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The Mythology of Privatization in Contracting for Social Services

States and municipalities have privatized services in an effort to improve their cost-effectiveness and quality. Competition provides the logical foundation for an expectation of cost savings and quality improvements, but competition does not exist in many local marketplaces—especially in the social services, where governments contract primarily with nonprofit organizations. As government increases its use of contracting, it simultaneously reduces its own public-management capacity, imperiling its ability to be a smart buyer of contracted goods and services. This article examines two questions about the privatization of social services based on interviews conducted with public and nonprofit managers in New York state: Does social services contracting exist in a competitive environment? And do county governments have enough public-management capacity to contract effectively for social services? The findings suggest an absence of competition and public-management capacity, raising the question of why governments contract when these conditions are not met.

Introduction

Privatization continues to sweep the nation as the federal government, states, and localities turn the production and distribution of goods and services over to nonprofit and for-profit organizations. Privatization involves “changing from an arrangement with high government involvement to one with less” (Savas 1987, 88). Contracting is the most widely used form of social services privatization and has been on the rise for more than four decades.¹ The passage of federal and state welfare reform legislation and a growing trend toward devolution has further stimulated its use by elected officials and agency managers, who seek less government involvement in private markets and service delivery.

According to its advocates, privatization promises better services at lower costs, but this promise depends on at least two conditions—competition and government capacity. In the words of a great champion of privatization, “the primary goal of any privatization effort is, or should be, to introduce competition and market forces in the delivery of public services” (Savas 2000, 122). Additionally, Savas (1987, 251) explains, “service-delivery options are essential. Total dependence on a single supplier, whether a government agency or a private firm, is dangerous.” Past literature and privatization practices define competition as a

market containing a range of provider alternatives from which government can decide who is best positioned to deliver the contract services with the highest quality, lowest cost, and greatest expertise.²

To reap the benefits of competition, government must be a smart buyer, a skillful purchasing agent, and a sophisticated inspector of the goods and services it purchases from the private sector (DeHoog 1984, 1990; Savas 1987, 2000; Donahue 1989; Salamon 1989; Morgan and England 1992; Milward 1994; Prager and Swati 1996; Wallin 1997; Johnston and Romzek 1999). This, Kettl (1993) argues, requires public-management capacity. Public-management capacity requires personnel with contract-management experience, policy expertise, negotiation, bargaining, and mediation skills, oversight and program audit capabilities, and the necessary communication and political skills to

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manage programs with third parties in a complex political environment. If an agency has personnel with these skills and experiences, then public managers can act as smart buyers in making contract decisions about what to buy and whom to buy from, and in evaluating whether they received what they purchased (Kettl 1993).

To understand the context of social services privatization, we should consider Milward's (1996) observation that the field of public management has ignored the realities of social policy and the constraints that public managers encounter as services are contracted out. The absence of clearly defined and measurable outcomes, long treatment time frames, and specialized expertise are factors that characterize social services management and delivery. These contextual elements are important considerations when exploring the management practices of government agencies and nonprofit organizations in the contracting relationship. New York state serves as the context for this research because of its long-standing system of social policy supports, its extensive use of contracting with nonprofit organizations for service delivery, and because counties share the responsibility equally with the state in providing services for needy residents, a mandate in the state's constitution. This article examines two key questions about the privatization of social services based on interviews conducted with public and nonprofit managers in New York state: Does social services contracting exist in a competitive environment? And do county governments have enough public-management capacity to contract effectively for social services?

The State of Privatization

Previous research suggests that as power and responsibility for public service delivery have devolved from the federal to state and local governments, public officials seek to reduce government size and costs while maintaining citizen access to high-quality services. To achieve these goals, they have chosen privatization. The arguments for privatization have emphasized a combination of reduced costs, improved service, increased management flexibility, specialized expertise, and decreased public monopoly inefficiencies (Bennett and Johnson 1981; Savas 1982; Morgan and England 1988; Donahue 1989; Salamon 1989; Kettl 1993; Smith and Lipsky 1993; Prager and Swati 1996; Goldsmith 1997).

Privatization may lead to cost savings in the areas of waste removal, some types of transportation (street repair, snow removal, etc.), towing, and data processing (Savas 1982; Goldsmith 1997; Donahue 1989; Chi and Jasper 1998; Franciosi 1998; Moore 1998). The evidence is less clear about the cost savings achieved by privatizing social services such as foster care, child welfare, domestic vio-

lence care, substance abuse treatment, homeless and emergency shelters, job training, HIV/AIDS services, Medicaid case management, and food pantries (DeHoog 1984; Schlesinger, Dorward, and Pulice 1986; Ostrander, Langton, and Van Til 1987; Savas 1987; Donahue 1989; Kamerman and Kahn 1989; Salamon 1989; Kettl 1993; Smith and Lipsky 1993; Kramer and Grossman 1994; Gibelman 1996; Moe 1996; Dudley 1997; Wallin 1997; Johnston and Romzek 1999). Privatization successes appear to depend on the specific types of services, the existence of highly developed and competitive markets, the specificity of the contract, and the ability to enforce accountability and evaluate program outcomes.

Each of the arguments for privatization is grounded in an assumption that competition exists. Even if it does, privatization supporters seldom acknowledge that contracting leads to additional public-management costs, such as³

- Developing program performance measures and evaluation tools
- Developing and maintaining management capacity to monitor and oversee contractors
- Developing competition in response to restricted market entry resulting from networked relationships between nonprofits, elected officials, and public agencies.

Proponents of privatization suggest the issue is less about public versus private provision and more about monopoly versus competition (Savas 1983). Borcharding (1977) argues from a public-choice perspective that a competitive marketplace produces goods and services efficiently, while monopolies in any sector breed inefficiencies. Schlesinger, Dorward, and Pulice (1986, 252) state that "the greatest potential advantage of a contract-based system rests in the ability to promote competition among private agencies." Prager and Swati (1996) warn that a lack of competition can diminish the gains normally achieved from contracting. Pack (1989, 3) notes that "competitive bidding is necessary to reveal the lowest cost producer," and this goal cannot be achieved in the absence of competition. And Donahue (1989, 78), a privatization skeptic, says, "without a credible prospect of replacement, it is hard to harness private capabilities to public purposes ... with meaningful competition being far easier to praise than to arrange." While DeHoog (1990) suggests the ideal contracting environment should have both competition among suppliers and buyers and the necessary resources to cover the many transaction costs involved in the contracting process.

Often when governments privatize, however, they also downsize their workforces. This is a logical and politically popular strategy: When third parties deliver more public services, the government needs fewer workers. Overdoing this downsizing, however, leads to what Milward (1994) refers to as the "hollow state."⁴ When governments reduce their workforces and rely more heavily on nonprofits for

expertise in providing public services, governments become more dependent on them for information and services and less able to manage contractors and enforce accountability.⁵ The General Accounting Office (1997, 17) found that “monitoring contractors’ performance was the weakest link in the privatization process.” Much of the scholarship about government’s privatization efforts, especially in the social services, suggests governments have been less than vigilant in monitoring and conducting oversight.⁶ Cutback management has taken its toll on public agencies’ capacity to oversee the work of their contractors.⁷

Social Services Contracting

Social services present a unique challenge for public and nonprofit managers. This policy area consists of programs with goals and outcomes that are not easily defined and measured, clients with varying degrees of tractable and intractable problems, and different levels of client motivation to receiving treatment. In addition, many social service programs require a level of continuous care. This continuous care can be difficult to achieve, however, because of variations in competition by geographic market and the high cost of entry into some service areas, such as residential treatment programs (Schlesinger, Dorward, and Pulice 1986). Legislative and funding lag times also adversely affect service implementation and delivery because funds may be allocated late in a legislative cycle, yet require program outcomes to be achieved based on a calendar-year service period.⁸ Given the rise in contracting with nonprofits, the costs associated with developing competition, and the complexity of social services, it is not surprising that contracting relationships “create serious public management and accountability problems for which public administration theory fails to prepare us” (Salamon 1989, 11).

Savas (1987, 206) notes that “a dearth of systematically collected, empirical data comparing the different service arrangements” exists for social services that have been privatized. More recently, there has been an increase in research on the government–nonprofit social service contracting relationship, but much of the work has been conceptual, prescriptive, and case specific rather than empirical and generalizable based on primary data collection. The empirical studies that have been conducted are summarized in table 1.⁹

There are several consistent findings across the empirical studies examining the government–nonprofit social service contracting relationship. These include a lack of competition, administrative capacity on the part of both actors—public and nonprofit—and performance measures; poorly defined and inadequately enforced accountability mechanisms; goal divergence between policies and imple-

mentation practices and procedures; and nonprofit dependence on public funds, which can lead to mission drift, deprofessionalization, and diminished service quality. Additionally, these studies find there are equity implications for clients as a result of strains in the government–nonprofit relationship that stem from a lack of information exchange and coordination and a failure to consistently deliver coherent messages about policies, programs, requirements, and expectations from government to its contractors and clients.

