractive by requiring substantial capital, which FPOs are more able to obtain (Krashinsky 1986:116; Weisbrod & Schlesinger 1986:146). Ryan (1999:130) also points out that FPOs are more likely to enter sectors where there is a higher level of risk for providers since they are able to more easily access capital to cover this risk. An alternative argument, however, is that FPOs are especially attracted by the existence of ‘government-guaranteed’ income because it reduces risk for a provider. Both points may well be true in that different sectors will attract FPOs with different attitudes to risk and the trade-off between return and security.

A second conclusion is that overall there is likely to be a greater presence of FPOs under QVL, although in those sectors with limited target groups and subsidies this may be smaller non-profit maximising FPOs (‘dwarves’ of capitalism). First, as noted above, some sectors will be particularly attractive to FPOs, because of the potential for higher profits. Second, under QVL, there are simply more opportunities for providers to enter the market than if there is a single contractor. Given that NPOs usually emerge to meet a specific need and tend to address existing needs, while FPOs are more likely to seek new fields of activity and growing markets (Austin et al, 2006), we can expect that new entrants to most human service sectors are more likely to be FPOs. Of course, in those (relatively fewer) sectors where FPOs currently have the contract(s), then the effect would be reversed by introduction of QVL and the presence of NPOs could well increase. Third, given that under QVL, providers have much greater capacity to exploit asymmetries of information, it is reasonable to assume that profit-maximisers, primarily focused on the bottom-line rather than clients, are more likely to do this. While FPOs will rightly argue that they will lose customers if quality is perceived to fall, a fine balance between limiting costs and an acceptable level of quality can be maintained, especially where information to customers can be restricted and marketing techniques used to shape customer expectations (Galbraith 1958; Stilwell 2005:233-234; Press & Woodrow 2005:282–83). Finally, where the introduction of QVL does lead to more FPOs, the new entrants may include powerful corporates that can use their political influence and lobbying power and resources to increase government funding for the service and dilute service standards; \(^{35}\) in turn this will make the sector even more attractive for FPOs.

Against the above factors, however, QVL does have some positives for NPOs. First, QVL allows NPOs to retain some presence in a sector where otherwise a single FPO might win the tender. Indeed, if under QVL the authorities decide to make the licensing requirements on an organisation more rigorous than would be required for entry to a tender process, it may exclude some cost-cutting FPO competitors offering a lower quality of service. Second, the greater flexibility allowed providers under QVL allow for a much wider range of NPOs that can appeal to different niche groups. Some NPOs may have a smaller client base, but they can remain in

\(^{35}\) See the discussion in Section 8.4 concerning staff-user ratios in child care.
the sector and cater to groups more closely linked to the NPO’s core mission. Third, if under QVL providers can cater to more people and a richer clientele, this can lead to the entry of politically influential FPOs, there may be greater funding and a larger ‘cake’, albeit a smaller market share for NPOs.36

Where dual (or stratified) markets develop (ie. where higher income users can make a co-payment to achieve more and/or higher quality services) NPOs are more likely to predominantly cater to the lower end of such markets (Marwell and McInerney 2005), especially given that social entrepreneurs are more likely to choose to pursue opportunities because of, not despite, an inhospitable context, (Austin et al, 2006). Hence in a growing market, we are likely to see the development of dual markets with FPOs servicing the upper end of the income scale and NPOs focusing on poorer groups and neighbourhoods. However, this too has the seeds of potential for NPOs. An NPO could exploit this situation for social ends by segmenting its market and catering to both groups by providing two levels of service. It can market its advantages as an NPO to higher income groups (as we now see in Australia with non-profit banks, superannuation funds, etc), and then charge those groups a premium rate, the revenues from which can cross-subsidise the service to poorer groups. In doing this, an NPO would need to be aware of the ‘pitfalls of profits’ (Weisbrod 2004), and it may require two distinct divisions within the organisation to ensure the social mission and culture of the NPO working with less affluent users is not threatened.

**Trust**

A number of writers have used the theory of contract failure37 to explain the relative presence of NPOs and FPOs in any field (Hansmann 1980, 1987, 1996). The theory essentially rests on two premises. The first premise is that where there is asymmetry of information between seller and buyer because the delivery of the service is largely unobservable by the buyer and/or the outcomes are largely unmeasurable, buyers base their decision on the trust they have in the service provider. The second premise is that, in such situations, buyers have more trust in NPOs because NPOs face a non-distributional constraint (ie. profits cannot be distributed as dividends to individual owners). Hansmann (1980:870 –871) further argues that ‘the non-distributional constraint…has real meaning only when an enterprise is of sufficient scale to develop large earnings.’

Davidson (2009) examines the premises of this theory to understand why we see the growing (and in some cases dominant) presence of FPOs, especially large ones, in human services, where the delivery of the service is largely unobservable by the buyer and/or the outcomes are largely unmeasurable. Under contracting, why do government agencies choose FPOs; and under QVL, why do individual users (or their agents) choose FPOs?38 In summary, it is argued that, with regard to the first premise, the need for trust is less of a concern for those buyers who believe they can accurately assess the quality and outcomes of a service, while many people make their decisions not by a simultaneous balancing of all the variables in a single function, but a series of filter decisions (Mannion & Smith 1998:128–29). Thus they only seek a minimum threshold level of quality, after which locality, price, efficiency, and other factors

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36 See Section 8.4 for an example from child care in Australia.  
37 In the context of this paper, the term ‘contract failure’ has the potential to create some confusion. The meaning of ‘contract’ here is not restricted to formal agreements as in contracting, but includes implicit understandings between buyers and sellers.  
38 Note that Hansmann’s original article (Hansmann 1980) focused largely on overseas aid, where donors (or ‘buyers of aid services’) have few means of checking on the supplier. He explicitly noted that his analysis needs further development to cover mixed market situations where NPOs directly compete with FPOs.
will be successively taken into account in their calculus of decision-making about human services to determine the ‘best value-for-money’. The second premise needs to be qualified by considerations as to how trust is gained - or lost. FPOs can gain greater trust in a number of ways, for example by employing well-qualified, experienced staff with good reputations, undertaking non-profit maximising activities, and marketing efforts to mould the attitudes and expectations of buyers. Conversely, NPOs as a group have lost some of their ‘trust advantage’, because some have adopted corporate strategies and processes aimed at maximising financial surplus, organisational growth, the ‘market-based’ remuneration of senior employees, and reducing the rights and conditions of staff (Horin 2007). While as a group NPOs may still have a stronger claim to trust, they no longer have a monopoly on it, and for many buyers, there will be FPOs, especially among the ‘dwarves of capitalism’, in whom buyers are prepared to place at least equal trust.

