

# Competition Policy and Human Services

Where Theory Meets Practice



ACOSS and CHOICE are passionate about the need for all human services to be equitable, affordable, of high quality, and sufficiently accessible so that people can live with dignity and control over their lives. There are major gaps between this vision and the reality of human services in many locations, for many cohorts of service users, and in many and various service sectors. The question is how to improve equity, affordability, access and agency in the most cost effective and efficient way while minimising potential risks of reform.

The potential extension of competition policy principles into new areas of human services delivery is currently the focus of significant attention by the Australian Government. The 2015 Competition Policy Review recommended expanding choice and competition principles into human services. The subsequent Productivity Commission inquiry final report identified a number of priority sectors for reform.

In this context, ACOSS and CHOICE commissioned a report, “Competition Policy and Human Services: where theory meets practice”, to inform the development of government policy. This brief was jointly developed by ACOSS and CHOICE based on the findings of the report. Our aim in publishing the report and this brief is to generate debate and inform government decisions about the use of competition to deliver human services.

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The report provides a framework for consideration of the likely impact of competition reform in different sectors which is informed by the experiences of non-profit service providers and service users. It also analyses Australia’s past experiences of introducing competition or contestability to human services. It reveals a strong tendency for decision makers to overestimate the benefits of competition whilst underestimating the risks of such reform, including the challenge of regulating human services. In all of the sectors examined, this has created unintended outcomes that have been detrimental to people accessing services, not for profit service providers and to the broader community as a whole.

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The report outlines an assessment process to be used in analysing the likely impacts of competition reform in a particular human services sector. The relationship between government, service provider and the service user is key in assessing the likely impacts of greater competition.

The report uses a framework introduced by Smith and Merrett to assess the benefits and costs of competition in human services in Australia. This analysis has considered two sectors where reforms to increase choice, contestability and competition have been introduced in recent years: vocational education and training (VET) and employment services.

The analysis indicates the importance of carefully assessing the specific demand and supply-side characteristics of particular sectors to identify the risks and opportunities of reform.

## Guiding Principles

In assessing the appropriateness of introducing competition (or further competition) into human services, ACOSS and Choice are guided by the following principles:

1. High quality and efficient human service delivery must be the primary objective for any reform.
2. Competition should not be assumed to improve service quality.
3. Governments have a duty to maintain and improve equity of access to essential services.
4. Human services must be affordable to all and free to those who can't afford to pay.
5. User control and service flexibility to meet individual needs should be maximised. Competition is not a precondition to increased user control.
6. The uniqueness of human services must be recognised, as well as the strengths of community-based not-for-profit providers in fostering cooperation and collaboration and providing diversity in service delivery.
7. Reform should facilitate cooperation and responsiveness to people and communities.
8. Services should be delivered cost-effectively. This does not mean at the lowest price but the aim must be to achieve the best outcome for the funding received.
9. There must be accountability to the community and to Parliament to ensure that the community knows what services they fund as well as their impact.

## Reasons markets fail in the delivery of human services

Our analysis suggests that there are a number of reasons that competitive approaches in human services often fail to deliver intended benefits:

- **Government must play a role in service delivery** – Government pays for the supply of services and, directly or indirectly, determines what services will be supplied, the amount of service supplied and the quality of service offered. Others, acting as agents for Government, deliver services. The preferences of people accessing the service are largely ignored in this process, particularly where they are a minority, marginalised or vulnerable group.
- **“Thin Markets”**- A “market” may be unable to support more than one or only a small number of suppliers due to limited demand, as may occur in rural, regional or remote areas (including Aboriginal and Torres Strait Islander communities) or in relation to some minority groups. Alternatively, there may be very significant economies of scale such as high overheads and/or extensive administrative processes. In other markets, participation by service providers is limited due to barriers to entry. These include regulatory restrictions, high sunk costs (costs that have already been incurred and cannot be recovered) and network effects (where increased participation in the network improves its value).

- **“Cherry-picking”** - Policy objectives of increased efficiency and improving quality do not necessarily work in tandem; they are often competing objectives. Constrained funding and payment incentives often result in service providers over-servicing sections of the market that need services the least and cost least (e.g. more highly qualified jobseekers in the employment services system) and the people who need the most assistance are the worst served in these scenarios (e.g. those who have been unemployed long-term).
- **Reducing staff costs by reducing quality of delivery** - Human services typically require humans to deliver care or a complex service. Given this, staff quality is extremely important. Staff continuity is often necessary to deliver more efficient care and to improve the quality of care, which is based on a person feeling comfortable and secure. Yet, one of the major cost inputs for the provision of human services is labour. This means one of the few ways for a service provider to maximise profit is to squeeze staffing quality or quantity.

