

# *Public Services and Blurring Sectoral Boundaries: An Introduction*

Sectoral boundaries are blurring as governments at every level rely more and more on private markets to deliver services. The reasons for this shift are as much political as economic. The shift toward privatization is generally explained with economic arguments that stress costs and benefits, efficiency, and program management. However, public officials' current romance with the market "is really a watershed about governance, the uses of power in society, and the boundaries between public action and private concerns."<sup>1</sup>

Some local public services financed by states and localities have long been contracted out to private providers. Building of roads and construction of schools are examples. Other services like child welfare, home health care, and youth services have been provided by both non-profit and for-profit providers. Others, such as prisons and fire services, are only rarely provided by a nongovernmental unit of any kind.<sup>2</sup> However, no public service function seems immune to privatization. The current environment reflects an increasing interest in market solutions that has encouraged outsourcing and competition, even in areas rarely considered before. In order to reflect on the size and direction of shifts in the provision of services and also to examine the trends and possible consequences of these shifts, this study limits itself to welfare-to-work services—a service area only recently experiencing change as a result of the mandates of new federal welfare reform legislation. This focus will establish a baseline from which to compare alternative arrangements for service delivery.

## Devolution and Welfare Reform

Devolution, both from the federal government to the states and from the states to county and local governments, provides a unique opportunity to observe sectoral changes in delivery of public services. Most states and localities have been seizing the opportunities provided by a loosening of federal mandates, responsibilities, and authority to restructure the arrangements for provision of services.<sup>3</sup> Nowhere have the changes in organizational arrangements been more dramatic than in the welfare reform and work force development systems, where they were catalyzed by the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) of 1996, the welfare reform act.<sup>4</sup> As a consequence of this legislation the new Temporary Assistance to Needy Families program (TANF) requires states to move increasing percentages of their welfare caseloads from public assistance to employment. States were to have placed 25 percent of their welfare clients in work by 1997 and 50 percent by 2002, or they would risk losing federal funding.<sup>5</sup> This has increased states' investment in job readiness, work experience, and direct job placement activities. TANF also eased federal restrictions on the use of for-profits, allowing local governments increasingly to expand the role of the private sector in meeting their needs in technology, systems management, training, and placement.<sup>6</sup> Around the country provision of services is being restructured, with case management, assessment, referral, job readiness, and placement organized and provided in new ways.

Many jurisdictions have long used local nonprofits—community-based organizations (CBOs) among them—to provide job training, job readiness, and placement activities under U.S. Department of Labor (DOL) programs funded by the Job Training Partnership Act (JTPA). Now, however, there is a dramatic increase in the use of private contractors—especially a few large organizations with experience in human services.<sup>7</sup> These large national for-profit corporations are playing increasingly dominant roles, and the effects of their participation are not yet well understood.

## Goals of the Research

This report is intended to shape the discourse about the blurring of sectoral boundaries and the changing role of government and to identify

the forces driving the particular shape and response of public and private organizations to these pressures to compete. I set out to assess the changes in the ways states and localities contracted out the provision of public services and to evaluate the potential impact of these trends on services, citizens, and governance. Since competition among the sectors may be inducing changes in the structure and behavior of public, private, and nonprofit organizations, my research also investigated potential shifts in the missions, management, strategy, and capacity of competing institutions. These changes may affect the success of individual organizations in this environment, but they are also likely to affect the capacity of a multisectoral service sector to meet a set of highly diverse needs of a modern urban society.

I undertook a “reconnaissance mission” in the form of a series of case studies in a single service area. Welfare reform challenged states to redesign delivery systems to move large number of clients from welfare to work quickly. While this analysis relies principally on four sites contracting for welfare-to-work services, the observations may have relevance in other jurisdictions and service areas. The insights gleaned from the study of a single service area in strategically selected sites should strengthen a set of hypotheses about how these contracting efforts are likely to alter the role and capacity of each sector to provide public services. A larger national survey would be necessary to determine with certainty the effects across many different service areas, and none has been conducted to date.<sup>8</sup> Even so, some interesting hypotheses are beginning to emerge, painting a picture of shifting sectoral relationships and an altered environment for public and nonprofit agencies.

The chapters that follow address four major questions. First, how significant is contracting out as a form of providing public services? Second, what are the major ambitions of state and local governments when they outsource their welfare-to-work efforts, and how have they designed their delivery systems to meet their objectives? Third, how have both the nonprofits and the for-profits been meeting the challenges around the country? Fourth, what are the risks and challenges when the private sector competes in these markets?