QVL will tend to accentuate these processes. Given that individual buyers have less capacity to collect and analyse information about providers (even if government operates some form of information/rating schemes), one might expect that trust would become more important. Against this, however, there are many different buyers each with their own preferences and ways of making decisions. In such a situation, with many differentiated buyers, marketing and persuasive techniques can be used to great effect. Further, where the subsidised service is more universal (as is likely under QVL), buyers will increasingly include people who are more confident of their own judgement and who put greater trust in FPOs to deliver services. This confidence may or may not be justified, especially if the assessment is based on only on a partial view of the service - but we are here trying to explain ‘buying decisions’, not the objective reality of the service. In these ways, the commercial advantage of large organisations and FPOs can come into play, especially in more capital-intensive sectors, providing there is an acceptable base level of quality. FPOs may be seen as more flexible and offering better services and thus increasingly replace NPOs in QVL systems where there is greater scope for these advantages. With regard to how trust is gained, under QVL it is likely that some NPOs will become more commercial (see next section) and there will be more non-profit-maximising FPO ‘dwarves’ entering many fields. Thus, in the more atomised QVL markets, while the dominant demand may still be for NPOs, there will be greater scope for FPOs.

**Incumbency**

Another important basis for establishing trust in a service provider is incumbency. Demsetz (1982) argued that underlying most of the barriers for new entrants to any market is imperfect information, which can affect decisions by all market participants, including producers, consumers, and providers of capital. In the absence of perfect information for buyers, he argues that the reputation of incumbents and the trust they have developed among consumers and investors is central to giving them an advantage over new entrants. In addition, the notion of ‘commercial-in-confidence’ can be used to further restrict the information available to competitors and consumers, and a means by which incumbents can entrench their advantage.

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39 Note that the non-distribution constraint does not normally apply to remuneration for employees in defining an organisation as ‘non-profit’. Indeed some governments have sought to remove tax privileges for NPOs paying excessive remuneration to employees.

40 Press and Woodrow (2005:282) note several studies showing that parents can overestimate the quality of child care.
It is instructive here to consider the influence of incumbency when a managed market is established or changed. Some Australian evidence suggests that while incumbency is important, its power may be reduced if there is a rapid change in the market and/or the incumbents are small. Thus, the establishment of the Job Network saw large NPOs retain their employment support, but there was a major fall in the number of small NPOs who were replaced by FPOs. Similarly, in the 1990s, a QVL system was introduced into child care, a sector dominated by small NPOs. A decade later, FPOs provide over 70% of child care places, with the market dominated by one large corporate. In community care, the removal of a ban on FPOs in the Home and Community Care (HACC) program in 2005 has thus far seen only minor inroads by FPOs.

Defending traditional NPO territory

Maxwell and McInerney (2005) present a model to show the development of mixed markets via a process that means NPOs ‘may sow the seeds of their own destruction’ (Maxwell and McInerney 2005:9). They posit a five-stage process whereby NPOs, having initially established a service in response to unmet social needs, develop the service to a point where it becomes potentially profitable and FPOs then enter the market. They argue that this may result in one of three possible market outcomes from the viewpoint of NPOs. The markets may end up stratified, with NPOs serving poorer clients and subsidised by donors and FPOs serving wealthier clients paying market rates; NPOs may be displaced; or the market may be defended by NPOs.

We can use this schema to analyse the introduction of QVL. Our earlier analysis suggests a range of forces could determine the outcome in any specific sector, but the major drivers are likely to include the proportion of the target population eligible for the subsidy, the size of the subsidy, the need and scope for a co-payment, the size of incumbent NPOs at the time of the change, and the rapidity of change. For example, it seems reasonable to hypothesise that stratification is more likely to occur where the service is more universal and there is a capacity to obtain a significant co-payment; displacement is more likely where there are many smaller NPOs and the change to the new system is relatively rapid and abrupt; and a defended market is more likely where there are well-established, larger NPOs, less scope for a co-payment and the subsidy is less universal.

Other factors - history, politics, and place

This paper is focused on the impact of the design of managed markets on NPOs, but this impact will be limited by history, politics, and place. For example, NPOs are likely to maintain a strong presence in sectors where large NPOs are long-established, and funding was initially made contestable via contracts. Indeed, it might be the case that NPOs are more likely to remain prevalent where contestability is first introduced via contracting rather than directly moving to QVL, or where a form of QVL has operated for many years with very limited subsidies. That is, QVL systems are more like conventional markets, and as suggested so far, major providers will operate more like conventional businesses. The transition phase enables

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41 However, events in 2008 have led to major doubts about the future viability of this corporate. See Section 8.4 below.
42 HACC is the major source of funds for this service in Australia (with 60% of funds from the federal government and 40% from the states). It uses contracting, and has a significant involvement of government providers.
43 This depends very much on the policy and attitude of the government agency and its staff. The more general case in Australia is that agencies, wishing to minimise early problems, choose larger NPOs as major providers; in some sectors, however, agencies have actively sought FPO involvement at the expense of small NPOs.
NPOs to make the adjustments and establish themselves in the market, thereby gaining the power of incumbency when the market is changed to QVL.

Politics is important and every sector has its stories of the lobbying of government at both the political and bureaucratic levels, to open up opportunities and close off competitors. Thus in some cases, causality may be in the opposite direction from that generally assumed, if the market has been shaped to favour certain players, rather than the players responding to the market. The opening up of human services to FPOs, together with the growth of large national NPOs and a greater corporate presence on NPO boards, has (ironically, in view of the alleged transparency benefits of contestability) increased the potential of lobbying for narrower interests.

The particular conjunction of history, politics and other geographical factors (eg. remoteness, population size and growth of each area, etc) means that the effect can change in terms of place. This is most obviously seen by the greater presence of NPOs and government providers in more sparsely populated regions, but it is also evident in the particular development of individual states and nations.

6. Behaviour of NPOs

There is a substantial literature on the impact of contracting on the motivation and behaviour of NPOs, encompassing a wide range of views on how deep and widespread the effects have been, and how much they are a cause for concern. Many of these effects will also be evident for NPOs operating in QVL, and in this section we consider in what ways the impact of QVL on NPOs may differ from that of contracting.

The main focus below is on how NPOs balance the tensions and complementarities of their social and commercial objectives. There are of course many ways in which this may be reflected in their behaviour. Of particular interest is the extent to which there might be mission drift whereby NPOs are move away from their original purpose; or institutional isomorphism, whereby NPOs operate more like FPOs or their funders. We now look at two well-known explanations of these phenomena to help identify what can happen under a QVL.

Kramer’s analysis of the impact of contracting

Kramer (2001) analyses the impact the purchase of service contracting (POSC) on NPOs. Importantly he notes that POSC has had a differential impact on NPOs depending on the size and age of the organisation and the type of service. He also notes that during the period in which POSC grew, there was:

...[an] increase [in] the size and scale of operations and a greater formalisation and bureaucratisation [of NPOs], although it is not clear to what extent these changes can be attributed to public funding such as POSC...It is ironic that smaller-community-based organisations survive in the contract culture by modifying the very qualities that might have made them attractive as contractors in the first place. (Kramer 2001: 374)

Kramer identified four main ways that contracting potentially affects NPOs. First, contracting may lead to goal distortion or deflection, which may occur either through being required by the contracting agency to ‘make certain decisions about the type of clientele, staff and mode of

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44 That is, there will be some conflict and trade-offs (‘tensions’) between social and commercial objectives, but the they can also reinforce and facilitate achievement of the other (‘complementarities’).
service’, or through the less direct processes of mission drift as the organisation itself makes changes in order to grow or simply to survive. As we have noted above, under QVL, the direct influence of the funding agency will be relatively less important, replaced by pressures more akin to those of conventional markets. In turn, this may mean that NPOs that wish to maintain or increase a large market share will adopt a modus operandi similar to profit-maximising FPOs. On the other hand, it does allow NPOs to remain operating in the way they wish by appealing to a smaller niche group of clients.

