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The Promise and Pitfalls of Performance-Based Contracting

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Introduction: Why This Paper and Why New York

In fiscal year 2002 New York City agencies entered into 4,630 new contracts, totaling $8.3 billion. Of that number 1,950 contracts, amounting to $2.1 billion, were for the provision of human client services, such as day care, senior centers, counseling and the like.

> Testimony of New York City Deputy Comptroller Greg Brooks before the New York City Council Committee on Contracts, January 22, 2003.

Unlike uniformed services, in which almost all the work done is by city workers, the social welfare and health agencies depend in large part on contractors. The seven largest such agencies have $3.5 billion in contracts and these represent 33% of their total budgets. Most of these are with nonprofits. In addition, the new Department of Education has well over $1billion in approximately 1,300 contracts for such services as transportation and schools for special needs.

> Gotham Gazette.com

This paper is about the interaction and intersection of two important trends in the delivery of government services, especially human or social services. The first trend is contracting services out to non-governmental organizations. The second is using outcome-based performance management techniques to improve the work of nonprofit service providers, which increasingly operate under government contracts. Both trends have important implications for contemporary efforts to reform and strengthen human services.
The paper focuses on how these two trends have played out and continue to do so in one setting – New York City. Very often, it is the gargantuan scale of New York's human service infrastructure that commands all the attention. This is not surprising; the magnitude of human service transactions in the city is remarkable. For example, according to *GothamGazette.com*, New York "has more than 18,000 contracts worth some six billion dollars, a sizeable chunk of the city's total $43 billion expense budget."

But once we look beyond the sheer scope of activity in New York, it becomes easier to see that the city is marked by some distinctive traditions and patterns of service provision that are increasingly relevant for jurisdictions of many different sizes throughout the U.S. To start, the widespread practice of establishing partnerships between government and nonprofit groups, which is only starting to take hold in other jurisdictions, already has deep roots in New York.[1] One illustration: For decades in New York, the nonprofit Catholic Charities, the Federation of Protestant Welfare Agencies, and the Federation of Jewish Philanthropies have been major-- arguably *the* major-- providers of government-funded child welfare services, and more recently, of a wide range of other human services to low-income groups.[2] Meanwhile, elsewhere in the U.S., the policy interest of the current Bush administration in opening the contracting of human services to religious organizations – the so-called "faith-based initiative" – has been described by both its proponents and opponents as a significant innovation.

New York's tradition of using nonprofits to deliver social services is well over 100 years old. In 1914, 22 states appropriated no funds at all for privately managed charities and in those that did so the amounts were small – for example, $15,000 in Kansas and $70,000 in Kentucky. But 15 years earlier, in 1891, the patterns were already very different in New York City, where 200 private agencies were receiving $2.6 million from public subsidies.[3]

Turning to near-contemporary and contemporary times, we can see signs of the continuation of New York's distinctive reliance on nonprofits for human service delivery. For example, writing in the early 1990s, political scientists Smith and Lipsky, in <u>Nonprofits for Hire: The Welfare State in the Age of Contracting</u>, described government contracting for human

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[1] While New York is especially notable in its reliance on nonprofits, the pattern appears to be generally most pronounced in the entire northeast region of the U.S. Lester Salamon reports that nonprofit organizations and even nonprofits per capita are much more prevalent in this area of the country than in others. Lester A. Salomon, America's Nonprofit Sector: Primer (second edition, The Foundation Center 1999

[2] Of course, these agencies also invented agency-provided foster care services and others before there was government funding to support them.

[3] Smith and Lipsky, 49.

services as a new and somewhat troubling development, but acknowledged that New York already had a long history of using this approach.[4] They reported that "in 1987 in New York State, 87 percent of all those employed (an estimated 143,000 employees) in the social services field worked in nonprofit agencies."[5]

Another measure of the prominent role of New York's nonprofits in this area is the scope of municipal government contracting for human services. A large and regularly published document called "The Mayor's Management Report," which will be discussed in more detail later in this paper, shows the dollar value of human service contracts for the city's governmental human service agencies. The following table from the preliminary "Mayor's Management Report for Fiscal Year 2003" indicates that the proportion of contracting for human services varies considerably across government agencies but that in all cases the scope of activity is substantial.