## Designing the “Reconnaissance Mission”: Methodology

I was particularly interested in investigating the effects when private for-profit contractors were part of the mix in an implicitly competitive ser-

vice sector. In the jurisdictions chosen for the study, the organization of service delivery to welfare clients is undergoing significant restructuring, and the number and character of contractors for serving TANF clients have changed. These jurisdictions have introduced innovations in the provision of services, particularly competition among vendors from each of the sectors, and are working with new kinds of contracting arrangements—especially for selecting and remunerating contractors. My goal was to begin to assess the motivation, strategy, and potential effects of the introduction of market forces on organizations, clients, and governance.<sup>9</sup>

Four jurisdictions met the criteria: San Diego, Milwaukee, New York City, and Houston (see box 1-1).<sup>10</sup> They represented different models of service delivery, but all included a mix of providers. Interviews were conducted in each site with current contractors (public, private, and nonprofit), public officials with significant responsibility for the design and management of the new systems, a selection of subcontractors or previous contractors who had lost out in the most recent contracting period, opinion leaders, and some researchers studying aspects of the transitions. Public documents, including contracts, newspapers, requests for proposals (RFPs), company websites, and published reports, were reviewed. Since each jurisdiction is in a different stage of implementation—some completing their second round of contracts and others still in the first round—sites could not be compared on the basis of performance. The findings below, therefore, do not speak to the ultimate effects of these arrangements on the jurisdictions' success in reducing costs, improving efficiency, or enhancing the long-term well-being of their clients, but instead suggest their likelihood of doing so and identify researchable questions about likely consequences.

Presumably, the traditional motivation, behavior, and practices of for-profits, nonprofits, and public agencies would change as a result of competition and market pressures. Indeed, the study showed that there is more variation in organizations *within* the sectors than *between* them. Size and experience matter. A large nonprofit like Goodwill in New York looks more like some of its private-sector competitors than some of the smaller CBOs.

Market forces appear to be simultaneously inducing favorable creative adaptations among some innovative nonprofits even as they have threatened the viability of others. Further, increased contracting, especially to large organizations, changes the role and capacity of govern-

ment, threatening accountability and responsiveness to groups with special needs even as it relieves local government of other roles it has traditionally performed poorly. Thus I was interested in how government agencies have adapted to their altered roles.

## When the Private Sector Competes

This book reports the findings of interviews with major players and observers of these changes in the provision of welfare services. The interviews showed how competitive contracting arrangements have changed the ways vendors and government agencies serve their clients. Changing the roles and behaviors of providers from all three sectors influences the character and quality of governance and therefore warrants close monitoring. This reconnaissance mission is not the last word on these issues, but these initial observations may identify the areas where public officials, policy analysts, and advocates need to maintain considerable vigilance.

The observations from my reconnaissance reported in the following chapters support several conclusions. The competitive contracting environment has had mixed results. Some of the market incentives have worked in the expected direction: in a number of nonprofits increasing innovation has improved the organization and performance of their services. At the same time, both for-profits and nonprofits are quickly draining talent and capacity as they compete for experienced executives from government and from one another. Substantial resources are necessary for local governments to be smart buyers and good contract managers. Adequate accountability and contract monitoring functions require far greater human capital and expenditures than are typically expected or budgeted for. Valuable and worthy nonprofits are becoming more businesslike; some have even formed for-profit subsidiaries. However, they also shows signs of “losing their souls” in their capitulation to market imperatives. Still others risk extinction. Contracting out and the competitive environment it spawns are clearly no panacea. New delivery approaches bring new challenges. For all the improvements in performance that they promise, they raise troubling questions about quality and accountability. The trends are unlikely to reverse themselves, but studying the problems can help design a midcourse correction.

The lessons in this study are meant to sound a warning and to induce a productive response. Scholars and practitioners need to develop a

**Box 1-1. Overview of Contract Characteristics in Four Cities****Houston**

*TANF client placement:* Clients are assigned to one of 30 career centers by zip code.

*Providers and sites per provider:* Six contractors each with multiple career centers.

*Services provided to TANF clients:* Centers are assigned TANF clients; receive case management services including assessment, employment planning, job readiness and job search; refer clients for intensive job and basic skills training and on-the-job training.