Kramer’s second potential effect of POSC is reduced autonomy for an NPO. One way in which autonomy might be further reduced under QVL is where (as noted earlier) the requirements for an organisation’s standards and processes under licensing are more rigorous than under contracting for the same service. However, even in such a case, a provider would have greater relative freedom in determining its particular client group and the way it conducts a number of professional and operational aspects.

Kramer’s third potential effect is greater accountability. As Kramer emphasises, however, NPOs have multiple accountabilities, both internal and external; in addition to government, they are accountable ‘to their boards, by-laws, clients, staff, contributors, and other funding sources (Kramer 2001:376). Under QVL, providers remain primarily accountable to a government agency for service standards and inputs (ie. to obtain and retain their licence), but there is a major shift in that they are now essentially accountable to clients for their performance with less need for formal performance indicators (PIs) to prove performance in order to obtain revenue. The PIs are now those of the market and will ultimately reduce to managers of service providers showing their principals (ie. the owners of FPOs or the boards of NPOs) that they have enough clients to at least cover costs. This may lead to a greater range in the quality of performance between all providers, both NPO and FPO, with some danger of lower quality providers but also enabling good providers to stretch the upper limits for quality, responsiveness and outcomes.

Kramer’s fourth effect is devoluntarisation. If an NPO takes the path of operating more like a conventional business, this could also occur under QVL. On the other hand, the use of volunteers can not only reduce costs, but can increase an organisation’s ‘reach’ into the community to help obtain additional clients, and thus increase an NPO’s revenue.

**Institutional Isomorphism**

Di Maggio & Powell (1983) identify three processes by which institutional isomorphism occurs. Given the factors outlined above, the likelihood of coercive change (ie. change arising pressure from other organisations on which they are dependent) is less under QVL. There may be more or less mimetic change (ie. change arising from imitation of others) because while there is a reduced need to satisfy a government department (ie. under contracting, an NPO may take on the characteristics of organisations perceived by the department to be ‘good’) there will be other pressures for mimetic change. First, there will be a wider range of models from which a NPO can draw ideas and copy; and, second, organisations wishing to grow are likely to draw

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45 However Kramer does argue that under contracting a reduction in autonomy is ‘less than is popularly imagined, especially with multi-product providers, while Ferris (2001:391) also argues that ‘the double edge sword of government [on autonomy] is not a sharp as is often perceived’. It is often claimed that contracting regimes are monopolies, but this tends to ignore the fact that large multi-service agencies can, over time, shift their resources into another sector.

46 Of course, they will also at times be required to be directly accountable to clients for standards and inputs first to gain their custom and later to explain any gaps in performance to a ‘customer’.
heavily on the experience of successful commercial enterprises. Similarly, the likelihood of normative change (ie. change that arises primarily from professionalisation) will depend on each case. On the one hand the reduced level of central control of the market by government may reduce the level of coordination and sharing of professional experience. More likely, however, is that the licensing requirements will enhance the importance of professional qualifications and norms, including the use of these qualifications as the basis for a licence) so that those service sectors more dependent on professional qualifications will be subject to greater normative change under QVL. A key driver in what happens in any sector is likely to be the strength and level of activity of professional associations and peak bodies.

We can also note another form of isomorphism with changes to delivery models in different sectors. Turnham (2007) distinguishes between the type of service model used by providers of community care on the basis of four ‘discourses’- biomedical, disability rights, welfare, and market - which reflect the background and values of the founders and principals of the organisations. She argues that in Australia the biomedical discourse ‘dominates the residential aged care industry and now appears to be increasingly informing the community aged care industry through Community Aged Care Packages’ and that ‘the majority of private for profit agencies are nursing agencies operating according to a combined biomedical/market paradigm’. (Turnham 2007:8-9). Residential aged care and these packages both use QVL systems.

**Other Factors**

The size of the subsidy payment may impact on whether QVL increases or decreases institutional isomorphism. On the one hand, if the payment is a substantial proportion of the total cost of the service, it allows each organisation to do its own thing. Conversely, NPOs in QVL also have to compete (eg. by price, promotion, etc) to survive and this could lead them to either niches or institutional isomorphism.

Whether and how an NPO is affected by each of the factors outlined above will be the result of a decision by the NPO to go down a particular path. These are choices by the NPO, and one conclusion from the above discussion is that just as QVL systems allow more choice for users, they can also allow more choice for providers. Different NPOs will go in different directions. It is likely to drive growth-oriented NPOs even more to commercial approaches, while others can follow a path they consider better meets client needs because they don’t have to meet narrow contracting criteria. The key threshold decision for an NPO is perhaps how big a market share the organisation wants, and a key driver as to what will happen is likely to be the background and philosophies of the organisation’s principals.\(^{47}\)

**Relational Approaches**

Davidson (2009) argues that from the perspective of the overall benefit to society, the selection of providers under contracting should be more relational-based and should take account of the capacity of a provider organisation to achieve other social objectives, including their activities to build social capital and the extent of their socially valuable non-profit maximising behaviour. Similarly, licensing requirements under QVL should require some such activity by potential providers. For providers, the effect would be parallel to reducing the profit or rate of return to the business, but it would also be a mechanism that gives financial credit to providers

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\(^{47}\) Dalton et al (2008) have undertaken an extensive examination of the basis on which mangers in NPOs in Australia have been selected.
for generating positive externalities from their service. Similarly, government activity has become increasingly atomised under the influence of marketisation, with each agency forced to meet its own performance targets regardless of the negative externalities it creates or the positive externalities it does or does not produce for the activities of other agencies. However, just as a corporate group is interested in the overall bottom line and uses transfer pricing to reduce profit in one department in order to increase total profit, so too a government can reasonably do this in terms of social benefits and take account of the broader social contribution of all players. Such an approach would be likely to benefit NPOs.

7. **Impact on broader social objectives**

Traditionally, NPOs, even those whose primary role has been to deliver services, have sought to contribute to achieving broader social objectives that go beyond their own organisation simply providing specific services to individuals or groups. Four key means by which they can contribute to these broader objectives and to civil society have been through the development of the infrastructure of the sector(s) in which they operate; the development of social capital in their local areas (Putnam 2000); advocacy for changes to policy and programs that will benefit both their clients and the broader society; and the development of the infrastructure and dynamic for broader social action.

Lyons (1997:91) argues, however, that there is a ‘bleak picture for the generation of social capital’ by NPOs, especially those NPOs whose primary role is to provide services. He argues that both contracting and quasi-vouchers ‘work against the creation of social capital’ by ‘strongly encourag[ing] the business model of management’, requiring competition with NPOs, and ‘re-directing both paid staff time and funds from the possibility of social capital building’ to pursuing additional revenue. Indeed, ‘[t]hose few non-profits which attempt to operate by a civil society model are particularly disadvantaged in the market-type environment.’ (Lyons: 1997:93). Along these lines, Kramer (2001:358) questions whether the blurring of the boundaries between NPOs and FPOs resulting from POSC ‘may indeed threaten the future of civil society.’

