



Productivity Commission Submission

NFP Sector

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1. Background

CTC Consulting Group Pty Ltd (CTC) is a management consultancy that provides a number of services to businesses primarily built around:

- Business Planning
- Research
- Operational Performance

Located in Newcastle, we service clients primarily on the east coast of Australia across almost all business sectors including the NFPs. Our clients include in the for-profit sector some of Australia's top 200 companies and some well known industry brands. Whilst in the NFP sector our clients include some well known names in the social welfare and health area.

As information and advice are at the core of the services we provide, CTC undertakes research into the market sectors in which we operate. This research is often client funded in addition to being self funded to ensure we stay abreast of the key issues.

Overall CTC promotes a philosophy of simplicity and efficiency based on our three core business operating principles being:

- Determine the capabilities a business requires and then recruit the people who have these capabilities – Right People

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- Develop the systems and procedures that enable the people to achieve the business objectives – Process
- Monitor and review the performance of people and process – Performance Management

Given these operating principles we are always actively contributing to the debate on waste and unnecessary duplication. As such we are keen supporters of the drive to improve energy efficiency and the elimination of unnecessary tiers of government.

In the NFP sector we see great variability in performance and therefore levels of efficiency in the delivery of social services. The extent of variability is perhaps no better or worse than is seen in the for-profit sector. However the special status offered to the NFP sector, can have the effect of diminishing the net benefit to the communities that NFPs aim to serve.

Duplication or overlapping purpose that results in excessive administration and operating costs diluting the value of donations is a major issue. This underpins a number of cascading issues that result such as:

- The size, availability and therefore the divvying up of the donations across the myriad of NFPs
- The size, availability and therefore the divvying up of government funding

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- How social need is prioritised and how funding is channelled to the area of greatest need
- When revenue from donations and government funding are insufficient to support the purpose, this can, at times, drive NFPs to develop other revenue generating mechanisms which are non core
- Increased complexity of NFPs that operate non core businesses to boast revenue shortfalls that undermine achievement of purpose
- Management and board capability to manage increased complexity and the sometimes competing demands of fulfilling purpose and operating a business or social enterprise

When NFPs have a clear purpose, and have a clear and simple process for funding fulfilment of their purpose, they can provide the most efficient solution to the delivery of social services. When purpose becomes confused by complicated funding mechanisms, and where social purpose takes a back seat to a fight for survival, NFPs can become very inefficient options for delivery of social services.

These are the issues that we will bring to the fore in our submission which at its core raises the question of the definition of an NFP, how this definition is administered and therefore how this special status is applied.

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2. Scope of Submission

The focus of our submission is on NFPs that provide welfare rather than clubs or sporting organisations. These NFPs may provide services to the elderly or disabled, the ill or injured and the mentally ill or the socially disadvantaged. Our submission is general in nature and therefore is not based on any given organisation, but moreover a view based on our exposure either directly through our work with NFPs, or indirectly as a result of our research.

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3. NFP Purpose

It is worth making some a simple comparison between the number of charities in Australia and those in the USA and Canada to gain some insight into the level of NFP service capacity. These countries are selected as US charitable practise and method are studied and at times applied by Australian organisations, while the size and demographics of Canada are similar to Australia and can provide a sensible benchmark. Whilst the following figures are based on charities, and therefore exclude many NFPs, they provide a sound basis for comparison.

Table 3.1: Numbers of Charities by Head of Population

Country	Population	Number of Charities	Population Per Charity
Australia	21m	297	70,707
USA	300m	5,324	56,349
Canada	33m	251	131,474

Source: The Book of Charities websites Australia and Canada. The Charity Navigator website in the USA

While it is necessary to identify community service needs and compare this to service delivery from private, public and NFP sectors in order to identify whether or not NFP service capacity is too high or too low, this data indicates that Australia may be well serviced and perhaps over serviced by charitable organisations and by inference NFPs in general. It is likely case for rationalising NFP service capacity is likely to exist. This begs the question “what has driven this level of per capita NFP activity in Australia?”

The number of “special” purpose “welfare” NFPs have increase over the past decade. These organisations have emerged to niche service community needs as government funding and services have shifted. The aim of these “special” purpose NFPs has been to increase community awareness for their particular issue, to increase pressure on government to provide funding and/or services and attract community support and donations. These NFPs are both lobbying organisations and revenue generators that channel funds to support their “special” purpose aims.

These new NFPs compare with older more established organisations that can trace their origins back to the Great Depression, international links or religious affiliations. Many of the older established NFPs provide a broader range of “welfare” services. These “welfare” services may include various levels of relief to the financially disadvantaged, for the aged, for education. The assistance is usually based around a purpose or objective of reducing reliance on welfare.

