Avoiding the Pitfalls of Privatizing Social Services

By Stuart M. Butler, Ph. D.

The extensive analysis of privatization undertaken in recent years indicates clearly that different methods of privatization are required for different situations. While high-quality and economical services may be delivered using one method, another method may lead to disappointing results — or even to more costly and poorer quality services than those of government provision. For example, the British experiment with selling public housing to tenants has been highly successful in social as well as in economic terms. By contrast, the U.S. experience with contracting out the management of public housing to private firms has in many instances led to high costs, corruption, and dismal conditions in housing projects. Simply turning over functions to the private sector is not enough: the method of privatization must be carefully chosen if the expected results are to be realized.

The U.S. experience provides an important case study in the pitfalls of using the private sector to deliver social services. In particular, it highlights the problems associated with the strategy of contracts between the government and private bodies for the delivery of social services to low-income individuals. The experience also indicates that any government intending to use the private sector to replace pure government provision needs to give close attention to the political and social dynamics involved.

Social Services in the United States

The U.S. has a long history of providing basic social services through private sector organizations. These organizations take various forms, some being purely groups of volunteers. Quite often they are associated with a church. Many churches in the U.S., for instance, operate food and shelter programs for the homeless. In other cases they are nonprofit organizations operating under contract with the government to serve certain categories of individuals. For example, most employment training and special education programs for disadvantaged people are run by nonprofits under contracts with the government. In other instances private profitmaking companies deliver the services under contract. Some educational and training services are delivered in this way, as is most subsidized low-income housing. And in other cases the consumer of services receives a voucher earmarked for certain services, and he or she may use that voucher to purchase services from the private sector. The largest voucher program in the U.S. is the Food Stamp program. In this program families receive coupons which can be cashed in for food at most food retailers.

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Problems with Contracting

Most of today's largest social service programs delivered by contractors were established in the 1960s, under the so-called Great Society programs created under the presidency of Lyndon Johnson. The basic mechanism of the Great Society was to raise finance at the federal (i.e., national) and state (i.e., provincial) levels and use this money to fund services delivered by private professional organizations at the local level. The regulations for determining the services to be provided, and the obligation for monitoring the providers, rested with bureaucracies at each level of the government – federal, state, and local. The same basic structure continues today.

In recent years there has been rising concern among privatization experts in the U.S. regarding the dynamics associated with contracting for social services. The general point is made that although spending on services has risen dramatically, the U.S. poverty rate has changed little during the last 25 years – with variations seemingly dependent far more on the ebb and flow of the national economy than on the expansion or contraction of social service programs. It is also noted that the U.S. currently spends about $150 billion on anti-poverty programs for about 30 million poor Americans, or $20,000 per year in income support and services for each family of four below the poverty line. If the money had simply been given to each family, rather than funnelled through the social service system, the income of that family of four would be more than $5,000 above the poverty line. Yet poverty persists.

The reason this spending on services has not substantially improved the condition of the poor is that the growth of contracting since the 1960s has led to the development of a huge professional social service industry. This industry "crowds out" less costly alternatives, distorts the traditional mission of America's nonprofit organizations, and uses political pressure to expand programs that enrich the industry itself rather than serve the best interests of the poor.

Government Requirements. This happened, paradoxically, because the government sought to use the contracting process to assure the highest quality, professional services for the poor. To achieve this worthy goal, the government generally made the allocation of grants dependent on an organization indicating a real need for services and showing that it had a qualified staff to provide the services. But such apparently reasonable conditions have had a profound effect on the delivery of social services in the U.S. Most important, once-independent and community-based social service organizations have become creatures of the government. By 1980, according to Lester Salamon and Alan Abramson of the Urban Institute in Washington, D.C., some 58 percent of the revenues of America's nonprofit social service organizations was coming from the government.[1] Salamon and Abramson note, as have other scholars, that this close relationship with government has caused most groups to alter their activities to comply with the funding requirements of government programs.

In addition, the Urban Institute scholars explain, the regulations accompanying contracts has led nonprofit organizations to professionalize their staff, shedding many "uncredentialled" volunteers and replacing them with paid and "credentialled" professional

1 Lester Salamon and Alan Abramson, *The Federal Budget and the Nonprofit Sector* (Washington D.C.,: The Urban Institute, 1982), p. 44.

service providers. Thus the net effect in many instances is that the government now pays for services that were once provided by volunteers or by organizations funded by voluntary contributions – the antithesis of privatization.

Were this professionalization of social services to have produced better services it might be said to be good value for money expended. But there are many reasons to conclude that services may have, on the whole, fallen in quality while rising rapidly in cost.