Once again, we ask how the effects of QVL might vary from those of contracting?

There are a number of forces inherent in marketisation that may lead to NPOs putting a greater relative focus on specific services at the expense of broader social objectives under both contracting and QVL. Focusing an organisation on one activity (such as service delivery) automatically precludes, or puts some limits on, its capacity for other activities (such as building social capital), especially in terms of governance and the allocation of resources (Lyons, 1997, 2001). Closely associated with this is the potential for mission drift as the principals of NPOs increasingly come to see their main role as service delivery and organisational growth, especially in an environment where there are greater limits on resources available to pursue social objectives because funding agencies increasingly require funding to be directly linked to specific services. Against this, however, there are NPOs that see their core role as building civil society and regard service delivery as a means of obtaining the revenue and resources to enable them to do this. Such organisations may be prepared to agree to directives from a funding agency that they consider do not lead to optimum services in order to retain the funding to pursue what they see as more important aims.48

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48 From current (and as yet unpublished) research by the author.
There are, however, several potential points of difference between contracting and QVL. The first arises from the greater potential for obtaining a co-payment since that could be made sufficiently large to subsidise the other activities of the organisation. Whether this occurs will depend on the universality of the service, the extent of the NPO’s concern with ensuring access to services for all users, and the price elasticity of the service. A key point, however, is that QVL does potentially give a NPO greater scope to overcome the limits of contracting and generate some extra dollars to support broader social objectives.

A second point of difference arises from the way in which an NPO must adjust to a decline in revenue when the scale of its operation falls, and the impact this can have on the stability of the organisation. Under contracting, an organisation’s total costs may be covered by an appropriate allocation of overhead costs across all projects and the scale of the organisation’s operation is likely to be constant until the time for contract renewal. Problems for the overall operation of an NPO largely dependent on contracts - particularly the operation of its ‘unfunded’ social objectives - will emerge if a significant contract is lost, since they cannot change prices for other services mid-contract period (or at least not ostensibly for this reason). Under QVL, negative movements in costs or revenues will generally be more gradual and adjustments can be made over time, for example by reducing some services and/or increasing the co-payment. It requires NPOs to operate very much more like a ‘normal’ business continually adjusting its ‘product’ lines and prices, with the likelihood of its free social ‘products’ bearing the greatest impact of periodic adjustments.

A third potential difference concerns the traditional role of NPOs in undertaking cooperative activities with other providers to develop ‘industry infrastructure’ (eg. training, sharing ideas for service development, etc). This has been one of the casualties of marketisation, and this may well be exacerbated under QVL, given the ongoing day-to-day nature of competition under these systems, especially at a local level. Cooperation is thus more likely to be restricted to the development of commercial alliances between ‘compatible’ organisations.

Fourth, QVL may reduce the scope for NPOs to devote resources to broader social objectives even further than contracting because it requires providers to be more responsive to the needs and wishes of individual consumers. On the other hand there are a number of counter-forces working in the other direction. Under contracting, the decision-makers in government agencies are less likely to be people who benefit from the local social capital developed by an NPO, whereas under QVL the work of NPOs in developing local social capital may be an important means of marketing themselves to local people. In this way, an NPO can strengthen bonding social capital between users of their services, for example where the parents of children at a child care centre appreciate the efforts of a centre to link them with other parents. Further, QVL systems not based on reimbursements to providers make the cost of the service appear as

49 This assumes, for example, that the organisation is operationally very efficient such that the price increase does not lead to a major fall in the number of customers.
50 ‘Price elasticity of demand’ refers to the rate that demand for a product falls as its price rises. The problem here is if the service is ‘price-elastic’ so that the fall in demand from a price increase leads to a fall in total revenue.
51 A more important driver of the final outcome in any sector and region, however, may well be the past history between the players and the background of individuals.
52 A good example is where a shop-front organisation at the neighbourhood level provides free micro-services (eg. information, minor assistance with transport, allowing a person to make a phone call, etc) that have an important impact in enabling the smooth functioning of people’s lives and enabling them to link into their local community.
53 Bonding social capital draws an existing group closer, in contrast to bridging social capital that links people to other groups.
Finally, QVL can have a different impact on the advocacy activities of a NPO. Kramer (2001: 375) notes that under contracting, ‘…some believe… [that among NPOs, there has been a shift] from advocacy on behalf of clients to organisational self-interest’, while governments may stifle advocacy by the conditions it places in contracts or by removing tax exemptions for what they perceive as ‘political action.’ (Casey & Dalton 2006; Hamilton & Madison 2007). Indeed, McDermott (2008:114) notes that in Australia, former Prime Minister Howard54 ‘saw no distinction between service delivery parameters and the reinforcement of desirable “social norms and values”’. Under QVL, the licensing provisions could include requirements limiting advocacy action, but in practice these are likely to be more difficult to monitor and enforce than under contracting once an organisation has gained its ‘licence.55 A contracting decision almost always has only limited transparency and ultimately can be defended on the grounds that people will differ in their judgements - but it is impossible to know what the judge is actually thinking. On the other hand it would be harder to take away the licence of a ‘commercial’ provider simply because members of the organisation had exercised their democratic rights. It is harder to discriminate against bodies that are essentially running a business, regardless of what other social activist activities they are involved in, although of course government could arrange to send in the ‘licensing police’ to ‘check’ all aspects of an organisation’s compliance.

A further difference arises from the closer relationship of providers to users under QVL. As we have noted, a provider can survive under QVL by appealing to a niche sub-group of users, and indeed action that government and contracting agencies see as undesirable lobbying may well be attractive to many potential users. However, there may also be limits as to how far advocacy and political action is ‘commercially sound’, even with a niche group of ‘customers’. For example, an organisation lobbying for better services for severely disadvantaged families may be attractive to users concerned with social issues, whereas an extension of this to advocate better treatment for refugee families runs a greater risk of alienating some clients.

Once again, as in the previous section concerning the behaviour of NPOs in relation to service delivery, we can see that while QVL systems may lead to NPOs reducing their activities aimed at broader social objectives, they also may give some NPOs greater scope to pursue these objectives than is possible under contracting.

8. Some Australian Evidence

This section will draw on Australian experience to illustrate propositions presented in earlier sections. We first briefly note some relevant points about the key drivers of Australia’s social, economic, and political distinctiveness; the history of QVL in Australia; and current interest in the use of QVL. We then examine a number of sectors in which QVL is being used or has been proposed.

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54 John Howard was Prime Minister from March 1996 until November 2007.
55 Under Medicare in Australia, the licence is essentially based on the individual practitioner’s qualifications and history of medical and financial integrity. At this time, it does not seem feasible that any government would revoke this on the basis of a doctor’s political statements.
8.1. Background

Smith & Lipsky (1993) argue that the function and form of NPOs in any nation derives in part from the form of the welfare state that operates in the nation. Much of Australia’s social, economic and political distinctiveness can be explained by two factors, the ‘harsh brown land’ and the convict origins of the nation, which continue to impact on the nation today. As with the US and Canada, Australia has a large land mass, with the opening of frontiers in recent centuries being an important feature of its development, and the adoption of a federal system of government as a natural response to the size and diversity of the land. As with Canada, the climate in much of the country can be harsh and unpredictable, and there are large areas with few inhabitants. Almost uniquely, however, modern Australia began as a prison colony.