*Bidding process:* Request for proposal.

*Contract structure and measurement parameters:* Cost reimbursement: Each contractor must achieve certain levels for eligible served, clients receiving continued service, clients entering employment, and clients employed above minimum wage.

*Level of subcontracting:* Relatively little.

**Milwaukee**

*TANF client placement:* TANF clients are assigned to one of six geographic regions, each with a sole provider.

*Providers and sites per provider:* Five contractors, all serving a single region except one that has received two regions.

*Services provided to TANF clients:* Contractors complete eligibility determination and provide complete services all the way through job training and placement.

*Bidding process:* Request for proposal.

*Contract structure and measurement parameters:* Pay for performance: Contractor must achieve and can receive bonuses for achieving an entered-employment placement rate, average wage rate, job retention rate, available health insurance benefits, full and proper engagement, and basic education/job skills activities; two optional measurements (faith-based contracts and basic education/job skills attainment) may be substituted for the bonus portion of two of the above categories.

*Level of subcontracting:* Extensive.

## New York

*TANF client placement:* TANF contracts are referred by Human Resources Administration (HRA) first to a Skills Assessment and Job Placement Center (SAP) contractor. If still without employment HRA will refer client to an Employment Services and Job Placement Center (ESP) contractor.

*Providers and sites per provider:* Five contractors with the SAP contracts; 12 contractors with the ESP contracts.

*Services provided to TANF clients:* SAP contractors receive TANF clients and provide skills assessments and services through preliminary job placement centers.

ESP contractors are referred clients who are not placed by the SAP contractors; they offer more intensive employment services and job training and placement.

*Bidding process:* Negotiated acquisition process.

*Contract structure and measurement parameters:* Pay for performance: SAP—payment is given for assessment, engagement in employment activities, job placement (higher rate for 30+ hours), with a bonus given for “high” wages and 90-day placement.

ESP—A percentage of base rate or a flat fee is paid for placement and 90-day retention, while a higher flat fee is paid for “high wages,” left welfare, or placement for 180 days.

*Level of subcontracting:* Very little for SAP; extensive for ESP.

## San Diego

*TANF client placement:* TANF clients are assigned to one of six geographic regions, each with a sole provider.

*Providers and sites per provider:* Two contractors run single regions, while both county officials and Lockheed Martin each run two regions.

*Services provided to TANF clients:* Centers are assigned clients; they handle all case-management duties including appraisal, assessment, and job search training; if clients do not succeed in finding employment, they are referred to a work placement network.

*Bidding process:* Request for proposal.

*Contract structure and measurement parameters:* Pay for performance: Certain amounts are paid for participant engagement, active caseload, 30-day employment, and 180-day employment.

*Level of subcontracting:* Very little.

more nuanced and sophisticated set of expectations about the costs and benefits of increased market arrangements for service delivery. Harnessing the virtues of the market will require more, not less, government management and oversight. Government's reliance on the private sector may have grown faster than its ability to manage it.<sup>11</sup> Difficult trade-offs are inevitable.

The study's findings should also serve as a warning to nonprofits whose future is increasingly tied to government contracts. High-performing, mission-driven organizations will have to change to remain relevant. New and blurring boundaries require new capacities, more innovation, and new kinds of collaborative relationships. The seductiveness of large government contracts and a desire to make a difference in a reengineered human services industry must be tempered by a balanced assessment of mission and capacities. Nonprofits differ among themselves as much as or more than they differ from their for-profit competitors. Each type brings different capacities, experiences, and comparative advantages. A commercialized service environment places new demands on all participants and, indeed, changes the likely success of many. Nonprofits have held a unique place in the civic infrastructure. This study thus pays particular attention to the effects of the changing environment on these critical social institutions.

The next chapter begins by placing the recent developments in context, first by reviewing the principal concerns that drove this study and then by describing the classic privatization debate that represents the foundation on which most rationales for government contracting rest. Reviewing what existing survey data show about the extent of contracting in subnational jurisdictions establishes the scale of recent changes. Chapter three explores the motivations of each of the study's jurisdictions for restructuring its delivery system, the nature of the changes made, and their expectations for performance. Chapters four and five explore the experiences of nonprofits and for-profits as they answer the call to do government's business under welfare reform. Chapter six offers some reflections about what the reconnaissance revealed and suggests some caveats about the future.