Erecting Barriers. One reason is that the professional private social service providers are not passive in the process of drawing up regulations to determine who is qualified to provide services. Like most professions and guilds, social service providers have a financial interest in convincing the public that they alone are capable of delivering a service, and that lower cost, "unqualified" alternatives are unsuitable. To reduce even the possibility that nonprofessionals might be selected, professional organizations press the government at all levels to erect licensing barriers against their competitors. As sociologists Peter Berger and Richard Neuhaus explain,

> Through organizations and lobbies, professionals increasingly persuade the state to legislate standards and certifications that hit voluntary organizations hard, especially those given to employing volunteers. The end result is that the trend toward professional monopoly operates in tandem with the trend toward professional monopoly over social services. The connection between such monopoly control and the actual quality of services delivered is doubtful indeed.[2]

Moreover, this pattern has a disturbing effect on the population supposedly being served. For one thing, community institutions that once bound low-income neighborhoods together become pushed aside by professional groups with few real links to the community. This weakens the fabric of the neighborhood, making it more likely that poverty and blight will spread. For another, the financial incentive of the professionals is to convince people that they need services and that these cannot be provided from within the community itself, and then to lobby the government for more money for professional groups to deliver these "essential" services. The result is that low-income people are persuaded that they are unable to function independently and are persuaded instead to become increasingly dependent on government-funded services for their daily existence.

Worse still, the professional social service industry and its academic offshoots have become the primary source of research to indicate the alleged need for services and by which to evaluate the services provided. The political process relies heavily on this research to design programs. The thrust of this industry-generated research is predictably monotonous: there are always more problems that need to be solved than were ever imagined; if programs have failed it is because more money is needed; and the only way to solve a problem is to contract with a professional organization.

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2 Peter Berger and Richard Neuhaus, *To Empower People* (Washington, D.C.,: The American Enterprise Institute, 1977), pp. 36-37.

Stifling Local Groups. The incestuous and monopolistic nature of the social service industry, observes neighborhood expert Robert Woodson, has been to suffocate indigenous organizations in poor communities – organizations that routinely outperform the professionals in cost, quality, and appropriateness because they are part of the community itself and thus have the incentive to provide the best possible services at the lowest cost. By contrast, the nonprofit and for-profit professional organizations funded under contract by the government, constitute

> .... a seller's market in that professionals themselves decide when, to whom, and how to serve. The result too often is the paradox of careless care....Since it is the professionals who control the criteria of professional success and the definition of its category of clients and their needs, professional services can survive any malfeasance and continue in business, unlike a friendship, a family, or even a true market enterprise. Professionals themselves determine whether they have succeeded or failed and, if the latter, what the remedy should be.[3]

This dynamic is seen continually in the U.S. One example is day care. For many years the professional day care industry – nonprofit and for-profit organizations – has persuaded state and local governments to introduce a stream of measures to regulate the provision of day care services. The ostensible aim is to protect children and improve quality. But in many instances the impact is not to improve care in any measurable way but simply to increase the number of providers for each group of children and to require more extravagant and costly facilities. The net result has been that less formal neighborhood day care centers are being driven out because they lack the funds or the paper qualifications to comply with regulations.

The professional day care providers took the next step along a now-familiar road a few years ago by publishing surveys alleging a shortage of day care in the U.S. (by which they meant, of course, a shortage of regulated professional care) and a supposedly shocking amount of unlicensed care (that is, care by neighbors, relatives, and the like). Their solution? An enormous new federal program to distribute money to state and local governments for them to contract with *licensed* day care centers to provide services.

Shutting Out Competition. The same pattern can be seen in many other examples, from job training to health care, and from education to housing. In each case the contracting mechanism is taken over by the profession under contract and becomes a device to shut out competition and secure a regular source of revenue. The customer is not the consumer of the service but the government, and so it is the latter, not the former, who must be satisfied. Social service contractors also have become masters of the political process, building public support to expand programs when money is plentiful and new problems are identified, and to block legislative efforts to end programs when money is scarce or results are disappointing.

3 Robert Woodson, "Helping the Poor Help Themselves," *Policy Review*, No. 21 (Summer 1982), pp. 85-86.

A Checklist for Successful Privatization of Social Services

The sorry history of contracting for social services in the U.S. should cause would-be privatizers to pause before assuming that simply turning over services to the private sector is a guarantee of success. Officials or legislators considering such a move should recognize that social services really are no different from commercial services in that they exhibit the same consequences of monopoly and other forms of provider control. Yet officials who instinctively would turn down a commercial firm requesting a regulation to restrict competition routinely assume it must be in the public interest to "improve quality" by reducing competition in social services. Officials who champion the consumer in the commercial sector routinely ignore consumer choice in social services. It is only by recognizing that the dynamics are essentially the same whatever the sector that an effective privatization strategy can be developed for social services.

Fortunately the U.S. experience indicates how to design such a strategy. While the simple contracting model has serious deficiencies, other forms of privatization, and variations of contracting, have been highly successful. It is possible, in fact, to assemble a checklist, based on the U.S. experience, to guide national or local levels of government in other countries considering the privatization of social services.

1) Wherever possible, use vouchers rather than contracting as the primary tool of privatization.