On the one hand this geography and history has meant that government played a significant role in the development of the nation before 1900. This continued in the delivery of goods and services throughout the twentieth century with governments owning and operating many business enterprises, including banks, airlines, insurance companies, phone and electricity services. On the other hand, the prison and frontier elements of the nation’s early history have also led to a scepticism about government and a ‘healthy disregard for authority’, coupled with a belief in the importance of both individual and collective community responsibility. The analysis by Esping-Andersen (1990) showing three main types of Western welfare states classifies Australia as ‘liberal’ (ie. favouring limits on government) alongside the US, Canada, and other predominantly English-speaking nations. Castles and Mitchell (1990), however, argue that Australia has had a distinctive ‘worker’s welfare state’, with a unique mix of individualism and extensive economic regulation by the state, aimed at affecting the primary distribution of income to workers but providing only a residual social security system (Castles 1985).

Thus in Australia, the expectation for much of the twentieth century was that government should promote a social and economic system that ensured a reasonable minimum income and living standard for those who want to work and their families; that all people, wherever they live, should have a basic and relatively uniform level of essential services (including health and education); and that those ‘genuinely in need’ are given some help. Beyond that, however, individuals and communities must look after their own welfare. This contrasts both with Esping-Andersen’s ‘social democratic’ nations (which have a high level of state involvement) and with other ‘liberal’ nations such as the USA. As Smith & Lipsky (1993:17) note, ‘[at least] until the 1960s, America had relied heavily upon a decentralised system of social protection’, the ‘roots [of which] lay in cultural values, ethnic diversity, and political decentralisation.’

One outcome of the above situation is the high level of voluntary and third sector activity in Australia. Tiffen and Gittins (2004:246-247) compare eighteen developed nations in terms of the results from the World Values Survey showing the percentage of adults who are ‘members of voluntary organisations’ and ‘active members of voluntary organisations’. While the authors note a number of reasons as to why ‘we must interpret the data with caution’, Australia tops both lists, with the US second, well ahead of the others. Australia’s leading position is based on a high level of membership of sporting bodies, but aside from US membership of church organisations and political parties, it also leads most nations in all other categories. In particular, Australia leads all nations in membership and active membership of

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charity, education and professional organisations, the type of organisations that have been major providers of human services for most of Australia’s history since white settlement.\footnote{The first permanent settlement by Europeans in Australia was in Sydney in 1788. The Benevolent Society established in 1817 (and which still operates) is generally regarded as the first non-government charity in Australia.}

Under the impact of marketisation, however, a number of the distinctive Australian institutions (and some would say, traditions) have been removed or diluted in the last quarter-century, in a process effectively begun with the Hawke Labor government elected in 1983, and accelerated by the Howard Liberal-National (conservative) government (1996-2007). Indeed, in a number of human service sectors, Australia has led the way in marketisation and provides a valuable source of evidence on the implications of managed markets. In some sectors (eg. job search for the disadvantaged, child care), new programs and funding systems have been introduced that have meant a major rupture with the past and a transformation in how the service has been organised and delivered. In turn this has had a significant effect on the presence and behaviour of NPOs, FPOs, and government providers in these sectors. On the other hand, there has been some continuation of the older tradition of expecting government to take ultimate responsibility to provide basic services, and as some of the problems of the new marketisation become apparent (eg. corporatisation of child care, and a growing bureaucratisation of Job Network) there is a move to rethink some of the mechanisms introduced in the last two decades.

8.2. The Australian experience with QVLs

Lyons (1995) outlines the history of the development of QVLs\footnote{As noted earlier, Lyons uses the term ‘quasi-vouchers’ not ‘quasi-voucher licensing’.} in Australia focusing particularly on the sectors of child care, disability services, nursing homes for the aged, and home care services. He notes that they emerged during the 1970s and 1980s as a result of ‘interaction within the bureaucracy rather than ministerial initiative’ (Lyons 1995:127) or any explicit policy decision to use QVLs. He argues they grew incrementally driven by (i) a need to curb the growth of demand an expenditure (ii) strong Commonwealth (ie. national) Government policy bias towards targeting, especially among the powerful central coordinating departments, and (iii) institutional isomorphism whereby one department became responsible for administering a number of programs in which QVLs came to be used.

Australia has some interesting differences from the rest of the world in its use of QVLs. As Lyons (1995:130) notes with regard to the early development of quasi-vouchers:

‘It is this change, not privatisation\footnote{‘Privatisation’ is here used in the sense of ‘any shift of emphasis from the public sector to the private sector’ (Stilwell 2002:391) including the use of non-government bodies as providers or the use of private sector methods, rather than the narrower sense of the sale of government enterprises that is the more common use of the term in Australia.} which… [was] …the most significant development in the provision of human services in Australia during the late 1980s. It is a change which is closely associated with so-called targeting and means testing of income security arrangements…. It is likely that Australia has gone further than other countries in targeting its support for human service provision. It has done this by developing quasi-voucher arrangements.’

Changes since the above comment was made have further extended the role of QVL in some sectors with significant impacts on the profile of providers in those sectors. The child care sector in Australia is now based on QVL and this arguably has underpinned the change from a sector that was primarily based on community-based NPOs in the mid-1980s to one where there is substantial corporatisation of the sector with over 70% of places provided by FPOs and
the growth of a company (ABC Learning) that until recently was generally agreed to be the largest child care operator in the world. On the other hand, while QVLs are used as the major funding instrument in community care in many other nations - (usually referred to in that sector as consumer-directed payments) - Australia continues to use contracting in its major funding program for this service. Thus in Australia these two services have systems that are approaching opposite ends of the spectrum in regards to the use of QVLs, yet the Australian position in each service is at odds with common practice in most other nations.

In general in Australia, programs administered by the national government are more likely to use QVL than state government programs. Lyons (1995) suggests that this reflects a difference in the policy stances of national and state governments and their agencies over the last twenty years. It can also be substantially explained by the fact that the QVL programs are more likely to be open-ended in terms of eligibility - and therefore potentially costlier - while there needs to be reasonable portability across the nation for any benefits that are linked to individuals.

QVLs are now used extensively in Australia, and represent a major form of funding for human services in Australia, including for many of the more costly government programs.

8.3. Current interest in QVLs

This issue is of more than academic interest in contemporary Australia. First, the Productivity Commission (2002) has proposed that QVL should be used for the Job Network, although the recommendation has not yet been accepted. Second, while a number of nations use QVL for community care, Australia retains a predominantly contracting system, and there is a strong push from some consumers to introduce QVL for this service, especially from disability groups (eg. Hughes 2006) but also in aged care (Coonan 2008). Third, the industry structure that has emerged in child care and associated problems with the quality of services have been sources of significant concern and may not be sustainable. Finally, there are other major areas of government expenditure on human services that are substantially financed by QVL system - notably schooling, Medicare, residential aged care, and university funding for teaching - and it is important to scrutinise these systems for quality, efficiency, and fiscal reasons.