In general terms “newer”, “special” purpose NFPs are more health focused. Whilst the “older”, “broader service” NFPs are focused on developing self reliance. There are however overlapping aims and/or purpose both between and within these organisations. At the core of all of these NFPs is the fundamental purpose to improve the situation of those people who are unable, for various reasons to provide themselves with an “acceptable” quality of life.

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Whilst this may be a fundamental aim or purpose it is clear when reviewing the number of these NFPs, and in dealing with them, that they have very different priorities and views on how this fundamental aim can be achieved. These differences in our view have resulted in a blurring of purpose and rigidity in approach that to a degree has fuelled the growth in NFPs. This growth has in some instances lead to improvements to the lives of some, but at the same time, added to the complexity and therefore a decline in effectiveness of NFPs to deliver against their core purpose.

As government funding and the “donational dollar” is increasingly spread across a growing number of NFPs, turf wars are beginning to emerge as some NFPs try to protect their “patch”. In the for-profit sector the usual evolution of a market will result in a point where competitors will need to be acquired simply because a market cannot sustain everyone. In the NFP sector the obvious need for rationalisation is being strenuously resisted and whilst this resistance continues, performance around core purpose is perhaps declining.

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4. Funding Mechanisms Supporting Achievement of Purpose

In the previous chapter we proposed our view on the growth in NFPs, and the resulting competition for funding both from government and the public.

Funding availability is a constant issue for NFPs regardless of the era. However, there is a case to be made that this decade and particularly the present time has heightened the issue as a result of a number of compounding issues such as;

- Growth in number of NFPs and the resulting demand on the “donational dollar”.
- Increase in costs as a result of an aging volunteer workforce, and the new generations much lower engagement in community work.
- Increased compliance and regulatory requirements meaning that NFPs are no longer excused for poor OHS and E performance.
- Increased overheads as NFPs are forced to employ people with for-profit experience to meet compliance requirements.

Whilst there is no doubt many other factors, these four we argue are at the core of what has driven NFPs to pursue other revenue mechanisms to address funding shortfalls.

These additional funding mechanisms in some instances may have simply been a decision to introduce a fee or charge for existing services. In such cases an assessment may apply so that severe hardship cases are provided free with charges in all other instances being heavily subsidised.

In some cases the funding may come from government who are essentially paying a fee or charge for the services being provided. In such instances the organisation may need to raise donations to strengthen its financial position to ensure long term sustainability, something often not factored into government funding formulas.

In the above examples, the NFP is not moving too far away from its core purpose via the delivery of its service. However, in other instances NFPs have been either driven or attracted to other funding mechanisms to make up shortfalls needed to support core services and or purpose. The following lists some examples of these alternate or additional funding mechanisms:

- Employment Services
- Aged Care Services
- Medical/Health Care Services
- Recycling businesses, typically focused on clothing

In a report called “Giving Australia” conducted by the Department of Family and Community Services and the Prime Ministers Community Partnership, 500 NFPs were surveyed. In the resulting report it was

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stated that some 29% of NFPs operated a commercial venture or social enterprise. In 87% of these cases the venture was an extension of services that the organisations provide as part of their primary purpose and mission. However we suggest that the NFP range of services has not only grown in part because of demand due to declining government services, but also as NFPs have been convinced of the opportunity to raise revenue through low cost ventures for “social” or “community” services.

The move into employment services is a very clear example. The opportunity to assist people to find work and earn a fee from government appeared to fit nicely with core purpose whilst providing an opportunity to earn additional funds. It was clear that some NFPs were aiming to make a “profit” from these services that could be directed to other activities. The experience for many NFPs was quite the opposite. Those that won long term unemployed contracts had to inject additional funds beyond government case fees to achieve outcomes. In these situations some NFPs were trapped by their social values, from which government benefited by shifting part of the cost for the long term unemployed to the NFP providers.

The fee for service model has driven a more “business-like” approach that some in the sector say has resulted in a harder edge. Social enterprises behaving like “business” is of concern to many, as they fight for survival at a time where there is a growing need, diminishing direct government services, increasing costs, and increased competition for the “donational dollar” – all of which is driving demand for improved

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performance. As such there is an increasing view that delivery of services to the needy is being lost or overwhelmed by the drive for efficiency, cost control and revenue (funding) – all of which sounds very business, rather than charitable like.

This type of environment results in high levels of demand on low paid staff. The corresponding effect is that as some staff have found these changes difficult and left the sector, they have been replaced by others with higher remuneration expectations. In turn this has placed pressure on costs. Additionally expectations of volunteers are increasing with volunteers becoming harder to find. As such, some NFPs have chosen to employ paid volunteer supervisions/coordinators to actively seek out new volunteers and lead existing teams to achieve improved outcomes. These organisations have accepted the higher cost of paid supervisors but appear to have achieved greater overall outcomes as a result.