The New Structure of Social Services in New York State

New York state has a long history of being progressive in providing services to the disadvantaged, with its home-relief program being the largest in the country relative to need. It is one of the most populated states in the nation, and it spends more on Aid to Families with Dependent Children program benefits than any state other than California. New York is one of only seven states with a state earned income tax credit for low-income working families and one of only four states with a refundable earned income tax credit, and it has led the nation in contracting with nonprofit organizations for social services (Riedinger et al. 1999).

The state’s Department of Social Services (DSS) both directly administered and contracted out programs such as adoption services, child day care, emergency shelters, foster care, offender rehabilitation treatment, refugee services, youth centers, job training, and vocational rehabilitation through 12 years of the Cuomo administration. Long-standing contracts allowed nonprofit organizations to develop and nurture strong relationships with DSS agency managers and other elected and nonelected officials in the Cuomo administration.¹⁰ When George Pataki replaced Cuomo as governor in 1995, he completely dismantled the DSS, replacing it with the new Department of Family Assistance, which comprised two offices—the Office of Temporary and Disability Assistance and the Office of Children and Family Services. The reorganization allowed Pataki to say the state no longer had a welfare office, merely an office of temporary assistance. Pataki’s dissolution of DSS and the formation of the Department of Family Assistance shifted programmatic responsibilities to the Department of Health, Department of Labor, Office of Alcohol and Substance Abuse Services, Office of Mental Retardation and Developmental Disabilities, and Office of Mental Health.¹¹

The reorganization had several outcomes, three of which are directly relevant to this study. First, personnel who had developed long-standing relationships with nonprofit constituencies were downsized or reassigned to other agency

Table 1

Author(s)	Study site	Methodology	Findings
DeHoog (1984)	Michigan	Interviews, documents, and archival sources UA = Public managers	Lack of competition, program evaluation, and bureaucratic incentives; weak accountability mechanisms; bureaucratic resistance; politically motivated decision making; and lack of administrative capacity for contract management.
Bernstein (1991)	New York City	Interviews and documents UA = Nonprofit managers	Nonprofits (NPOs) see contracting relationship as a "game;" ambiguous accountability requirements; lack of public-management expertise; and politicization of the process.
Saidel (1991)	New York	Interviews and survey UA = Public and nonprofit managers	Funding and expertise interdependence; nonprofit political networks; goal divergence; and NPOs act as "constituency" and "clientele" to public agencies.
Smith and Lipsky (1993)	Massachusetts	Interviews, documents, and archival sources UA = State and nonprofit officials	Nonprofit dependence on government funding; survival and adaptation strategies and techniques by NPOs in response to decreases in state funding; and NPOs acting as agents of the state.
Smith and Smyth (1996)	North Carolina	Interviews, documents, and archival sources UA = Contracting participants	Lack of competition, performance measures, and formal accountability; and management based on trust, reputation, and long-term government-provider relationships.
Commons et al. (1997)	Maine	Client level performance measures UA = Agency reported data	Performance contracting shown to be positively related to indicator effectiveness and program measures.
Meyers et al. (1998)	California	Field observations, interviews, documents UA = Public agency employees; observations of worker-client transactions	Policy reforms are not fully implemented by street-level bureaucrats; agency-client transactions are poorly aligned with new policies; and equity implications-information and technical assistance to clients is incomplete and inconsistent.
Johnston and Romzek (1999)	Kansas	Interviews and documents UA = Public and nonprofit officials involved in contract	Lack of market competition and contract management capacity; service complexity; inadequate administrative accountability such as monitoring, performance measurement, and politicization of the contract process and relationship.
Alexander et al. (1999)	Ohio	Surveys and focus groups UA = Nonprofits	Survival strategies for NPOs—government funding dependence reduces nonprofit autonomy and decision-making authority; increased need to be financially and programmatically accountable; and mission and organizational character are threatened by need to become more "businesslike."
Beinecke and DeFillippi (1999)	Massachusetts	Interviews UA = Public and nonprofit officials involved in contracting relationship	Privatization does not replace the need for public management personnel and resources; and given a lack of competition and administrative capacity, a relational model should be used in managing contractors.
Chambre (1999)	New York City	Interviews, archival, and fieldwork UA = Eclectic	The AIDS epidemic gave rise to government development of service providers that led to a complex and fragmented delivery system in which there is redundancy among services.
Sandfort (1999)	Michigan	Interviews, focus groups, participant observation, and documents UA = Organizations involved in the contracting relationship	Examines collaboration between public human service providers and private agencies at the street level; organizational structure and social processes influence level and type of collaboration; and barriers to coordination between the two parties creates inefficiencies, conveys ambiguous messages to clients, and causes inaccurate information.

UA = Unit of analysis

bureaus. This reflected Pataki's belief that Cuomo had appointed individuals so far down within the agencies that the only way to remove them was to eliminate the DSS or move them to positions that required different types of expertise, thereby reducing public-management capacity. Second, agency-nonprofit relationships were disrupted at the state level, but not at the local level. Program responsibility and block grant funding continued to devolve to the counties under the 1997 New York State Welfare Reform Act, and therefore local networks remained intact. Not only did these efforts increase county officials' authority and responsibility for program funding and service delivery, but local government-nonprofit networks also grew. Third, new government-nonprofit relationships were developed

that restricted market entry and opportunities to those perceived as friendly to the Pataki administration.

This research expands our current knowledge and empirical base by focusing on the contract relationship involving public managers and nonprofit managers at the state and county level given recent welfare reform legislation and increased decentralization of authority, responsibility, and funding to counties.¹² Previous empirical studies have tended to focus on only one of the contracting parties rather than both, and they have not examined the contract relationship and how it has been managed since the passage of the Personal Responsibility and Work Opportunity Reconciliation Act in 1996. Specifically, the Temporary Assistance to Needy Families (TANF) program,

which replaced the existing Aid to Families with Dependent Children (AFDC) program, was largely responsible for going forward with social services privatization and substantial changes in the manner in which programs are implemented.¹³ The TANF legislation is more punitive with sanctions and work requirements than those imposed by AFDC, uses a broader range of financial incentives such as earnings disregards, and has resulted in greater management challenges for states and counties in policy enforcement (Schoeni and Blank 2000).

Finally, what makes this study different from prior empirical studies is that spending patterns in state and local social service offices have changed: Whereas welfare money was being spent largely on cash benefits, states now have greater discretion in spending block grant funds on services such as education, job training, child care, transportation, and substance abuse counseling.¹⁴ This is important considering that the programmatic and management focus of public social service agencies has changed from determining who is eligible for cash assistance to getting people into work opportunities while providing the necessary resources to help them become self-sustaining. To do this, states and their counties have had to change the manner in which they manage their agencies, programs, budgets, and contractors.

Methods

Unlike previous research studies on contracting, this study was guided using tenets of agency, stewardship, and network theory.¹⁵ Agency and stewardship theory were selected because they represent opposite ends of the management continuum, and network theory was used because of its growing importance in the field of public management, given that managers are involved in managing and overseeing networked relationships.¹⁶

In conducting this research, I administered a semistructured, 15-question interview instrument to a purposive sample of 12 county-level public managers,¹⁷ 11 state-level public managers,¹⁸ and 12 nonprofit executive directors.¹⁹ In all, 35 complete interviews were used in this analysis.²⁰ The interview instrument can be found in appendix A. Each of the individuals interviewed was involved in social service contracts in one of the five New York state counties selected for this sample during 1999. The number of contracts by county and representative program areas is denoted in appendix B. The interviewee characteristics are summarized in table 2.²¹ Each interview took approximately one hour and 30 minutes.²² The interviews focused on three themes: competition, public-management capacity, and reasons for contracting. Interviewees described the contract solicitation, evaluation, and award process, the number and quality of bids, the importance of competition, the

conditions under which competition is more or less important, and the extent to which contractors are managed and evaluated. Other interview questions focused on the role of coordination, incentives, sanctions, information exchange, accountability measures, monitoring and oversight, and the public-management values that underlie contract-management practices.

The interviews were tape recorded, transcribed, and coded based on interviewee responses. The coding was guided by the theories identified and involved memoing and concept mapping, techniques designed to avoid interjecting subjective bias by the researcher. In addition, both techniques contribute to the sorting of some codes and the integration of others.²³ The data were analyzed using *Ethnograph* v. 5.0.

A number of contract documents, government reports and audits, news sources, and organizational materials were analyzed to validate interviewee responses. These materials are listed in appendix C. They were also used to examine the extent to which contract documents, agreements, processes, award decisions, and management controls were consistently used across service areas, agencies, and managers. Reviewing these documents provides baseline data on reliability from which we can generalize across interviewees regarding the consistent implementation and use of contracting and the corresponding management practices employed across public social service agencies in New York state.²⁴ Finally, different data sets assembled by 40 percent of the nonprofit organizations and 60 percent of the public agencies were used to understand capacity levels, contract performance, and reporting requirements. Each of these sources of information, interviews, content analysis of archival and secondary document sources, and analysis of existing data sets was used to triangulate the data and to minimize threats to validity.