- **Funding creates perverse incentives**

- For-profit firms, and even not-for-profit firms within a constrained funding structure, will maximise profit or income leading to perverse outcomes such as mis-selling of services to vulnerable groups (e.g. selling VET courses to groups that cannot reasonably complete the course) or reducing service quality leaving no or low provision of services to those who most need them.

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- **Inefficient operators do not always fail** - One of the accepted assumptions of competitive markets is that less efficient operators fail. This enables a reallocation of resources to those that operate efficiently in the expectation that welfare will be increased. This is less likely in situations where governments fund services and people are unable to influence outcomes through switching or genuine informed choice.
- **Market failure harms people** - Conversely, significant human costs accompany the failure of businesses delivering human services such as child care and residential aged care. Not only is an established relationship destroyed, alternative equivalent placements are rarely available due to high utilisation of competing services.
- **High barriers to entry for new providers** - Government responses to unintended outcomes tend to result in a constant state of regulatory flux. This in turn leads to risk management strategies (by both Government and providers) which favour incumbents over new entrants and discourage innovation. An initial expansion of provider numbers has typically been followed by contraction where competition reforms have been introduced. Exploiting economies of scale (some of which result from the complexity of the regulatory structure) is a key way in which ‘effective’ competitors can reap the benefits of their efficiency. For-profit providers face particular incentives to cherry pick, leaving less profitable segments for not-for-profit and Government providers.
- **High switching costs for service recipients** - Many human services involve the establishment of long term relationships between the supplier and the recipient of the service and these relationships may take quite some time to become established. Switching from one supplier to another destroys that

relationship. In other cases, switching may not be possible due to financial or other practical barriers (e.g. due to deposits needed for residential aged care). For these reasons, switching may be limited. However, in competitive markets, if switching does not occur, or occurs only in response to extreme circumstances, an important constraint is removed. Indeed, in competitive markets, switching may be forced upon service recipients when businesses fail or withdraw their services.

- **Low collaboration** - There are strong disincentives to collaborate, share information or share best practices in competitive markets. Whilst users of human services will commonly benefit from collaborative delivery approaches, providers are mostly motivated to provide an integrated approach only to the extent it involves related businesses in adjacent sectors.
- **People are not always able to make an informed choice** - For a well-functioning market to deliver outcomes it is essential that people accessing the service have choice, which requires the capacity to access and interpret useful information in a timely fashion. Frequently, the circumstances under which human services are procured will mean that this is simply not possible, for example in the case of a hospital emergency or crisis housing or in the case where people are unable to assess quality of service over a period of time before committing, such as with aged care.
- **Intermediaries (brokers) that benefit from sales rather than quality** – In complex markets there may be a need for intermediaries to navigate and interpret information in order to assist users to make quality assessments. However, such intermediaries are not always independent or able to act in the client’s best interests. The need for such intermediaries is arguably inefficient and represents a cost that should be factored in when considering the overall benefits likely to flow from increased competition. The risk of conflicts of interest also need to be assessed (e.g. where engaged by providers) and the impacts on access and equity (e.g. where those who can pay for the services of intermediaries privately).