The drive for increased “professionalism” fuelled by increasing costs to operate and pressure on revenue has lead some NFPs to develop a competitive approach. This competitive approach has been adopted to ensure that they position themselves to extract as much funding as possible from the government in addition to maximising their share of donations from the public.

Increased professionalism and therefore competitive behaviour by some NFPs have made it more difficult for those that have not made these changes either by choice or as a result of limited resources to do

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so. The larger and more professional NFPs have also been able to use their “brand” by forming partnerships with large corporations who are attracted by the “image” benefits that they believe will be derived. As a result, those NFPs that have not been able to make these changes are being drowned out by these new re-engineered NFPs in addition to a rush of new “special purpose” and in some cases “celebrity” NFPs.

The consequence for some is that they are facing financial difficulty and a very real threat of collapse. Yet, despite this stark reality there remains great resistance to self initiated rationalisation in the sector. There is almost a culture at work in the sector that implies, “if we can't survive as our own identity, we won't survive at all”.

As such, scant resources can be lost to the sector which may otherwise have been saved had it not been for a willingness to embrace a broader purpose that could accommodate others. We can only see pressure intensifying for many NFPs as they struggle to survive clinging to falling revenue mechanism such as, for example recycling. In the employment services industry, NFPs have been the new entrants largely taking a share of the business not wanted by the for-profit sector. However, in recycling NFPs are the incumbents, particularly in clothing, but are now being threatened by the newcomers, being the for-profits.

Waste management is big business and with increased pressure on landfill, recycling is the new growth market for the for-profits. Many of the for-profits are capable of providing extensive recycling solutions for councils unlike the limited and selective focus of the NFPs. This growing

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reality coupled with cheap clothing from China and the declining quality of recycled product is placing pressure on this funding mechanism.

The sustainability of these other funding mechanisms to support core purpose is therefore in doubt. This along with the increase in competition for government funding and the “donational dollar” further evidences the need for rationalisation in the sector.

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5. The Purpose Conflict

In Chapter 4 we explored the funding mechanisms that support achievement of purpose, the pressure these funding mechanisms are coming under, and the implications for the NFP sector that are arising as a result. The inevitable consequences we referred to in Chapter 4 are that some NFPs will not survive these pressures. The reluctance to pursue rationalisation raises the issue of “purpose” conflict.

The “purpose” conflict is brought about by the fight for survival, with the survival purpose competing with the real purpose for existing. The survival of the organisation increasingly becomes the focus as those NFPs that are most vulnerable rush to restructure and or reinvent themselves. The survival focus continues to support the drive to adopt a more “business-like” approach and with it, more competitive behaviour. As such many NFPs have worked hard at redefining themselves, so as to provide the community a clearer message as to who they are and what they do. In some instances this has resulted in a change or modification of purpose to avoid being confused with other “market offers”.

The tighter definition of purpose may result in communicating a clearer message to the public, but it has also resulted in a reduction in the extent of services or the extent of services that are provided for free. In turn there is an increased emphasis on achieving a contribution from those services or activities where a fee/charge is applied.

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The paradox created by this action is a resulting gap in what is being provided where community needs are not being met resulting in new “special purpose” NFPs emerging. In filling the gap these “special purpose” NFPs add additional competition. The ease by which NFPs can be established simply compounds the situation.

The sheer number of charities, let alone NFPs as referred to earlier for a country our size must reach a point where it becomes unproductive. Duplication of overhead and or administrative function, and overlapping purpose can only result in less resources available to help those that the NFPs were established to assist. In any sector where there is an explosion of service providers; there is inevitably a period of correction, where rationalisation takes place. In the NFP sector this period has come despite much resistance.

The ease of achieving NFP status has somewhat mimicked the availability of cheap money that fuelled unsustainable growth worldwide, providing a catalyst for the current global financial crisis. Whilst government policy isn't necessarily the cause for this type of unsustainable growth, it can unintentionally add to the size of the problem.

NFPs have a duty to the community for the special status they enjoy. As such NFPs need to have a structure and mode of operation that is sustainable and is therefore capable of fulfilling their social purpose. Whilst the commitment by an entity to devote energy to help the disadvantaged is to be applauded; it is less desirable for all involved if

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the mechanism for supporting its achievement of purpose is flawed. The result is that funds via perhaps government grants, public donations and other sources are diverted away from more sound organisations resulting in an overall dilution of services and therefore benefit to the community.

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6. Management and Boards

Whether it is seen as a negative by some elements of the NFP sector or not, the reality of the current environment is that NFPs have had to become more “business-like” to survive. This situation has created a recognised need to improve the skills of management. To achieve this NFPs have increasingly sought to recruit from the for-profit sector. This has perhaps led to a clash of cultures as a more results orientated managers have encountered a far more pragmatic and forgiving culture in NFPs.