New York state serves as the research site for this study because it has consistently used contracting as a vehicle for service implementation, and it is one of only 12 states in which counties have responsibility for federal programs. The state is one of only four states to “tap ... federal funds to ‘supplant’ state spending” (Nolan 2001),²⁵ and it is frequently cited as one of the best examples of a state in which

Table 2 Interviewee Characteristics

	Male	Female	Education	Age ¹
State public managers	7	4	6 Bachelor's only	3 30–39
			5 Some graduate work	5 40–49
				3 50–62
County public managers	5	7	9 Bachelor's only	8 40–49
			3 Some graduate work	4 50–62
Nonprofit executive directors	7	5	1 High school	2 30–39
			7 Bachelor's only	8 40–49
			4 Some graduate work	2 50–62

¹Age categories for purposes of clustering are 30–39, 40–49, and 50–62.

counties provide general assistance as a result of a state constitutional mandate (NACo 1997).²⁶

Competition Findings

Only one of the five counties, a large urban county, used a competitive bidding process to evaluate provider proposals before awarding a contract. Each of the state agencies used a competitive bidding process, but the consistency and depth of request for proposal issuances, bid proposal evaluations, and the use of award criteria varied by service and agency. The other four counties had some competition in certain service areas, but that usually meant two providers, who frequently were segmented in different ways and did not compete directly against each other in the proposal process.²⁷ For example, one medium-sized county had two domestic violence providers, but one was residential and the other nonresidential, thereby providing no competition on which managers could evaluate the cost or quality of the service to be delivered.²⁸ All of the state and county public managers cited several barriers to developing competition:

- Environmental constraints
- Actions by nonprofit organizations
- Networked relationships
- Government-enacted barriers.

Environmental Constraints

The cost of developing competition and capacity is a barrier for many public agencies, especially at the county level. The levels of competition and public-management capacity are largely interdependent on one another. At the county level, all of the public managers cited staff and resources as necessary for developing competition. The following quote accurately expresses the sentiment of public managers: “We would not discourage new competition. I think we have too many things to think about that we don’t have the time and staff for developing competition [therefore] we seek out nonprofits without really doing an RFP because if there’s a lack of providers then we don’t really have much selection anyway.”²⁹

More than one provider would require the county department of social services to supply those providers with clients and resources and to retain sufficient staff resources to monitor and enforce accountability. Unless alternative providers have funding and revenue stability aside from government contracts, subsidizing multiple providers would not contribute to the cost-efficiencies normally associated with contracting and competitive markets.

This creates a paradox for public agencies: With each additional provider, there are diminishing marginal returns in the contracting arena, but without additional providers that compete against each other to deliver the same ser-

vice, there is no genuine competition. While public managers want to reduce the number of clients who need services, this requires the expertise and service-quality improvements normally achieved through contracting with several nonprofits. A one-size-fits-all perspective does not serve all clients equally. Therefore, provider alternatives are needed for clients to have successful treatment outcomes across a range of needs, severity levels, and treatment options. Yet, simply having more providers deliver services to a group of clients with the same level of need does not alleviate the necessity of obtaining providers that can deliver services to clients with varying needs. Currently, an absence of competition and provider alternatives requires public agencies to support a private market. As a result, the projected cost savings and quality improvements associated with contracting are limited.

According to more than 65 percent of the county managers, social services clients expressed concern and anger about their limited choice of service providers. When county managers were asked about the lack of competition, more than 90 percent responded there was no immediate advantage in having only one provider. While expressing a need for additional providers, three-quarters of the county managers said they felt constrained in their ability to develop competition and provide clients with alternatives because of their own capacity limitations and the political disincentives associated with adding staff or encroaching on private markets. These public managers explained that “Yes, a second provider would be beneficial in negotiating price and would provide clients with different needs options on which provider best serves their needs, and they really should have that.”

A larger problem is that high-need clients may have no place to turn if the contracted provider serves only clients with moderate needs and there are no other providers to treat high-need clients. This was found to be the case especially in small and medium-sized counties. The lack of competition, capacity, and provider alternatives exposes agencies to the risk of having nonprofits engage in creaming activities.³⁰

Three-quarters of the county public managers and nearly two-thirds of the state public managers expressed concern about contracting for service delivery when there is essentially a transfer of responsibility from a public to a private monopoly. However, nonprofit executive directors expressed almost no concern about the lack of provider alternatives for clients. In speaking about threats to democratic actions, approximately 60 percent of the public managers were sensitive to issues of equity, justice, and access and were sympathetic to client situations because of the restrictions on selecting alternative providers. Yet, they were conscious of their limited ability to change the will of elected officials and the electorate, who view con-

tracting efforts as successful based on the perceived measures of government growth, public program expenditures, and tax rates.

More than 80 percent of the state-level public managers suggested they were more inclined to use a request for proposal process than their county-level counterparts because they believed the process contributes to the stimulation of outcomes, readjusts the philosophy of care, and potentially changes market share. However, nearly 85 percent of the county managers said that using a request for proposal process did not save their agencies money or bring about new providers. They found that rebidding made it difficult for their nonprofit partners to budget based on the uncertainty of competing annually for program funds, and that undertaking such a process was more frequently the result of a political directive rather than concern about the competitiveness of service markets. This dichotomous outcome is interesting because both groups manage contracts locally at the county level, but state managers manage from the state capitol in Albany. As such, this difference of opinion was cited by half of the county managers as creating difficulties for those activities requiring inter-governmental coordination.

Actions by Nonprofit Organizations

Nonprofit organizations have taken steps to ensure that competition remains very limited in most county service markets. Whereas a public agency would need staff and resources for multiple service areas, many nonprofit organizations specialize in particular service areas (such as domestic violence or job training). The service specialization that nonprofits offer enhances their expertise and reduces competition in local service markets. Many nonprofit organizations specialize in specific service areas, such as homeless housing for those with chronic mental illness or chemical addiction, because a need exists. Other organizations develop expertise based on the mission of the organization or because a public agency approaches the organization about new funding opportunities for service delivery. The latter reason can create difficulty for some nonprofits that become dependent on public funds. Two-thirds of the nonprofit executive directors referred to public funding as “hang-yourself money,” especially if it is the organization’s sole source of revenue. This is consistent with the findings of other researchers, which show that nonprofits’ actions diverge from their organizational missions because of a lack of revenue diversification apart from government funding (Smith and Lipsky 1993; Scott and Hill 1995).

A constant challenge for county managers is to explain to their legislatures why a particular nonprofit is the only organization that provides a specific service, such as rehabilitating sexual offenders. Approximately 85 percent of

the county managers and nearly 65 percent of the state managers explained the situation in terms of specialization. This theme was explicitly cited by more than 90 percent of the nonprofit executive directors and is illustrated by the following quote: “We self-selected a very difficult population to serve that no one else wants to serve because of our mission and experience. As a result there’s been enormous interest and public funding for this service ... we did not go looking for this interest and funding, but rather, this is the next wave of service delivery and we’re seen as a model, in part because we were the first to get into this service area, and the expertise and reputation we’ve developed.”

Nonprofit executive directors, in speaking about why their organizations deliver the services they do, suggested several issues that are consistent with the quotation above. First, there was a need in the communities they served that was aligned with their organizational missions. In the case of homeless housing for those with chronic mental illness or chemical addiction, several organizations suggested they would accept anyone seeking shelter, but frequently those clients had one of the aforementioned conditions. Therefore, the decision to focus on this particular clientele was not fundamentally divergent from their mission. Second, nonprofit executive directors are actively engaged in and track new legislation and policy changes in their service areas. As a result, many of these directors can identify trends in which future funding is likely to develop for specific services. Third, many nonprofit organizations advocate on behalf of clients and services for which they believe a need exists. Finally, being the only service provider in a region can provide the necessary resources to develop higher-quality services, be more innovative, augment expertise and reputation, and limit competition based on repeated transactions between the public agency and the nonprofit, thereby ensuring the nonprofit’s survival, a strategy that is consistent with the actions of interest groups and organizational survival theories, such as population ecology.³¹ While some groups may counter that these actions are opportunistic and nefarious, others question whether nonprofit niche monopolies are any riskier than unspecialized public agencies. One explanation for the growth of niche nonprofit monopolists is the proliferation of social service legislation and the concomitant lack of government capacity to manage and oversee the growth of services.³²

Nonprofit organizations also demonstrate their expertise to public agencies while limiting competition in other ways, such as advocating for legislation that requires professional certification or accreditation. All of the social service agencies provide services that require a provider be certified by an accrediting body, as in foster care and mental health. The accrediting bodies mandate specific levels of professional credentialing, quality of care and

treatment, and physical facility and capital resources. These bodies have the direct effect of regulating market entry. Public managers use the different certifications as a management tool and benchmark for evaluating provider qualifications and expertise. Because many accrediting bodies successfully advocate for legislation requiring provider accreditation, competition is further limited. Sixty percent of the county managers and nearly two-thirds of the state managers described the process in this way: "The programmatic legislation called for a certified residential domestic violence shelter. We only have one. They knew it, they [the nonprofit] knew before we did that they would be the only qualified provider and that the law specified this requirement. Frequently their state senator or legislator calls them before those of us at the county level know anything about it."

In the domestic violence example, counties are limited to attracting other certified providers to the region or developing competition in which certification requirements can be met. The use of screening mechanisms, such as accreditation, to limit competition was evident in nearly half of the service areas in which managers were interviewed.