Thus there are pressures to introduce QVL in some service sectors, while at the same time governments and professionals have concerns about the cost and quality of services in some sectors that have made extensive use of QVLs over the last decade. Further, the extension of public subsidies for human services to more affluent and socially and politically powerful citizens over recent years means that there is a strong constituency for whom choice is very important and who want to control the use of public subsidies aimed at benefiting their family. From the perspective of government, a better understanding of the issues canvassed in this paper will enable it to make informed decisions about the impact of moving to a QVL in terms of the types of providers and the quality of services that might emerge. As Lyons (1995) notes, much of the development of these schemes has been ad hoc with limited prediction - or even post hoc appreciation – of the impacts they have. From the perspective of NPOs, it is important that they are able to understand the implications of moving into sectors using QVL and what it may mean for their mission, operation, and ultimate viability.

Once the Rubicon is crossed to QVL for any service, history shows that such a change can lead to a major shift in the profile and behaviour of providers, including the increased presence of

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60 In response to the Productivity Commission, van Dyke (2002) argues that the sue fo a QVL system would lead to wasted resources in marketing and more providers than are needed or efficient.
FPOs. The following examples do not necessarily show causality, since there are many other forces operating. They do however, give significant evidence of some link, and suggest some important research questions to examine in this field.

8.4. Some Human Service Sectors

Child Care

Prior to the 1970s there was no formal government financial support for child care in Australia, with long day care ‘…provided by a mix of philanthropic organisations and private businesses… 520 of the 560 day care services operating in 1969 were operated on a commercial basis’ (Brennan et al 2007:3). In 1972, the Commonwealth government introduced the Child Care Act which enabled it to make capital and recurrent grants to non-profit child care organisations. This led to the development of an extensive network of community-based neighbourhood centres operated by NPOs over the next decade. The move towards a QVL system began in 1985 when the Commonwealth restructured its model for funding child care ‘so that it was paid on the basis of the number of children enrolled in a service, not on the basis of the staff employed’ (Brennan et al, 2007:4). In 1990, FPOs became eligible for the assistance. Between 1992 and 2008, a series of decisions have been made (Brennan et al 2007:3-4; Lyons 1995:131) so that the current system consists of a means-tested Child Care Benefit plus an additional Child Care Tax Rebate (which can meet 50% of costs up to $7500 per child per year). A major change in the early 1990s was to remove the capacity to make capital grants to the NPO centres that had existed for twenty years.

Over the last twenty years, during which the QVL system was introduced and continuously expanded, there has been a major growth of FPOs in the sector and a substantial takeover by big corporates of child care in Australia. Table 1 (adapted from Brennan et al 2007:14) shows two major phases in the development of the pattern of ownership between 1991 and 2004. The first was from 1991 until 1996. In 1991, NPOs provided 52% of long day care places. By 1996, the number of places in NPOs had increased by 15%, but by then NPOs provided only 27% of places, because total places had increased by 120% and FPO places by 234%. This was a smaller share for NPOs of a much bigger cake, but there was still an increase in the number of places that NPOs provided. Then, in 2000, the Howard Government extended the Child Care Benefit, and ended the remaining operational subsidies for NPOs. Following these changes, there was an 18% increase in the total number of places between 2001 and 2004, with 89% of the growth going to FPOs.61

Associated with the growth of FPOs in the sector has been much concern about the effect on the quality of care, for example in the time devoted to children and the qualifications and experience of staff in corporate-run centres (Rush 2006; Press & Woodrow 2009 in press; Brennan et al 2007; Hill 2007). Most community NPOs and child care neighbourhood centres have retained a strong allegiance to quality care, with the community sector childcare peak body very active in defending the need for high service standards, in the face of more commercial concerns from corporate FPOs. The development of the sector is also complicated by the significant undersupply of places in some areas which gives providers (including NPOs)

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61 In addition, the corporatisation of the sector galloped ahead after 2000 with one company, ABC Learning, floating on the Stock Exchange in 2000 and engaging in a major takeover campaign that led to it increasing the number of places it provided in Australia by 1,435% (sic) between 2001 and 2005, and purchasing major companies in the US and elsewhere. For a range of reasons, however, this growth has not proved to be sustainable, and since February 2008 the future viability of ABC has been in question.
significant leverage over parents and dilutes ‘consumer sovereignty’. There has also been a clear example of corporate influence on government with the successful efforts by FPOs over the last 5 years to block the reduction of the child-to-carer ratio from 5 to 4.62

The child care industry in Australia thus illustrates some of the major propositions from earlier sections. For much of the 1970s and 1980s, childcare was substantially provided by locally-based NPOs. Then, despite the fact that there was an increase in the actual number of places provided by NPOs in virtually every year from 1991-2004, they now have a much smaller share of total places. FPOs now provide over 70% of long day care places after the introduction and continuous expansion of a QVL system based on individualised subsidies, periodic increases in both the value of the subsidies and the proportion of the target population that could claim them, and the end of capital assistance for NPOs. In this context, the FPO lobby has also been able to contain the capacity of the regulator to exert greater control over quality.

Residential Aged Care

The introduction of a nursing home benefit by the Commonwealth Government in 1963 ‘led to a massive growth in mostly for-profit nursing homes’ followed over the next few years by ‘many attempts by government to curb this growth’ by a variety of means (Lyons, 1995: 132). Two mechanisms used in this period were the provision of capital assistance and deficit-funding to NPOs, so that during the 1970s and 1980s, NPOs, especially large religious and charitable organisations, were able to establish their place in the sector. From the mid-1980s, as part of a strategy to stem rising costs, the government has gradually introduced a QVL system with the level of subsidy based on each individual resident’s level of need (as determined by government Aged Care Assessment Teams) rather than income or capacity to pay.

Table 2 shows that in 2005, FPOs provided 31.2% of residential aged care places in Australia in 2005. This sector is similar to child care in that (i) for a human service they are both capital intensive (ii) before 1970 most providers were FPO (iii) deliberate government policy in the 1970s (especially via capital and operational subsidies) led to NPOs predominating, and (iv) over the last twenty years, capital subsidies have been phased out and a QVL system introduced. With these similarities, why have the patterns of ownership developed so differently? In summary, it would seem to be a function, first of the limits that have been placed on co-payments in nursing homes; and second that the NPOs operating nursing homes have been larger, often national, organisations, and thus have been more able to compete with the corporate FPOs. Notwithstanding this, however, some NPOs have re-assessed their position and chosen to move their efforts and resources out of nursing homes into other sectors (eg. in 2007, Anglicare announced it would sell its residential centres to an FPO, although subsequently it was purchased by another NPO).

Community care

In Australia, government support in the community care sector is primarily via contracting, and the subsidised services are mainly provided by NPO and government providers. The major program is HACC; FPOs have only been allowed to tender for HACC services since 2005, and currently provide less than five per cent of places. As we have noted, this contrasts with many

62Most recently, in 2007, the NSW Government rejected the majority findings of a inquiry it set up and accepted the minority recommendations of the two FPO representatives to not reduce the ratios. In NSW, NPOs have supported higher mandatory staff-user ratios in child care (ie. more staff per child), one effect of which is that costs rise and profits fall.
other Western nations where QVL is widely used and FPOs have a major presence as providers, although concerns have been expressed about the development of consumer-directed care for the aged in other nations (Keigher 1999).