Boards have also had to reassess the mix of skills and experience required to operate in a more challenging and complex environment. Many of these boards remain voluntary which presents its own challenges, especially given that now the regulatory environment can result in board members being personally liable for the actions of the organisation. This fact is in many instance not understood, with many NFP directors being surprised when their personal liability for issues such as OHS and E are highlighted. The tendency for voluntary boards to be unaware and then surprised by their responsibilities is somewhat driven by the view that volunteering absolves people from prosecution. If you follow this view to its logical conclusion, it suggests that lower levels of performance and compliance are perhaps acceptable across the wider organisation.

An increased understanding of director’s responsibilities is being developed and there are some outstanding examples. Often though

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the drive for greater awareness of the board's responsibilities results from a change at CEO or GM level, where these roles have been recruited from the for-profit sector. This of course presents complications for the new management that often experience resistance to change not only from below, but also from above.

New management will often require more reporting to enable better analysis of performance. This approach drives greater levels of responsibility and accountability. This kind of management will typically question the value of certain activities and begin to question aspects of the organisations purpose. Financial sustainability is often the catalyst for such debate, with any proposal for change or modification to purpose usually being met with resistance.

This potential conflict between boards and management can and has placed many NFPs into a "strategy" limbo, leaving management of these NFPs left with one option to maintain services by reducing costs. As the struggle for share for funds becomes harder, the cost of capturing donations increases.

All this leads to resource poor organisations struggling to fulfil their purpose. This situation is not likely to abate given that the operating environment is continuing to deteriorate. This only intensifies the need for NFPs that find themselves in a strategy limbo, to re-open debate on who they are, what their core purpose is and how best this can be achieved. Perhaps then, amalgamations, partnerships or other such options might be given the consideration that is clearly required.

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7. Conclusions

The NFP sector clearly faces a number of challenges consisting of:

- Growth in the number of NFPs competing for community funds.
- Increased costs of compliance and dealing with regulatory complexity.
- Increased costs associated with recruiting the management skills required.
- A diminishing volunteer workforce.
- Increased operating complexity resulting from having to explore and adopt alternate funding mechanisms.
- Threats to the sustainability of existing commercial operations.
- Unforeseen cost and liabilities associated with taking on new commercial opportunities.
- Complex and conflicting regulatory requirements at all levels of government

This environment has resulted in a fight for survival for some at the very worst, and at the very least increased difficulty in fulfilling their purpose. Overlapping purpose and duplicated administrative structures will inevitably result in a less efficient delivery of services to the disadvantaged resulting in purpose conflict – survival versus social responsibility.

There is a need for boards and management of NFPs to effectively assess their purpose, what is required to sustain achievement, and the

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effectiveness of the organisation to adapt to the resulting changes. Such a review will in many instances highlight the vulnerability of many NFPs unless they explore options such as partnerships or amalgamations.

Government needs also to review regulation associated with the issuing of NFP status. In addition government regulation should try to minimise complexity at all levels of government. A reporting regime that ensures compliance to NFP status needs to be simple and should also include a purpose effectiveness and community assessment. However, such reporting requirements need to be constructed so that compliance costs don't excessively divert resources away from achievement of purpose.

Government also needs to apply an effectiveness and or sustainability test to its funding activities to NFPs. This needs to take priority over popularity based funding that whilst vote winning, often only fuels the proliferation of NFPs adding to the potential inefficiency. This change is undoubtedly significant but inevitably unlikely.

Government needs to direct funding based on greatest benefit for the community and effectiveness of service delivery. NFP status needs to be assessed against ability to deliver against stated purpose. These measures should contribute to building a stronger, more effective and sustainable NFP sector.

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The NFP sector has provided the community with a low cost non government welfare service. Government has clearly taken advantage of this over many years and in particular the past decade. However, the current number and duplication perhaps offers a lower level of effectiveness when compared to re-instituted government services supported by higher taxes. Only if the benefit and effectiveness of NFPs is better assessed than it is currently, can we be assured of an NFP sector that can deliver these services more effectively than government.

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8. Recommendations

- Government needs to apply a community benefit and effectiveness test to organisations applying for NFP status.
- Performance needs to be assessed against an NFP's ability to deliver against its stated purpose.
- Government funding needs to be directed based on an assessment of community benefit and effectiveness to deliver.
- Government needs to encourage NFP rationalisation through funding policy.
- Support should be given to NFPs to review their sustainability and explore new organisational structures such as mergers or partnerships.
- Regulation of NFPs should ensure that directors and management are aware of their personal responsibility and liabilities.
- Incentives should be explored to encourage for-profit enterprises to provide "volunteers" from their staff to work in NFPs on exchange programmes to assist skills development in NFPs and general improvement in greater community awareness of the plight of the disadvantaged.
- Adopt an NFP programme should be encouraged by government so that for-profits are encouraged to proactively seek partnerships with NFPs.