The actions of nonprofit organizations in this sample positively affect the service providers that enact them and limit competition. This is different than the nonprofits in Bernstein's (1991) study because those nonprofits felt they were victims in a contracting game in which the rules of the game were dictated exclusively by public agencies. Additionally, other researchers have found nonprofits involved in relationships characterized by interdependence and dependence (Saidel 1991; Smith and Lipsky 1993; Scott and Hill 1995).

Networked Relationships

Networks and relationships between nonprofits and agency and elected officials are costly barriers to creating meaningful competition. Sixty-seven percent of the nonprofit executive directors in this study suggested the relationships between state agency managers and nonprofit providers bordered on incestuous, implying that agency managers were so connected with nonprofit personnel that the contracting relationships were anything but competitive and objective. Public managers point to constraints placed on them by elected officials to contract with specific providers and organizations cited in legislation, or to those with whom they have long-standing relationships and that are "wired into the system." Seventy-five percent of the public managers agreed that "nonprofits still do not know networks and advocacy the way businesses do, but they are learning quickly." Welfare reform legislation was frequently cited as pushing nonprofits to advocate, develop networks and alliances, and be more forceful in gaining a role at the policy table

because of the entry of new competition, specifically from private companies.³³ Nonprofits have changed their behavior to compete for new sources of block grant funding. With the passage of New York's Welfare Reform Act of 1997, all of the executive directors spoke of developing strong relationships with elected officials and local DSS managers and advocating that their organizations be the recipient of services going out for contract. While nearly half of that group expressed considerable discomfort in doing so, they nonetheless engaged in this type of relationship building and networking activity.

In one nonprofit, the executive director became so accomplished in her role of developing relationships with the elected county leadership and public managers that her organization went from having \$93,000 in contracts in 1998 to \$210,000 in 1999, a 126 percent increase.³⁴ Networks with elected officials and managers and the newly awarded contracts built her organization's financial capacity, thereby increasing its reputation as a quality provider with the capacity and capitalization necessary for larger contracts. This was not an isolated incident among the nonprofit executive directors interviewed. In another case, a good illustration of the experiences in nearly two-thirds of the nonprofits, the executive director said, "you help those you know," suggesting that providers known to their political and agency bosses will receive benefits that lesser-known organizations may not.

Nonprofit executive directors spoke about using their personal and organizational networks, including those of board members,³⁵ to advocate and educate elected and appointed officials in the governor's office about services to be contracted out. However, a dichotomous outcome was found with respect to this issue: More than 40 percent of the nonprofit executives cited direct pressure from appointed public managers to have elected officials intervene on a nonprofit's behalf and "put in a good word." The nonprofit executive directors who cited this believe the appointed managers wanted to see which elected officials supported which nonprofits. If a Republican member supported a nonprofit, that organization would have a comparative advantage in state contracting over a nonprofit supported by a Democratic member.³⁶ In this case, the nonprofit executive directors stated they worked hard to remain apolitical and resented the implication that their expertise and reputation would not earn them the contract, but the support of a ranking member would.

On the other side of this issue, nearly 60 percent of the executive directors spoke of joining groups, taking on community responsibilities, and meeting elected officials and agency executives with the specific goal of asking, how is this relationship going to help us? These actions were very strategic and direct and resulted in the expressed theme of "when my organization is under attack in terms of fund-

ing, I call in all my favors and get us connected, get our funding restored.” The situation of getting funding restored is not unusual in New York given its long history of late state budget adoptions. One executive director in particular spoke of using her networks, not only to facilitate payment to her organization for contracted services during a period when the budget had yet to be adopted, but for all of the other service providers as well. The public manager responsible for managing these contracts expressed amazement and gratitude at the depth and power of the nonprofits’ contacts in getting payments expedited for all of the program contractors. This action had fortuitous and unintended consequences for the public manager, in that it improved her ability to manage the contracted providers because they remained financially solvent throughout the budget impasse. While this set of actions by the nonprofit executive director was directed at maximizing the interests of her own organization, positive externalities resulted for the collective group of providers, and subsequently for the public manager. In contract negotiations, the public manager continually renewed the contract of the nonprofit that used its networks to benefit her bureau, monitored the nonprofit infrequently, and spread the word that “this is a nonprofit you can work with ... they won’t embarrass you.” The nonprofit’s success in expediting contract payments resulted in its continued contracting and enhanced its reputation with the public agency and manager, and competition in the service category remained limited. Eighty percent of the public managers confirmed that a major management motivation in contracting with certain providers is that they feel secure their public agencies will not end up on the front page of the newspaper because of malfeasance, abuse—or worse, the death of a client. This was expressed most succinctly as follows: “We’re on boards with them, we relate to them, we go to meetings with them, and we have a pretty good idea of who we can work with.”

In a different example of networked relationships, elected officials periodically direct public agencies to distribute financial resources for service delivery within their communities. Legislatures also apply pressure to agency managers to contract with specific nonprofit organizations. Seventy-five percent of the county public managers described the political pressure to spread the money to less developed regions of the county where economic development was needed. The following quote illustrates this: “Contracting can become political. In this county, it’s more of a geographic issue to spread the money around, especially over in the eastern portion of the county where they claim no one uses nonprofits. The classic case is preventative services for children. We decided years ago to just contract rather than hiring people and we went to this provider because they had places throughout the county. Even

though I might say we’ve gone beyond the need out there, it’s politically difficult to cut that.”

Two themes emerge from the statement: First, the political appeal and pressure to provide resources in specific areas, and second, the use of private providers rather than hiring additional public staff. In these instances, service funding is hard to remove even when a service is no longer required. This is a perspective that is absent in the literature on privatization. Contracting with nonprofit organizations not only eliminates the need to hire public staff, but also provides economic development and employment opportunities for communities. A stark reality develops in which organizations are funded to provide services that are not needed, but are politically difficult to eliminate.

Finally, public managers cited a number of instances in which nonprofits served as their mouthpieces in advocating for additional funding for services to legislatures. Even though public agencies felt under siege in their ability to respond to community needs because of the increasing propensity to contract and downsize, many social service departments voiced their messages and needs through nonprofit organizations advocating to the legislature. In such instances, public managers believed that legislatures afforded greater levels of trust and legitimacy to nonprofits than to public agencies. While these advocacy efforts did not result in the public agency delivering the services, they did receive the necessary funds to contract for service delivery. In instances in which public agencies relied on nonprofits to get their messages across to the legislature without implicating themselves in the process, public managers suggested they would contract with those nonprofits because they could be trusted.

Government-Enacted Barriers

A lack of competition, a lack of clearly defined outcomes, and insufficient cost and performance data have led public managers to actively develop and use public–public partnerships. Public officials and their agencies turn to one another for service provision in geographic markets where there are no alternative providers or where the provider lacks the necessary capacity. Each of the counties studied had contracts between the DSS and other county agencies. Such internal organization arrangements create an auditing advantage. “The auditing advantage of internal organization ... is attributable to constitutional and incentive differences which operate in favor of the internal mode” (Williamson 1975, 29). Therefore, fewer incentive differences exist for agencies to act opportunistically, and each can be more easily monitored by the other. Contracting between agencies can minimize the costs associated with putting services out for bid, contract management, and oversight. For example, the county DSS contracted with the county department of labor for services under the

Job Training Partnership Act. While nonprofit organizations are engaged in vocational education and job placement and have expertise in this area, the DSS found that the department of labor could do the work as effectively and efficiently as a nonprofit organization.³⁷

Nonprofit executive directors expressed frustration with the complex nature of integrated service components under federal and state welfare reform legislation, and the political expediency with which elected officials and public managers sought to achieve their goals through contracting with other public agencies. Integrated service delivery across a range of services requires joint production of services and extensive coordination and planning by private providers. For example, an individual may need job training services, transportation, child care, and substance abuse services. Each service provider must work together if the client is to be served effectively and become self-sustaining. Welfare reform proponents have pressured nonprofits to achieve this goal quickly without increasing costs, a transition that nonprofit executive directors have found difficult and with real costs.

Consequently, public agencies have turned to other public agencies for internal contractual relationships in an effort to reduce the transition time and financial costs of contracting with nonprofit providers. The monies appropriated through the legislature still appear as resources for private service provision in the form of contracting, but in terms of consolidating political power, agency commissioners assist other agency commissioners through these partnerships. The allocation of resources is as it would be under a contract, but the administrative and paperwork costs are minimized because the work shifts from one public agency to another. This arrangement is consistent with the recommendations of public-choice theory, in which the provision of services is separated from its production. Theoretically, there is little need for a contract process, and fewer resources are necessary for oversight, considering the contractor and provider are both public organizations in the same county with public managers working jointly to maximize the effectiveness of their agency's contractual resources.³⁸ Such efforts have frustrated nonprofit executive directors because of the exclusionary nature of these government-enacted mechanisms for reducing costs, time lags, and oversight costs. Public-public partnerships limit competition because they lack the true costs of contracting out and offer few opportunities to compare the costs of public versus private service provision.