More recently in Australia, there has been the development of individualised aged care packages under a number of small programs, although government-appointed brokers play a key role in determining who will provide services under the packages. These packages are essentially QVL systems. In 2007, there were 1369 organisations that provided packages, of which less than 7% were FPO, so relatively few inroads have been made by FPOs in this sector, although it is early days in the development of these programs.

There is, however, a substantial presence of FPOs providing community care services. They dominate the unsubsidised sector where individuals with additional funds can pay for more hours than they have been approved. It also appears that some of these ultimately receive government funds, since there is sub-contracting by NPOs to FPOs, although there is only anecdotal evidence about its extent. The author is currently researching the providers of community care for the aged in two local markets in one Australian state, looking at both subsidised care (via contracting and QVL) and unsubsidised care.

Medicare in Australia

The Australian Medicare system provides universal coverage for basic medical treatment outside public hospitals. The system, which was first established as Medibank in 1973 and revamped as Medicare in 1983, is based on individual practitioners (doctors, physiotherapists, etc) obtaining a ‘provider number’ which entitles their patient to claim a rebate from government (with an extensive schedule of charges depending on the specific nature of the service as defined by the practitioner). In terms of a QVL system, the ‘licence’ is vested in the individual practitioner. With regard to the ‘subsidy’, a provider can choose to either (i) ‘bulk bill’ for some or all of his/her patients (ie. the patient signs a form and the doctor makes a bulk claim directly to Medicare for all such patients) or (ii) charge an additional co-payment whereby the patient must pay the full amount and claim the subsidy themselves. Under this system, an individual provider could work alone or in partnerships, or corporations can grow a substantial business and establish chains by employing practitioners with provider numbers.

In 2006-07, a large majority of medical practitioners were in private practice (eg, 63% of all general practitioners) while 73% of all services were bulk-billed (Medicare Australia 2007). Hence Medicare Australia is a QVL system where most providers are FPOs, but where practitioners do not claim a co-payment for nearly three quarters of the services that are provided.

There are also various grant and contracting systems with NPO specialist providers, such as Aboriginal Medical Services. While few have done it, these providers would appear to have the alternative option of employing medical practitioners with provider numbers and bulk billing their patients under Medicare. This would certainly give them greater autonomy from government, and possibly higher revenues by moving to Medicare.

Other Factors

The differing effects of history, politics and place on the profile of providers of a service are very evident in paid care in Australia. Tables 2-3 show the profiles of providers in each state in child care and residential aged care. While the data in the tables must be approached with
caution, especially if we want to compare the two sectors, they suggest some significant differences in the relative presence of NPOs and FPOs between states and service types. Both nationally and in every state and territory, FPOs are more prevalent in child care. There are also major differences between jurisdictions for each service, with the proportion of places provided by FPOs in aged residential care ranging from 11.8 per cent (Tasmania) to 43.5 per cent (Victoria), and the proportion of FPO providers in child care ranging from 26.2 per cent (NT) to 82.5 per cent (Queensland). There are also differences in the type of NPOs in each sector; over 30 per cent of aged care places nationally are provided by religious organisations, a group that has a negligible presence in child care. In part, these differences in the provider profiles are driven by local circumstances including the size, structure, and location of the target group and the history of NPOs in the state, and by the development strategies of major providers. But they also reflect differing policy and practice of state and territory governments, with for example, the licensing function in child care being carried out by state authorities.

9. The Way Forward

9.1. Some Tentative Conclusions

We here present some tentative conclusions based on the above data and analysis. These are necessarily tentative both because there is a need to develop a more formal model of the distinct effects of QVLs on NPOs relative to contracting, and a need to empirically test the propositions directly rather than, as has been necessary so far, to draw inferences from studies done for other purposes.

With regard to the presence of NPOs, there is a strong likelihood that FPOs will be more prevalent where QVL operates, but that (assuming the level of subsidy is a reasonably high proportion of the minimum amount required to provide the service) QVL markets can also create a number of opportunities for NPOs where they can identify and respond to niche needs. This can both ensure their continued presence and enable that those that wish to stay closer to their original social mission to do so. Further, in some sectors, much of the displacement of NPOs may be by small non profit-maximising FPOs. However, possibly dominating these effects is the importance of incumbency when the changes are introduced. If small NPOs dominate a sector when QVL is introduced and FPOs are admitted, it is less likely that NPOs will hold their position, given that large capital may be needed (as in child care and residential aged care) for physical assets or to achieve significant back-office economies of scale. One effect may be the development of stratified markets, with NPOs servicing less affluent clients. However, while NPOs could lose a significant part of their market share in a sector, they may at the same time increase their absolute level of activity if QVL leads to substantial increases in the level of funding for a sector through the involvement of corporate FPO providers and pressure of higher income and powerful people getting subsidies.

With regard to the behaviour of NPOs, QVL can allow for greater diversity between organisations, with the likelihood of a bifurcation between NPOs, as some become more commercial and others have an increased capacity to follow their own mission. An important factor in determining the extent to which smaller NPOs will go more commercial or stay with their basic mission is likely to be the role and strength of peak bodies in any sector. Further, under QVL, any movement to institutional isomorphism is likely to be with NPOs becoming more like FPOs than like funders compared to what happens under contracting. As with the

63 See notes on tables. There is also a different base for each table, with Table 2 showing the number of places managed by each type of provider and Table 3 showing the number of providers of each type.
impact of QVL on the presence of NPOs in a sector, there is likely to an increased encroachment of more commercial and private sector behaviour, but the possibility of greater freedom for those NPOs that wish to develop their own thing, especially where they do not have major growth ambitions.

With regard to the capacity of NPOs to pursue broader social objectives, the impact may be less about whether QVL changes all NPOs or whether certain types of NPOs will become more or less prevalent. Once again, there is a similar tale, in that the effect of QVL varies with the type of NPO and it may lead to some NPOs being less focused on social capital, but it also allows others to enhance their broader social impact as their social activities become a means of attracting clients and individual clients develop better networks and linkages.

9.2. Obtaining Empirical Evidence

None of the above is intended to be conclusive and the subject requires further research. While there is much evidence about the impact of contracting and of commercialism (including in QVL markets), very little research has been done on the particular effects of QVL on NPO presence and behaviour in mixed markets. Given that each situation is dependent on the nature of the service and on a number of locally-specific factors, it is difficult to empirically determine the specific effects of QVL markets. Ideally, we would need to have two alternative systems operating for each service and place from a green-fields start - and then compare a range of services to try to control for the impact of the particular characteristics of each service.

However, we can identify the sorts of study that may help to shed some light on these questions, bearing in mind the limitations of any study given that the outcomes in any sector do not simply reflect the design of the funding system and the structure of the markets, but at least partly reflect differences in the nature of the service, or factors of history, politics and place.

First, we can look at sectors where the change has been made, such as the child care sector in Australia and look at what has happened to NPO providers over the last two decades, including at different stages of the changes. A second focus of research can be on NPOs that operate in both types of markets, examining whether they operate differently in each market. In Australia, the focus would be mainly on the larger church-based bodies operating services across a wide range of fields such as residential and community care services for the aged, job network, and family support and homeless programs. A third focus may be to consider the same service in different government jurisdictions (by nation and state/province). An example would be to focus on the community care sector, comparing the Australian experience with its predominantly contracting regime with the experience of providers in other nations using QVL.