Vouchers place the control of services into the hands of the consumer. The provider of a social service therefore, is forced to pay close attention to the desires of the consumer, and to compete for his "business," rather than to satisfy the desires of the government. Food Stamps (vouchers for food) have been highly successful in the U.S. They are a very efficient method of providing the poor with the financial power to buy food in the open market. There is no vast professional social service industry to deliver food to the poor, and hence no lobby to press for regulations to micromanage the meals of poor Americans. Low-income Americans buy food in the same retail outlets as anyone else, at the same prices, and they have the same incentive as anyone else to demand the best quality at the best price.

Needless to say, vouchers are strongly opposed by the social service providers who rely on government contracts. Vouchers for food in the U.S. were a part of the Great Society programs of the 1960s, and so were introduced before the growth of the professional organizations spawned by other Great Society programs. But vouchers for day care services have been bitterly fought by the professional day care providers, just as housing vouchers are opposed by housing contractors and education vouchers by teachers and administrators in the U.S. public school system. Of course that very opposition from monopoly providers is precisely why consumer-empowering vouchers are so important as a privatization tool.

Vouchers also are surprisingly versatile. Despite opposition, they are used in the U.S., usually at the state or local level, for such services as job training, special education services for children with learning disabilities, housing, day care and even technical assistance for community groups engaged in economic redevelopment. In each case the consumer of the service receives funds that can only be used for a certain purpose, and is relatively free to "shop around" for the best combination of quality and price.

Admittedly, vouchers do not preclude manipulation of regulations by the social service providers. Normally there are some regulations governing the standard of service or quality of product that can be purchased with a voucher. Day care vouchers normally carry the restriction that only licensed services can be purchased. Housing vouchers can only be used for units where a certain level of quality is maintained. Nevertheless, the experience with vouchers is that such regulation is less severe. There are two chief reasons for this. First, voucher holders tend to resist being denied the same range of choices as other individuals when the providers are the same. And second, because the providers in a voucher program are not routinely dealing with the government, or dependent (usually) on the government for the bulk of their income, they have less opportunity or incentive to press for exclusionary regulation.

2) When contracting for social services, wherever possible contract with an organization from within the community being served.

Vouchers are not always an available option. In some cases the client or the type of service makes vouchers technically unattractive. For instance, a pure voucher program may not make sense in providing shelter and medical services to a seriously mentally ill homeless person. But officials still should be skeptical in general of the argument that the consumer is incapable of making an informed choice – the supposed ignorance of the consumer is a routine argument advanced by all professions seeking to secure a monopoly.

Vouchers may also be politically impossible to introduce, at least as a first choice, in fully privatizing a service already dominated by contracting. In this case the wiser strategy might be to propose modifications in the contracting process. A key strategy to reform contracting in the U.S. has been for the government to contract with organizations within the communities being served. The logic is simple. An organization from the neighborhood being served or, better still, formed of those being served by a government program has a clear interest in seeing the best possible services delivered at the best price (so that the same funds can serve more people). The U.S. experience suggests that local organizations tend to be more creative and adaptive to the local situation, rather than to stick to the government contract rule book, and that in very many instances they provide better services.

Of course a similar objection can be, and is, made against community-based service contractors as against vouchers: how can the low-income people be expected to have sufficient expertise to provide essential social services? And once again, as in the case of vouchers, this often turns out to be the argument that poor people are ignorant and incompetent. But in areas as diverse as adoption services, rehabilitation of young offenders, management of housing, day care, and education, non-professional community organizations often have dramatically outperformed professional service organizations. Even when community organizations lack essential technical expertise, a contract can allow them to obtain training or to assemble their own choice of technical talent – as the catchphrase goes among inner city groups, to "keep the experts on tap, not on top."

Although contracting with local community organizations, as well as using vouchers, normally incurs the wrath of the professionals, contracting is often easier to introduce politically than vouchers are. This is because such contracting appeals to organized groups within the affected community, while vouchers target individuals. By appealing to groups, community contracting builds a political base to organize public and political support for the reform. In the U.S. case, virtually every example of a switch from contracting with professionals to contracting with community-based organizations has been preceded by a political struggle in which the community groups have played a decisive role.

3) Deregulate social services.

As described earlier, regulations determining who can legally provide social services have been a device used by professional social service contractors to block competition from other providers. Thus steps to deregulate social services are crucial to assuring that a privatization policy, operating though vouchers or contracting with professional and/or community organizations, does not lead to an excessive reduction in competition. This does not imply no regulation, but simply that a government engaged in the privatization of social services should recognize that the pressure for anti-competitive regulation by powerful providers is just as intense, and possibly more intense, in social services as in commercial municipal services.

Conclusion

There is now overwhelming evidence that privatization can lead to considerable improvements in the quality and economic efficiency of delivering services to people. But as many privatization experts have pointed out, if privatization leads to private monopoly, whether it be through the sale of a telephone system or through a contract to collect garbage, the result actually may be a deterioration of service. The experience of social services contracting in the United States provides supporting evidence for this concern. Thus if other countries contemplate the privatization of their social services, they would be wise to take steps to insure that competition and consumer control is built into the privatization strategy.

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