Governor Pataki's blessing of this union occurred largely because he was under pressure to cut the cost and size of government while maintaining services. At the same time, he was facing tremendous pressure from public employee unions, which were protesting the deep and wide cuts he was making to the bureaucracy. The unions asserted the

cuts were not well thought out, a theme they consistently echo but which appears to have merit in this situation given the shifting of public personnel with specialized expertise into different program areas as a result of the creation of the Department of Family Assistance. By using public-public partnerships where feasible, the governor was able to fulfill the divergent goals of shrinking government coupled with fewer public personnel layoffs. While nonprofit advocacy efforts intended to minimize the occurrences of this scenario met with legislative resistance, contracting with nonprofits and public-management capacity reductions continue to be the theme of the day in providing social services.

Public-Management Capacity Findings

Public agencies face obstacles in adding personnel, leading them to contract for services even if only one provider is qualified and available. All of the county public managers and nearly 75 percent of the state public managers described the following: "Contracting out is usually easier to get through the budget process because it does not appear as a county employee. It's easier to make a case for services that are needed than to suggest or request new staff to provide services, so in the budget process it's easier to put in \$90,000 for services as opposed to \$90,000 for two new county DSS staff. No one ever challenges us on this issue."

The public objects so strongly to the addition of personnel—according to public managers, citing elected officials—that many public managers reluctantly agree to contracting arrangements rather than waiting on legislative authorization for additional staff. The argument that legislatures make to public managers is that a public employee is frequently kept on an agency's payroll even when a service is no longer needed because managers find work for them.³⁹ However, with a contract, the position can be terminated and the appropriated monies reallocated. More than 90 percent of the public managers suggested that "the political motivation is to have public agency staffs get smaller ... elected officials think the public trusts nonprofits more than government ... [therefore] it's easier to spend more and contract with a nonprofit than add staff to the payroll."

As public social service agencies increase their contracting efforts, they simultaneously reduce their staffing levels, thus creating capacity shortages in critical areas such as contract management.⁴⁰ According to almost 80 percent of the public managers, contract-management expertise and capacity is needed to develop detailed requests for proposals, solicit bids, evaluate bids, award contracts, and provide technical assistance to contractors. In addition, these same managers, as well as nearly 75 percent of the non-

profit executive directors, agreed that public-management capacity is necessary for managing and overseeing the contract after it is awarded, evaluating service outcomes, and acting as a liaison between agency executives, elected officials, clients, and contractors. This lack of contract-management skills has been noted in a number of audits conducted by the General Accounting Office and New York's Office of the State Comptroller. The General Accounting Office, in one of several studies on social service privatization, found that state and local governments have "little experience in developing contracts that specify program results in sufficient detail to effectively hold contractors accountable" (GAO 1998, 2). All of the public managers said that capacity significantly affects how they manage contractors and the level of oversight performed. "We can't do the type of oversight that we use to do in the old days. Every I was dotted, every T crossed, every program was visited at least twice annually and so on."

A public manager captured the sentiment of all of the state public managers and more than 80 percent of the county managers, stating that her staff of 12 was responsible for managing more than 500 providers; of all the management functions they perform, monitoring is the one that policy makers do not ask about on a daily basis, and therefore it receives the least amount of time and attention. This is not an isolated example. The Office of the State Comptroller found many instances across agencies and service areas in which there were too few personnel with service expertise who were also trained in contract management.

Public managers recognize that county agencies are at risk of being exposed to fraud, waste, and abuse because they are unable to provide adequate levels of oversight because of budget and staff reductions.⁴¹ Legislatures and state officials seeking increased accountability press for greater reporting requirements from providers. However, this action only serves to exacerbate the capacity challenges facing public managers. The paradox is that as reporting requirements increase, so do program administration costs. Relying on reporting requirements to fill public administrative capacity shortages, although necessary for overseeing contractors, may have the unintended consequence of creating capacity challenges and overburdening providers that have to complete them and taking them away from service provision.⁴² Multiple providers and extended reporting mechanisms require public-management capacity for reviewing reports and ensuring contract compliance. If providers know that public agencies lack the capacity to substantively review contractor reports, then there is some question as to whether a provider should invest the time and resources into fully and accurately completing the reports. This type of scenario also leaves the public agency vulnerable to contractor opportunism.

A second capacity threat, loss of institutional memory and policy expertise, is an issue that public managers try to correct for by involving nonprofit providers in the development of outcome measures. This is common, given that government consults and collaborates with organizations that have expertise it lacks. However, it raises questions about democratic accountability because the nonprofits are no longer exclusively implementing services, but also are engaged in policy formulation and evaluation.⁴³ Nonprofit involvement in the development of performance criteria for contracts they hold and others may bid on, sets a dangerous precedent for ensuring accountability and objectivity. Such actions also limit government's ability to be a smart buyer of goods and services because of the specialized information that nonprofits possess. Even considering this potential conflict, however, public managers believe that developing clearly defined and measurable performance indicators can stimulate competition for future funding rounds, reduce costs, and enhance service access and quality—but this requires public-management capacity.

Another problem facing public social service agencies is developing excess capacity for times of emergency. Many public and nonprofit managers described incentives and rewards as flowing to those who focus exclusively on short-term results and outcomes. Yet, in times of crisis and increased client demand, these same public managers are publicly sanctioned for not having foreseen the potential crisis and developing strategic plans to address critical capacity shortages. Forty percent of the public managers said, "If there is no reward for capacity building—we're going nowhere on it." Appropriating monies for capacity building positively affects the way the contractual relationship is managed and overseen. However, very few public managers have found a way around the obstacles constraining them in developing excess capacity.

Nonprofit managers expressed frustration with their public-management counterparts because of their lack of expertise, institutional memory, and capacity constraints. Seventy-five percent of the state-level public managers offered a perspective shared by two-thirds of the nonprofit managers, illustrated in the following quote from a nonprofit executive director: "In the past there has been program development generated at the state level ... but you cannot understate the impact that the Pataki administration has had. They have gutted all of the career professionals at the state agencies. And the state agencies no longer have the capability to do anything creative. They can occasionally approve or disapprove, but their creative capability is gone."

Reduced public-management capacity not only limits government's ability to develop competition, it also hinders government's ability to be a smart buyer, monitor, and accountability enforcer. Therefore, public managers have

taken matters into their own hands to protect what they believe is the public's work and what is in the best interest of clients and citizens.

Public managers understand which services they do not need to contract out, but they are discerning in identifying situations and programmatic environments in which it makes sense to use private providers. They understand this issue because in service areas where providers exist, they apply pressure to elected officials to create funding support, and these same officials turn around and pressure agencies to contract with specific organizations for delivering services. But, agencies have gone to legislatures in the past and made the case that certain service areas were not competitive and alternatives did not exist. County managers stated that the legislature usually accepted this response because they lacked the time and motivation to verify whether it was true. To that extent, nearly 60 percent of the county public managers claimed they understand which services they need to contract for, but they declined and resisted efforts at contracting for services they deemed to be inherently governmental, such as eligibility determination. Identifying situations in which county managers felt they had to contract achieved several outcomes, including maintaining or enhancing relationships with the legislature, extending an olive branch to nonprofit providers, and reducing the scrutiny directed toward their agencies by external constituencies.

Sixty percent of the county managers used information the legislature did not possess, such as the extent of market supply and demand imperfections, as a bureaucratic strategy for increasing agency power and staffing while maintaining control over the services they believe are inherently governmental. County managers, experiencing political pressure to decrease the size of their agencies, took actions that circumvented the policy directives of the legislature and directly contrasted with the edicts espoused by their superiors. This finding is quite different from DeHoog's (1984) study, in which bureaucrats enacted strategies to minimize their work loads, but it is consistent with Terry's (1995) study on administrative conservatism, in which he found public managers taking actions for reasons other than opportunism. How did the county managers achieve this result? The following quote most closely represents the set of values and actions expressed by the county managers: "DSS is the only county agency authorized by law to investigate child abuse and neglect. I don't want nonprofits doing this sensitive work. I want to keep that authority, so I want to be the best in that, and I'll invest in my staff so that we're the best at that. I don't want other agencies or nonprofits to have an opportunity for this service area to become competitive, nor do I want legislators thinking this is the kind of work that someone other than a public agency should be doing."

Public managers felt that if the legislature were set on curtailing their involvement in service delivery, then they would ensure that their agency possesses expertise that is not easily replicated in the market. This example illustrates that agents, in this case local DSS officials, possess information that is not readily verified by principals, such as legislatures. Incentive differences and conflicting agency goals and missions have contributed to situations in which public managers have tried to maintain their agencies' capacity by preserving expertise they perceive critical to government.⁴⁴ These findings suggest that a lack of administrative capacity, programmatic expertise, trained procurement personnel, and political will give rise to contracting. Only when the capacity exists to conduct the contract-management activities described can public managers be smart buyers of the goods and services that clients, citizens, and elected officials expect.

Conclusion

Privatization proponents speak of the advantages of exposing public services to the competitive forces of the marketplace. This is consistent with economic and public-choice theory, but does all privatization lead to cost savings and improved service quality? The data from this study suggest that in certain cases and in particular locations, privatization takes place for reasons other than the benefits normally associated with competition. Privatization and contracting for social services with nonprofit providers was used for politically symbolic reasons to demonstrate that government is getting smaller, working more efficiently by disengaging itself from direct service delivery, and not encroaching on private markets. What we learn from studying the government–nonprofit contracting relationship is that privatization is more a political than an economic act (Savas 1987). Competition is a fundamental assumption underlying many of the privatization success stories, yet the lack of competition and subsequent reduction in public administrative capacity poses significant managerial challenges when contracting.