9.3. A Final Note

A first reaction may be to see QVL as an even greater threat to NPOs than contracting because it removes intermediate term guarantees of revenue, creates stronger forces for commercialisation, and increases competition from FPOs. However, under QVL there is also greater scope for NPOs to stay in the field and appeal to niches so that they can operate more as they want, including playing a stronger social role in their community.

In summary, NPOs are likely to get a smaller share of the cake, but it may be a bigger cake. And the cake under QVL can be many-layered, ranging from basic sponge to rich chocolate, with NPOs having greater choice as to which layers they want a part of.
### TABLE 1

**Funded Long Day Child Care Places in Australia, 1991-2004**

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Places</th>
<th>Proportion of Total</th>
<th>Percentage Growth from Previous Year</th>
<th>Percentage Cumulative Growth after 1991</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>NPO</td>
<td>FPO</td>
<td>Total</td>
<td>NPO</td>
</tr>
<tr>
<td>1991</td>
<td>39,567</td>
<td>36,700</td>
<td>76,267</td>
<td>51.9</td>
</tr>
<tr>
<td>1992</td>
<td>40,262</td>
<td>53,210</td>
<td>93,472</td>
<td>43.1</td>
</tr>
<tr>
<td>1993</td>
<td>42,777</td>
<td>61,375</td>
<td>104,152</td>
<td>41.1</td>
</tr>
<tr>
<td>1994</td>
<td>43,399</td>
<td>80,374</td>
<td>123,773</td>
<td>35.1</td>
</tr>
<tr>
<td>1995</td>
<td>44,566</td>
<td>99,909</td>
<td>144,475</td>
<td>30.8</td>
</tr>
<tr>
<td>1996</td>
<td>45,601</td>
<td>122,462</td>
<td>168,063</td>
<td>27.1</td>
</tr>
<tr>
<td>1997</td>
<td>46,294</td>
<td>136,571</td>
<td>182,865</td>
<td>25.3</td>
</tr>
<tr>
<td>1998</td>
<td>51,710</td>
<td>142,844</td>
<td>194,554</td>
<td>26.6</td>
</tr>
<tr>
<td>1999</td>
<td>50,589</td>
<td>139,737</td>
<td>190,326</td>
<td>26.6</td>
</tr>
<tr>
<td>2000</td>
<td>50,368</td>
<td>140,547</td>
<td>190,915</td>
<td>26.4</td>
</tr>
<tr>
<td>2001</td>
<td>61,248</td>
<td>132,561</td>
<td>193,809</td>
<td>31.6</td>
</tr>
<tr>
<td>2002</td>
<td>n.a.</td>
<td>n.a.</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
<tr>
<td>2003</td>
<td>64,255</td>
<td>147,390</td>
<td>211,645</td>
<td>30.4</td>
</tr>
<tr>
<td>2004</td>
<td>65,260</td>
<td>164,343</td>
<td>229,603</td>
<td>28.4</td>
</tr>
</tbody>
</table>

* - 2003 is growth from 2001

Derived from Brennan et al (2007), Table 3, p.14
### TABLE 2

**Aged care residential places in Australia and each state/territory,**  
Proportion of places by type of provider, June 2005*

<table>
<thead>
<tr>
<th>Type of Provider</th>
<th>NSW</th>
<th>VIC</th>
<th>QLD</th>
<th>WA</th>
<th>SA</th>
<th>TAS</th>
<th>ACT</th>
<th>NT</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Religious</td>
<td>32.5</td>
<td>17.2</td>
<td>43.7</td>
<td>33.6</td>
<td>28.6</td>
<td>38.4</td>
<td>23.5</td>
<td>55.6</td>
<td>30.4</td>
</tr>
<tr>
<td>Community-based</td>
<td>15.6</td>
<td>16.0</td>
<td>12.3</td>
<td>12.1</td>
<td>13.0</td>
<td>25.1</td>
<td>6.7</td>
<td>15.3</td>
<td>14.7</td>
</tr>
<tr>
<td>Charitable</td>
<td>19.8</td>
<td>6.0</td>
<td>14.1</td>
<td>15.5</td>
<td>26.2</td>
<td>21.8</td>
<td>47.9</td>
<td>17.4</td>
<td>15.8</td>
</tr>
<tr>
<td>Private-for profit</td>
<td>29.3</td>
<td>43.5</td>
<td>23.8</td>
<td>34.1</td>
<td>23.4</td>
<td>11.8</td>
<td>21.9</td>
<td>11.6</td>
<td>31.2</td>
</tr>
<tr>
<td>State/territory</td>
<td>1.4</td>
<td>14.6</td>
<td>5.3</td>
<td>0.6</td>
<td>6.6</td>
<td>2.6</td>
<td>-</td>
<td>-</td>
<td>5.9</td>
</tr>
<tr>
<td>Govt</td>
<td>1.3</td>
<td>2.7</td>
<td>0.8</td>
<td>4.1</td>
<td>2.2</td>
<td>0.4</td>
<td>-</td>
<td>-</td>
<td>1.9</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Type of Provider</th>
<th>NSW</th>
<th>VIC</th>
<th>QLD</th>
<th>WA</th>
<th>SA</th>
<th>TAS</th>
<th>ACT</th>
<th>NT</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>55,027</td>
<td>40,708</td>
<td>28,173</td>
<td>13,418</td>
<td>15,319</td>
<td>4,270</td>
<td>1,556</td>
<td>430</td>
<td>158,901</td>
</tr>
</tbody>
</table>

* Excludes multi-purpose services and flexibly funded services.


### TABLE 3

**Centre-based Long Day Care child care providers in Australia and each state/territory,**  
Proportion of providers by type of provider , 2004-05*

<table>
<thead>
<tr>
<th>Type of Provider</th>
<th>NSW</th>
<th>VIC</th>
<th>QLD</th>
<th>WA</th>
<th>SA</th>
<th>TAS</th>
<th>ACT</th>
<th>NT</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Community-managed</td>
<td>22.4</td>
<td>23.7</td>
<td>15.5</td>
<td>34.8</td>
<td>51.2</td>
<td>48.7</td>
<td>68.4</td>
<td>73.8</td>
<td>25.7</td>
</tr>
<tr>
<td>Private-for profit</td>
<td>77.6</td>
<td>64.6</td>
<td>82.5</td>
<td>62.5</td>
<td>46.5</td>
<td>29.5</td>
<td>31.6</td>
<td>26.2</td>
<td>71.0</td>
</tr>
<tr>
<td>Government **</td>
<td>na</td>
<td>11.7</td>
<td>2.0</td>
<td>2.6</td>
<td>2.3</td>
<td>21.8</td>
<td>-</td>
<td>na</td>
<td>3.3</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

| Total providers      | 1,938 | 913  | 1,197 | 531  | 258  | 78   | 98   | 65   | 5,078 |

* The Productivity Commission (2006:14.13) notes that its data on child care services by provider type ‘needs to be interpreted with care because the scope of data collection varies across jurisdictions’.

** Includes local government owned services, but excludes Australian government supported services.

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