## Framework for assessing the likely impacts of competition on human services

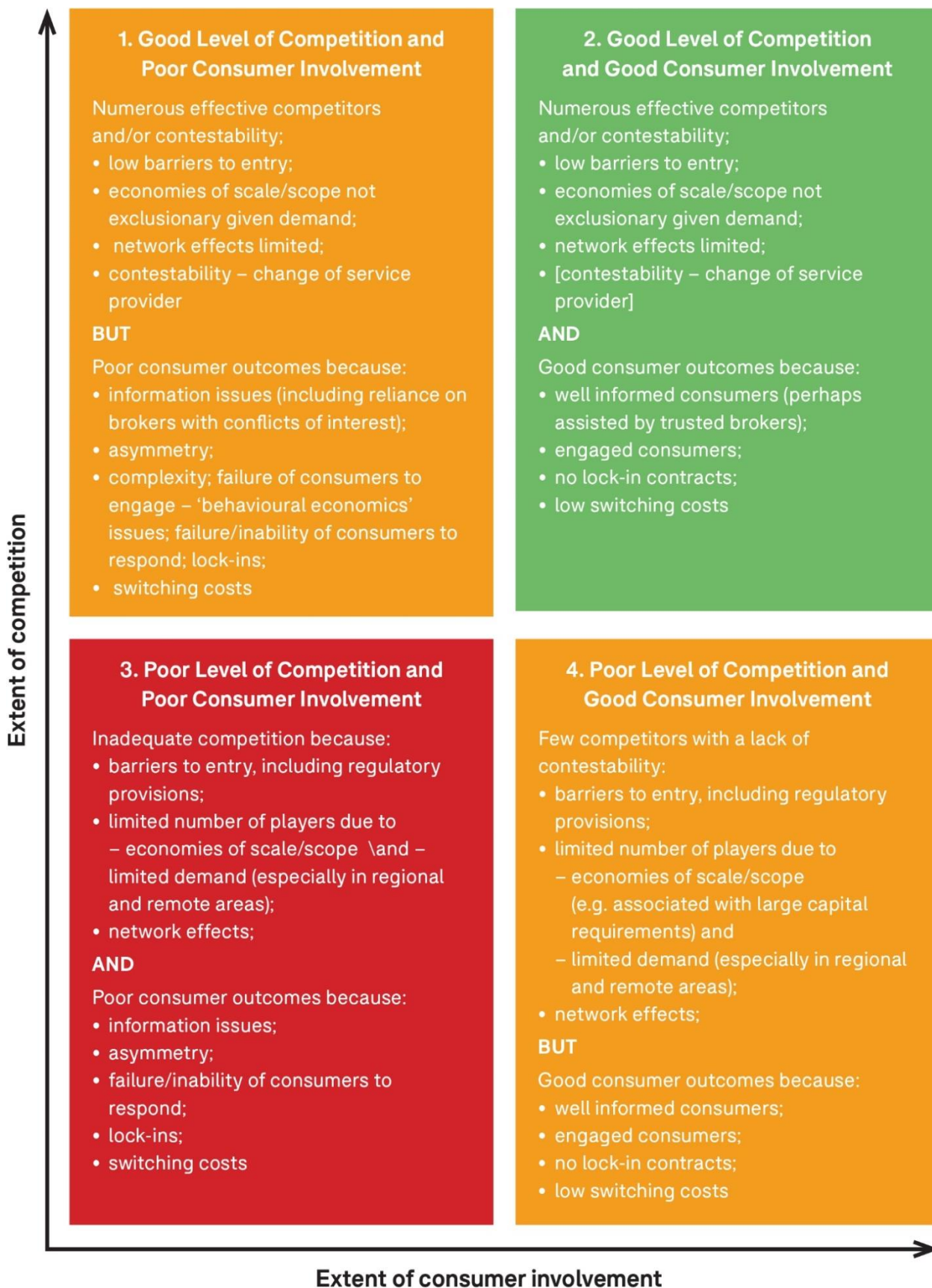
The report provides a framework, outlined below, through which to assess the impacts of competition in human services (Figure 1).

It is only when there are a number of providers actively competing and the people accessing a service are able to make informed decisions that the benefits of supply-side competition are potentially unlocked and good outcomes for people able to be delivered (Figure 1, quadrant 2).

In other words, a viable supply –side would entail numerous effective competitors; low barriers to entry for service providers; funding that incentivises quality; and no/low cherry picking, so that services are accessible to all. A service sector that lends itself to further competition would also demonstrate a viable demand-side, with features such as evidence of people being willing to, and capable of, making decisions; low switching costs; and no lock-in factors.

Service sectors that could theoretically lend themselves to further competition or contestability would demonstrate plenty of supply-side competition or contestability because entry barriers are low for new providers, and there is sufficient demand to enable numerous suppliers to operate viably. Finding examples of these services in human services is challenging, if not impossible.

Figure 1: Supply-side competition mapped in relation to consumer involvement





In the case studies analysed in the Smith & Merrett report, Vocational Education and Training (VET) and employment services align with Quadrant 1 (poor consumer involvement but some level of service provider competition) and they concluded that Residential Aged Care aligned with Quadrant 3 (poor level of competition and poor consumer involvement).

Quadrants 2 and 4 indicate situations of higher consumer involvement i.e. greater demand-side maturity. Quadrant 4 indicates services without a viable level of competition (for example, rural and remote locations that are under-served).

Ultimately, it is only service offerings that fall within Quadrant 2 that offer a viable balance between supply and demand, with a bona fide potential to offer desired social outcomes that are cost effective to government, viable to suppliers and beneficial to consumers.

## Conclusion

The report provides a useful lens through which to assess the impacts of competition in human services and inform current debate. It also speaks to the reasons markets fail in human services.

Overall, ACOSS and CHOICE consider that the report demonstrates that finding examples of areas of human service delivery that lend themselves to further competition or contestability is challenging.

Even when services are identified as viable, due to good consumer involvement and good levels of supply-side competition, analysis and careful thought is needed about whether competition is the most effective and efficient way to deliver good outcomes.

Once the costs of regulation, involvement of third-parties such as brokers and ongoing consumer education and engagement initiatives are factored in, competition in human services does not seem worth the costs.