Public managers' ability to act as smart buyers of goods and services is compromised when there is a shortage of public managers trained in contract management and substantive policy areas. In addition, the issues of goal divergence, competing incentives, and political and bureaucratic realities further inhibit a public manager's ability to manage contract relationships and provide meaningful oversight that mitigates against fraud, waste, and abuse. Increased demands for smaller and more efficient government have led many elected officials and agency executives to seek privatization as a vehicle—some suggest panacea—for controlling costs. Yet the privatization of social services in many areas in New York state has transferred pub-

lic monopoly power and authority to private monopolists, with few increases in performance and accountability.⁴⁵ Administrative constraints in public agencies have contributed to the rise of nonprofit networks. These networks have limited competition rather than expanded the number of providers, and they have created opportunities for nonprofits to become involved in formulating and evaluating policy. Yet their presence also concerns how to most effectively monitor their actions, especially in cases in which there is a lack of policy expertise and capacity. This concern gives rise to the question of how to resume responsibility for service delivery if there is a need to do so. Only in times of crises, when an abuse or tragedy has occurred, do elected and agency officials question why a public agency was unable to manage and oversee its providers. Yet, repeated requests from public managers to their superiors to add staff for auditing and oversight functions continually meets with resistance. The resistance is based partly on the competing incentives and goal divergence that exists among the various actors involved in the contracting relationship. The administrative costs associated with privatization in developing competition and providing meaningful oversight is seldom figured into the cost-saving calculus used to describe privatization successes. Such transaction costs inevitably are revealed through capacity investments or because of capacity gaps that are exposed when there is a tragedy.

The extent to which competition, capacity, politics, and a lack of clearly defined and measurable outcomes affects the public management of contract relationships with nonprofit social service providers has a significant impact not only on the quality of the services being delivered, but on the trust that citizens and clients have in government. Politics is inherently a part of the privatization and contracting process, and it affects how contract relationships are managed. It affects the level of funding and staffing allocated to public agencies, resources that are critical to providing services and ensuring service quality and accountability when contracting. These resources are necessary for developing competitive marketplaces in which contracting can take place and for which critical evaluative work can be done in assessing the strengths and weaknesses of programmatic, intervention, and treatment strategies. All of these evaluation processes are necessary if there is to be movement toward developing and defining outcome measures that receive majority support, are measurable, and inform strategic policy decisions and the allocation of finite resources.

If government is to contract for services that are available in a private market, it should have the resources to manage, oversee, and enforce accountability. Savas (1987, 257) notes that "corruption is not to be tolerated, and the best defense against it is effective competition." To avoid

the pitfalls of privatization absent competition and public-management capacity, government must take a long-term outlook and invest in contract management. However, as Donahue (1989, 13) warns, "unless we are luckier or more careful than we are likely to be, political pressures will tend to retain for the public sector functions where privatization would make sense, and to privatize tasks that would be better left to government." More empirical research is needed to examine the public-management implications of contracting with nonprofit organizations beyond the rhetoric of privatization. One question is whether a public agency is a monopoly or monopsony, and does the transfer of power and authority regarding contracting with nonprofit in markets with little if any competition constitute a form of public monopoly transfer to private monopolists?⁴⁶ If government were to act as a monopsonist—a sole buyer of labor—rather than as an entity seeking to correct market failures, then the only counterbalance to those actions would be for the seller (nonprofits) of labor (service provision) to collectively organize. Is it good public policy, therefore, to overlay one market failure with another? Is there another self-correcting market or policy mechanism for reducing monopsonistic opportunism, such as providing service vouchers to clients so they can directly purchase the service and training they require in a private market? Or would we have a more effective government by investing in public-management capacity, wherein contractors could be vigilantly managed, overseen, and evaluated? If a smaller, more results-oriented government is what citizens and elected officials desire, then the answer is not that all bureaucrats are opportunistic agents who create market failures for their own self-interest, and the answer is not to destroy competition by encouraging nonprofits to collectively organize with a single voice of opposition to a public monopoly. Rather, the issue appears, strictly from a cost-benefit perspective, to be that rigorous contracting requirements and public-management capacity are more efficient investments because these resources can be invested in public-management and agency capacity toward creating smart buyers. Examining these questions and others will help to advance theories about public management, as well as practices and tools used in privatization arrangements.

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Notes

1. Contracting is one of 10 different forms of privatization. It is the most widely used form of privatizing social services, mental health, health, corrections, transportation, and administration (GAO 1997). A number of political directives and legal challenges in the 1960s created widespread use of contracting, most notably the Public Assistance Amendments of 1962 and 1967, which favored a climate of contracting out for services. These amendments came about as a result of the War on Poverty and the Great Society programs of the Kennedy and Johnson administrations. The Economic Opportunity Act of 1964 also made the use of contracting for the production and distribution of services a more widespread practice. Smith and Stone (1988) note that social service privatization is usually dated from the 1967 amendments to the Social Security Act, which allowed purchase-of-service contracting for the first time. A general review of the purchase-of-service contracting development can be found in Derthick (1975) (see also Kettner and Martin 1986; Netting et al. 1990).
2. The structure of competition depends on a formalized and structured solicitation and bidding process in which bids are submitted, evaluated, and an award decision made by the government agency requesting bids. At the local level, three or more providers is ideal. At the regional or national level, two providers may be enough if the organizations are competing for market share. A competitive market is one in which there are enough sellers—in this case, private providers—so that each has a negligible impact on the market price of goods and services.
3. It is important to recognize that government would incur the costs of the first two activities if effective performance is expected of government. Some scholars have suggested the real distinction between in-house and contracted services is the transaction costs that can increase in these ventures.
4. Williamson (1975) refers to the “hollow corporation” in a discussion in which transaction-cost problems are reduced in the vertically integrated firm by *not* contracting out the important functions of the firm. In public administration, these are services thought to be inherently governmental. Other scholars have contributed terms for thinking about the government’s increasing hollowness and its reliance on private contractors for service provision: Kettl’s (1988) “government-by-proxy,” Wolch’s (1990) “shadow state,” Smith and Lipsky’s (1993) “contracting regime,” and Salamon’s (1989) “third-party government.”
5. While it is true that privatization usually affects lower-level employees disproportionately to managers and policy analysts, it is the lower-level employees, such as case workers, who frequently interact with and serve clients in need of services and treatment. When these positions are reduced or eliminated, government agencies lose expertise and institutional memory, which can be critical to the way contract relationships are managed.
6. Again, there is widespread disagreement with this tenet of Savas’s ideal contracting arrangement. A number of authors have found that government is not an effective monitor or inspector of contracted goods and services (Kettl 1993; Donahue 1989; DeHoog 1985; Smith and Lipsky 1993; Kamerman and Kahn 1989; Kramer and Grossman 1987, 1994; Ostrander, Langton, and Van Til 1987; Salamon 1989, 1993, 1994).
7. Cutback management refers to government efforts to cut public staff, limit hiring, enact administrative cost constraints on agencies, and generally limit efforts to make public compensation levels competitive with the market. Levine (1980) was one of the first public-management scholars to use this term.
8. If the program outcomes are based on a January–December evaluation period, but the funding and service implementation is not in place until May, then public agencies and nonprofits scramble to meet program goals.
9. In this table, I include only works in which data have been collected and that are widely recognized and cited. In addition, studies that primarily summarize disparate literatures or rely exclusively on secondary and archival data sources are not included. “Documents” refers to the collection of contract and organizational documents for content analysis. “Archival” refers to the use of historical documents. Documents and archival sources are used in many of these studies for purposes of triangulation.
10. This includes program managers, contract managers, auditors, technical specialists, agency executives, budget examiners, and representatives on social service committees.
11. Meier (2000, 148–49) states that “reorganization can be used to shape the environment of an agency by creating a climate hostile to or receptive to agency programs.” He goes on to note that studies have found that reorganization alters power relationships, increases a governor’s appointment power, and generally strengthens the position of the chief executive.
12. Ruth Hoogland DeHoog (1984, 11) notes, “If scholarly research in this field [public management] is to be of some utility to decision-makers, we must begin to identify the environmental conditions and administrative procedures conducive to contracting arrangements achieving the organizational aims of improved efficiency and good quality services.” In a spirit consistent with this specific call for empirical research, this study responds by examining the public-management implications of competition and capacity on privatization efforts.
13. See Haskins, Sawhill, and Weaver (2001). In this policy brief, the authors identify “the five characteristics [that have] rendered TANF a radically different program than the AFDC program it replaced.”
14. The aim of these programs is to help individuals and families prepare for self-support. Under TANF, states have financial incentives to use block grant funds for purposes designed to get people off welfare.

15. In a forthcoming paper, the author examines the manner in which the contract relationship is managed from the theoretical perspectives of agency, stewardship, and network theory.
16. My interest is in examining social service delivery from the theoretical perspectives above, given that the realities of implementing social programs through a third party in a complex area with poorly defined outcomes and inconsistent levels of competition appear to be at odds with the theoretical tenets advocated by public-choice scholars, who favor privatization as a method of reducing costs and improving services.
17. These individuals were in five different counties that included one urban, three suburban, and one rural. A multiple-case sampling across program sites increases confidence in the findings by examining a range of similar and contrasting cases. This technique not only strengthens the validity and stability of the findings, but also the precision, and thus makes the findings more robust. The Census Bureau defines a "small county" as having a population under 100,000, based on 1998 total resident population. A medium county ranges from 100,000–250,000, and a large county is 250,000 and above. Based on these population ranges as a definition of county size, there are 15 large counties, 11 medium counties, and 36 small counties in New York state. Two large, two medium, and one small county were examined in this research study.
18. The five New York state agencies include the Office of Children and Family Services, Office of Temporary and Disability Assistance, Office of Mental Health, Department of Health, and the Office of Alcohol and Substance Abuse Services. All of the state contract managers were involved in overseeing state contracts that were being administered at the county level. Essentially, then, all of the contracted services being delivered by nonprofit organizations are at the county level. This is important because the manner in which state and county public managers oversee contract relationships can be examined, a subject that is explored in greater detail in a forthcoming paper.
19. The nonprofit organizations varied by revenue, clientele, service area, location, and number of government contracts. Only 40 percent of the nonprofit organizations had government contracts in more than one county, and none had contracts in three or more counties.
20. Other interviews were conducted; however, there are missing data for some of the questions. Therefore, the 35 interviews used here represent complete data cases. This lends itself to greater levels of generalizability.
21. Because of confidentiality and requests for anonymity, all of the counties, interviewee names and titles, and names of the nonprofit organizations have been omitted. To gain access to "elites" with specialized knowledge, I had to offer the respondents complete anonymity given their concerns that the nature of their comments could have adverse affects on the contract relationships they are involved in and repercussions from agency superiors and elected officials. I have chosen to use the following terms to describe the respondents. The term "public managers" represents individuals interviewed at either the state or county level. The individuals were appointed and nonelected civil servants. Individuals with the responsibility and authority for managing social service contract relationships with nonprofit organizations were interviewed. In four of the five counties, this meant interviewing the commissioner and deputy commissioner separately, as well as division directors. A commissioner and deputy commissioner would be roughly equivalent to the number one and two position within a social service agency. At the state level, all of the managers were bureau chiefs or division directors. The respondents representing nonprofit organizations were all executive directors.
22. A purposive sampling strategy was employed in a cross-site analysis in New York state. The interviewees' peers and other experts were identified as having the most knowledge and experience in contract development, administration, monitoring, and evaluation. Programmatic, financial, and administrative personnel are also included in the sample. The conceptual design of the study dictates that data be gathered from those who are most involved and are considered experts in the contracting process. Miles and Huberman (1984) refer to this process as "snowball or a chain sampling strategy" because it assists in identifying cases of interest from individuals who know the cases that are information rich.
23. One of the strengths of a qualitative approach to primary data collection is that there is richness to the data, what Geertz (1973) refers to as "thick descriptions," which can be gathered only in person at the site where the events are taking place. Qualitative research studies people and events in their own contexts and is especially appropriate in environments with multiple actors and in interdependent and complex organizational environments. Lofland and Lofland (1995, 103–6) note that this type of research is especially appropriate for examining "practices" and "relationships," especially where there have been few theoretical and empirical studies of the subject, thus necessitating the need for additional research. An open coding process was used (Strauss and Corbin 1990).
24. This excludes New York City and Long Island because no interviews were conducted there.
25. One issue that makes New York state an interesting case site is its use of federal funds to supplant state funds while having a constitutional mandate that counties provide assistance to those in need. As a result, the state was able to fund tax cuts for individuals and corporations.
26. The National Association of Counties cites California and New York as two of the best examples of counties providing general assistance as a result of a state mandate. Far more is known today than when DeHoog (1984) conducted her study in Michigan about the role of counties in providing services to communities in need. New York's counties have won several awards for innovative programs and practices, making selection of the State an important criterion. Four of the five counties in this sample are members of the National Association of Counties.

27. Ruth Hoogland DeHoog (1990, 321) indicates that "three or more potential suppliers are essential for competition." Adrian Moore of the Reason Institute for Public Policy states, "ideally if the firms bidding for the contract are local firms, you would want to have three or more."
28. Some privatization experts suggest that a rigorous request for proposal process may mete out alternative providers in the bid-competition process.
29. Two opposing arguments could be made about this statement. The first is the importance of setting up a proper solicitation. If only one organization submits a bid, it could be that other organizations were competed out in the pre-bid process. Second, if the county DSS were to set up the solicitation process and release a request for proposal, knowing that only one organization was qualified and capable of submitting a bid, then trust in the ensuing contract relationship could be damaged and present management obstacles for the public agency.
30. The term "creaming" denotes organizational actions in which a firm selects clients based on a contracted per diem because its informational advantages and expertise suggest those clients can be served for less than the contracted per diem, thereby allowing the firm to maximize revenue for each client served. For example, if a contractor is paid \$5,000 per client, then the provider who engages in creaming uses its expertise to select clients it knows can be treated for \$5,000 or less. In other words, given that all clients with varying levels of need may have only one provider to choose from, the contracted provider may select only clients with low to moderate needs, knowing it can treat them for \$5,000 or less and keep the difference without the government principal knowing this. Such actions may be the result of an opportunistic agent taking advantage of a lack of government expertise and capacity, or they may be strategic, in that the provider selects clients for which it has expertise, thereby ensuring its contract performance will be satisfactory and its reputation enhanced for meeting the terms of the contract. The danger for clients and public agencies is that, in the absence of competition, those who are most treatable will be selected by contracted firms to receive services, while those with intractable problems will be left to receive services and support from public agencies, frequently at a higher cost than the contracted service price. The obvious advantage for organizations to engage in creaming is that it maximizes dollars per client while minimizing organizational expenditures on client-service intervention. Savas (2000, 312) notes that creaming is, in fact, simply another form of market segmentation, which can have positive consequences for the public, clients, and the contractor, though not necessarily be positive for the public agency itself.
31. Williamson (1975) and other organizational economists argue that two effective strategies exist in competing for contracts. The first is to become a full-service provider, which allows for the cross-subsidization of costly services. The second is to be the best at a given thing, thereby doing something better and cheaper than anyone else.
32. Still, the question remains whether localized nonprofit monopolies are more or less effective than monopolistic public agencies, and whether they are truly more innovative in providing services to clients.
33. Maximus and Lockheed Martin are the largest for-profit corporations contracting with government agencies for social service delivery.
34. The deputy commissioner responsible for contracting in this program area confirmed this case.
35. This finding is supported by Harlan and Saidel (1994).
36. This is because Republicans controlled the executive office and Senate, while the Democrats controlled the assembly.
37. One could think of this as an increase in competition, but this would be true only if the public agency providing the service were required to submit a formal bid that accounts for the administrative and infrastructure costs that nonprofits must figure into their bids (rent, utilities, photocopying, telephone expenses). A related question is the transaction costs that occur because of this type of venture, as opposed to the costs that result when government transacts with a private firm for contracted service delivery.
38. However, one could make the case that agencies may exploit information asymmetries for their own organizational gains directed at maximizing budgets, personnel, and services.
39. Donahue (1989) and Milward (1994) both find this to be the case in their own studies on contracting.
40. Kettl (1993) and Milward (1994) both find that, although contract management continues to grow in its importance, it is not considered central to the missions of many agencies. A number of General Accounting Office reports also point to the lack of contract-management, monitoring, and program auditing expertise in many agencies in which private providers deliver public goods and services (GAO 1997).
41. While fraud, waste, and abuse have frequently been used in concert with one another, they are, in fact, different, fraud being a crime punishable in court. Waste and abuse, if detected, would subject those engaged in these acts to both legal and financial sanctions.
42. For nonprofit providers contracting to provide shelter to homeless men who are mentally ill and chemically addicted, they are required to complete a quarterly consolidated fiscal report. This document is 60 pages long and requires extensive data. This report is used by only one agency bureau. Therefore, for a nonprofit contracting with multiple bureaus at the state and county level, such a task can expend any surplus capacity that may exist. Smith and Lipsky (1993) highlight this issue in their study on the public funding patterns of nonprofit organizations. Alexander, Nank, and Stivers (1999) find similar issues with nonprofit capacity. See also Alexander (1999).
43. There is a long history of nonprofit advocacy in the agenda-setting phase of the policy process (Kingdon 1995). Public-management scholars working in this area consistently raise this concern (DeHoog 1984; Donahue 1989; Kettl 1993; Milward 1994; Moe 1996; Johnston and Romzek 1999).

44. One could argue that public managers act opportunistically by exploiting asymmetric information. However, each of the public managers discussed public-service values and motivation in the context of what they considered to be inherently governmental services. Agency theorists would contend that such actions are the result of bureaucrats trying to maximize their power and control. Other scholars, such as Moe (1996, 144), contend that “disinvestment in the capacity of government to perform the functions citizens expect of their government is a high-risk strategy where the negative consequences tend to be cumulative and difficult to reverse.”
45. One question that has yet to be resolved with clarity is whether the public agency acts as a monopolist or monopsonist. Some scholars suggest that because the public agency (the firm) is the only buyer of labor in a market, it acts as a monopsonist. Therefore, would clients with vouchers who can purchase services directly from providers increase competition in a market, thereby reducing a public agency’s monopsonistic actions?
46. Joan Robinson (1933) was one of the first economic theorists to study monopoly, price discrimination, and monopsony, from which many of our modern economic concepts were developed.

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Appendix A Interview Instrument for Governmental Contracting Organizations*

Thank you for agreeing to participate in the interview today. The focus of the interview is on understanding what factors affect the management of the contract relationship with nonprofit providers. I understand that your agency contracts with nonprofit organizations across a range of program areas. I would like to discuss with you how the contract relationship is managed and ask that you think about and use a program area that you are most familiar with as the context for this interview. The interview consists of fifteen questions and should take approximately one hour and 30 minutes. Do you have any questions before we begin?

1. Could you please describe the contract process with nonprofit organizations and your role in it? [what are the different pieces of the process?]
 - A. Are all contracts awarded in the same manner? If NO, then under what conditions are contracts awarded differently?
 - B. How is it determined who would receive a contract? Who determines this?
 - C. What role does a nonprofit organization's reputation play in the selection of contractors by your agency?
 - D. How is a nonprofit provider evaluated in terms of qualifications and expertise?
2. What outcomes is your agency most interested in when contracting with nonprofit organizations?
 - A. What outcomes is the nonprofit organization most interested in when contracting with your agency?
 - B. Each party in a contract relationship often has different goals in mind. What implications does such a difference in goals have for the contract relationship and how it is managed?
3. How much competition among other service providers exists in (name contracting environment)?
 - A. How important is the level of competition to how the contract relationship with a nonprofit provider is managed?
 - B. Are there conditions under which competition is more or less important?
4. What values, beliefs, and attitudes affect how the contract relationship develops between your agency and a nonprofit service provider? For example, some organizations initiate trust at the beginning of a relationship while others develop trust based on the outcomes of the contractual relationship.
 - A. Where do these originate?
 - B. Are there political values, beliefs, or attitudes that affect why public agencies contract with nonprofit providers?
 - C. Are there differences in how public managers manage contract relationships with nonprofit providers?
5. What do nonprofits provide your agency with in the contract relationship?
 - A. What do they not provide you with that you need?
 - B. Do they advocate for legislation that your agency supports?
 - C. Do you consult with nonprofit providers on policy or budget proposals your agency is developing?
6. How is trust built in contract relationships with nonprofit organizations? How important is it to the effectiveness of the relationship?
7. How is coordination achieved between your agency and nonprofit providers?
 - A. What is the most effective method?
8. What types of conflict exist in the contract relationship with nonprofit providers?
 - A. Under what conditions does conflict occur?
 - B. How is the conflict resolved?
 - C. What happens if the conflict cannot be resolved?
9. Are there specific types of information that you want your nonprofit contractors to disclose to you? What are the types of information that you want to know about?
 - A. Recognizing that confidentiality about clients is sensitive and must be guarded, are there other types of information that you possess that could be useful for a nonprofit contractor to know about, but which you do not disclose? Why would you not disclose this information? Are there different mechanisms that you use for sharing information?
 - B. If you believe that a nonprofit service provider does have information that you need but it does not share it with you, how do you go about obtaining that information? For example, some public agencies find out that per client treatment costs may be lower than the contracted amount agreed to with the service provider. How do you obtain accurate information?
10. What are the measures of success that your agency uses to evaluate nonprofit organizations that you contract with?
 - A. What measures do you think the nonprofit service providers use?
 - B. If these measures are different from one another, what implications does this have for the contract relationship?
 - C. Are there different measures of success for member item grants/initiatives?
11. What kinds of rewards does your agency use in contract management?
 - A. Under what conditions are these different rewards used?
 - B. How are these applied?
 - C. Are there personal incentives for the way in which you manage contract relationships with nonprofit providers?
12. What kinds of sanctions does your agency use in contract management?
 - A. Under what conditions are these different sanctions used?
 - B. How are these applied?
 - C. Are there personal sanctions for the way in which you manage contract relationships with nonprofit providers?
13. What risks are there in delegating responsibility to nonprofit organizations for service delivery?
 - A. Are there conditions under which contracting with nonprofit organizations presents greater risks for your agency?
14. How does your agency monitor and oversee nonprofit providers?
 - A. What resources are required for effective monitoring and oversight? (Human, Financial, Technological)
 - B. Are there conditions under which you conduct more or less monitoring of nonprofit providers?
15. Who in your agency or elsewhere determines which actions are necessary for maintaining accountability?
 - A. How are nonprofit providers held accountable?
 - B. Under what conditions are they held accountable?
 - C. Are there specific programs for which accountability is more or less important?

*The same survey was administered to nonprofit executive directors though the language was changed such that "nonprofit organizations" was inserted in place of "state and county agencies." The same substitution pattern holds true for "public managers" and "nonprofit executive directors." The instrument administered to nonprofit executive directors contained an additional question regarding "what actions do you take to insure that the governmental contracting agency upholds their end of the contract?" This instrument is available upon request and is not included here because of space limitations.

Appendix B Number of Contracts and Representative Program Areas

	County A	County B	County C	County D	County E
State Office of Children and Family Services	15	7	4	15	13
State Office of Temporary and Disability Assistance	16	5	3	5	3
County contracts	95	15	11	18	13
Program Areas					
Youth centers	Special delinquency prevention program	Domestic violence	Day care/child care programs	Homeless housing/single room occupancy	Housing opportunities for persons with AIDS
Operation of supported AIDS housing	Emergency shelter grants	Continuing education-job training	Settlement housing program	Access and visitation program	Foster care/adoptive care, child care resource and referral
Single room occupancy support services program	Refugee assistance program	Homeless veterans program	Home-based intensive supervision	Legal services	Training and technical assistance
Teenage and adolescent pregnancy prevention	Vocational rehabilitation	Persons in Need of Supervision	Homeless Housing Assistance Program	Income maintenance	Dispute resolution

Appendix C Contract Documents

Contract data from the Office of the State Comptroller—used in the sample selection process. (This is a listing of the contracts, by service area, that the Office of Children and Family Services and Office of Temporary and Disability Assistance had with nonprofit organizations by location.)

Catalog of State and Federal Programs Aiding New York's Local Government (1997 and 1999 editions) published by the state Legislative Commission on State-Local Relations.

Nonprofit annual reports and informational publications for the 15 nonprofit organizations in which executive directors were interviewed. Local newspaper sources were also used.

Office of Temporary and Disability Assistance procurement process—internal memos—used to understand the request for proposal process, procurement development checklist, tasks/responsibility/time frame, etc.

County Budget Appropriation Requests by Contract. Other county contract documents include: county contract riders, contract certifications regarding lobbying, contract boilerplates including payment schedules, contract threshold review instruments with ranking and point distribution by criteria categories, contractor/subcontractor background questionnaire, and examples of county contracts by service area, such as Persons in Need of Support, foster care, domestic violence, child protective/adult protective services, and delinquency prevention programs.

State Program Award Criteria matrices, in which weights are allocated by program area/agency/bidder and client categorization (that is, families, singles, mentally ill, mentally disabled/retarded, history of chemical dependence, ex-offender, persons with HIV/AIDS).

Summary Progress Reports—quarterly performance reports required of nonprofit contractors.

Annual Consolidated Fiscal Reports—required by nonprofits working under Homeless Housing Assistance Program, Operating Support AIDs Housing, Single Room Occupancy Support Services, and Emergency Shelter Grants.

Committee memos on "Using new technology to improve the NYS/Nonprofit Organization Grant Process." These are from committee meetings in which the NYS Office of the Comptroller partnered with various nonprofit organizations to improve the contract and grants process. Office of the State Comptroller—"Initiatives for the Not-For-Profit Sector: Survey Results of Not-For-Profit Organizations that Contract with NYS Government" (April 1998).

Report to the New York State Assembly (May 1999) on "Losing Our Children: An Examination of New York's Foster Care System," released by the chairman of the Oversight, Analysis and Investigation Committee and the chairman of the Children and Families Committee.

A number of materials on Office of Temporary and Disability Assistance contracting processes and procedures were collected and analyzed including Homeless Housing Assistance Program application review process, Homelessness Intervention Program 1999 request for proposals and application, Homeless Housing and Assistance Program: Report to the Governor and Legislature (March 1998), Homeless Housing Assistance Program application completeness checklist, award criteria, and point ranking.

A number of legislative amendments pertaining to policy changes in social service programs were collected and analyzed including the corresponding departmental regulations on program implementation.

Internal audits of agency bureaus and programs by the Office of the State Comptroller, the responses by an agency bureau to the internal audit including agency bureau internal memos. Various other reports from the Office of the State Comptroller were used regarding internal agency, bureau, and program audits.

Nonprofit contract budget documents submitted as part of the request for proposal, grant program definitions and policy guidelines, actual requests for proposals by program area, contract tip sheets by program area for program managers, contract final award agreements, contract preconstruction agreements.