Table 1 [6]

City Agency	Human Services Contracts	Total budget
Department of Health and Mental Health	$ 874.0 (66.3%)	$1,318.7
Human Resources Administration	650.6 (10.9)	5,972.6*
Administration for Children's Services	1,368.3 (57.6)	2,375.1
Department of Homeless Services	358.5 (71.3)	540.4
Department of Employment	79.5 (58.5)	135.9
Department of Aging	179.7 (77.7)	231.2
Department of Youth and Community Development	126.6 (82.7)	153.0
Total	$3,637.2 (33.9%)	$10,726.9

[4] While Wallace Sayre's and Herbert Kaufman's classic Governing New York City: Politics in the Metropolis, (WW Norton, 1960), written in the late 1950s does not mention contracting for services, the book devotes an entire chapter to "Nongovermental Groups and Governmental Action."

[5] Steven Rathgeb Smith and Michael Lipsky. Nonprofits for Hire: The Welfare State in the Age of Contracting. Harvard University Press, 1993.

[6] "New York City Mayor's Management Report, Fiscal 2003 Preliminary Report"

* This includes funds devoted to direct benefit payments to 430,400 Public Assistance clients, 820, 500 Food Stamp recipients and 2,028, 100 Medicaid participants.

Overall, as the table indicates, one-third of the expense budgets of the city's human service agencies are contracted out. And if the direct benefit payments made by the Human Resources Administration (HRA) under Medicaid and TANF (Temporary Aid for Needy Families – public assistance) are excluded, the data indicate that the agencies spend almost two-thirds of their budgets (62.8 percent) on contracts for human services. In Remaking Federal Procurement, Steven Kelman observes that in agencies that contract out central activities, such as information technology applications, that are crucial to running their operations, "*contracting* ***management*** *must be considered a core competence of the organization.*"[7] **(**Emphasis in the original**)** One of the questions this paper will examine is the extent to which New York City's human service delivery system has shared Kelman's appreciation of the capacity needed for managing contracts.

New York City's history of *measuring and managing* the performance of governmental and nonprofit agencies is by no means as venerable as the city's heavy reliance on nonprofits for service delivery. Nevertheless, as this paper will show, the city has also been a trailblazer in this area, experimenting earlier and often more actively than other jurisdictions with methods of assessing what service providers do and holding them accountable for their performance. As we shall also see, the pace and vigor of work has been uneven, suggesting lessons about the degree of follow-up and attention that is needed to bring performance measurement and management systems to maturity.

In all, then, New York has been and continues to be an intriguing laboratory for activities that are almost certain to be increasingly important to both government entities and nonprofit agencies -- and ultimately to the people they serve. To develop a closer-up picture of what we can learn from this laboratory, this paper provides some background on the development

[7]Steven Kelman, Remaking Federal Procurement, Visions of Governance in the 21st Century, Working Paper. No. 3, Kennedy School of Government, 2001.

of performance management and measurement practices in New York and then draws on a survey and contemporary case studies to discuss how these practices are now being used. To set that information in context, the paper first offers a brief definitional discussion of performance measurement and management and performance-based contracting.

The Lexicon of Reform: Unpacking the Concepts of Performance Measurement and Management and Performance-Based Contracting

Wherever there is or has been government, there has been government performance. But how good is that performance? The truth is that for a long time nobody knew – or to be more precise, nobody had very much systematic information with which to answer the question. From the vantage point of today's world where government and nonprofit groups regularly use terminology like "assessing outcomes" or "measuring how well goals and objectives are met," it is instructive to recognize that until quite recently the practice of measuring performance to strengthen it was mostly uncharted territory. Writing in the early 1970s, the sophisticated policy expert Alice Rivlin[8] endorsed the value of this approach in terms that today sound almost self-evident:

> *It therefore seems to me that analysts who want to help improve social service delivery should give high priority to developing and refining measures of performance. Relatively little effort has gone into devising such measures so far, despite their importance and the apparent intellectual challenge of the task... Performance measures for social service are not, of course, ends in themselves. They are prerequisites to attempts both to find more effective methods of delivering social services and to construct incentives that will encourage their use.*

At this early stage, Rivlin was already well attuned to what she had identified as "the … intellectual challenges of the task." She cautioned against confusing different dimensions of the overall concept of *performance*, particularly *effort* and *achievement*, with one another. Her

8 Systematic Thinking for Social Action. 1973.

warning continues to be well worth heeding, because when we talk about *performance*, we may mean: an *input*, an *activity* (or effort), an *output*, or an *outcome* (achievement).

There was a time when evidence of "performance" in the field of job training would have been "dollars appropriated or spent" (an input), or number of training courses offered (an activity). An advance in performance measurement occurred when agencies and program began reporting the number who attended or -- even better -- graduated from training courses (output). The last stage in developing indicators of performance was asking and answering such questions as: "Did the trainees get a job -- or keep the job for three months or a year? And what kind job did they get?" It was these kinds of questions that led to measuring outcomes. Outcome measurement was introduced in the job training field relatively early, where it was applied to programs like the federal Job Corps initiative, but it is only recently, if at all, that it has been used in many other areas of human services.

The four dimensions of performance measurement – inputs, activities, outputs, and outcomes -- are causally linked: The nature of an organization's input into a particular undertaking affects the nature of the activity associated with the undertaking, and so on. At the same time, each dimension is distinct. Moreover, performance measurement can focus on any and all of these dimensions, and has done so. And as Rivlin observed, a common mistake – particularly in the early days of performance measurement but even now -- is to equate measuring effort with measuring achievement.

There are other important distinctions. As this paper will show, it is not always well recognized that performance measurement, while necessary, is rarely sufficient for improving performance. A related but different strategy, *performance management*, builds on measurement by using the information that emerges from an assessment to plan, implement, monitor, and further evaluate performance, and to hold managers accountable for doing so. And finally, of course, performance is affected by the political and fiscal context in which it occurs and by constraints that are often wholly outside of the control of the government and contracting organizations directly involved in service delivery.

Performance measurement and management techniques can help organizations improve their own operations, but the story gets more complicated when the organization responsible for a particular operation or service is a subcontracted vendor not in the direct chain of command of the public agency that has asked that organization to do something. In that case, the government agency needs some mechanism of control to ensure the quality of the performance. Increasingly, that mechanism has been a *performance-based contract* (or PBC). This kind of contract builds on performance management techniques, but adds the critical factor of financial incentives that reward organizations for good performance and sometimes penalize them for failing to achieve outcomes. As with performance measurement and management, the focus of performance-based contracting can be on inputs, activities, outputs, or outcomes. However, even though outcome measurement is by no means a universal practice among organizations that measure performance, in the past decade there has been a dramatic shift toward outcomes as the dimension that really matters for performance-based contracting.

Finally, there are *performance-based budgets* – budgets that show not only how funds will be spent but what outcomes the expenditures are expected to help produce. For government agencies and nonprofit organizations that decide to develop these budgets, the complexity of performance-based contracting is compounded yet again, because more than one government entity (and occasionally private supporters) usually need to be part of the process. Thus, in contrast to performance-based contracting, which usually involves agreements between service providers and single agencies within the executive branch of government, [9] performance-based budgeting – like most budgeting in the governmental arena -- ultimately

[9] Except of course in those cases where the courts are deeply involved in the administration of government agencies, not such a rare occurrence in New York City, but a dynamic beyond the reach of this paper. See Ross Sandler and David Schoenbrod, Democracy by Decree: What Happens When Courts Run Government, Yale University Press, 2002.

must take into account the activities of multiple agencies. Furthermore, the practice depends on negotiations between the executive and legislative branches of government. The challenges and issues raised by performance-based budgeting, which have been well addressed by Allen Schick[10] and others, are part of the discussion of how to improve the performance of service providers but are beyond the scope of this paper.

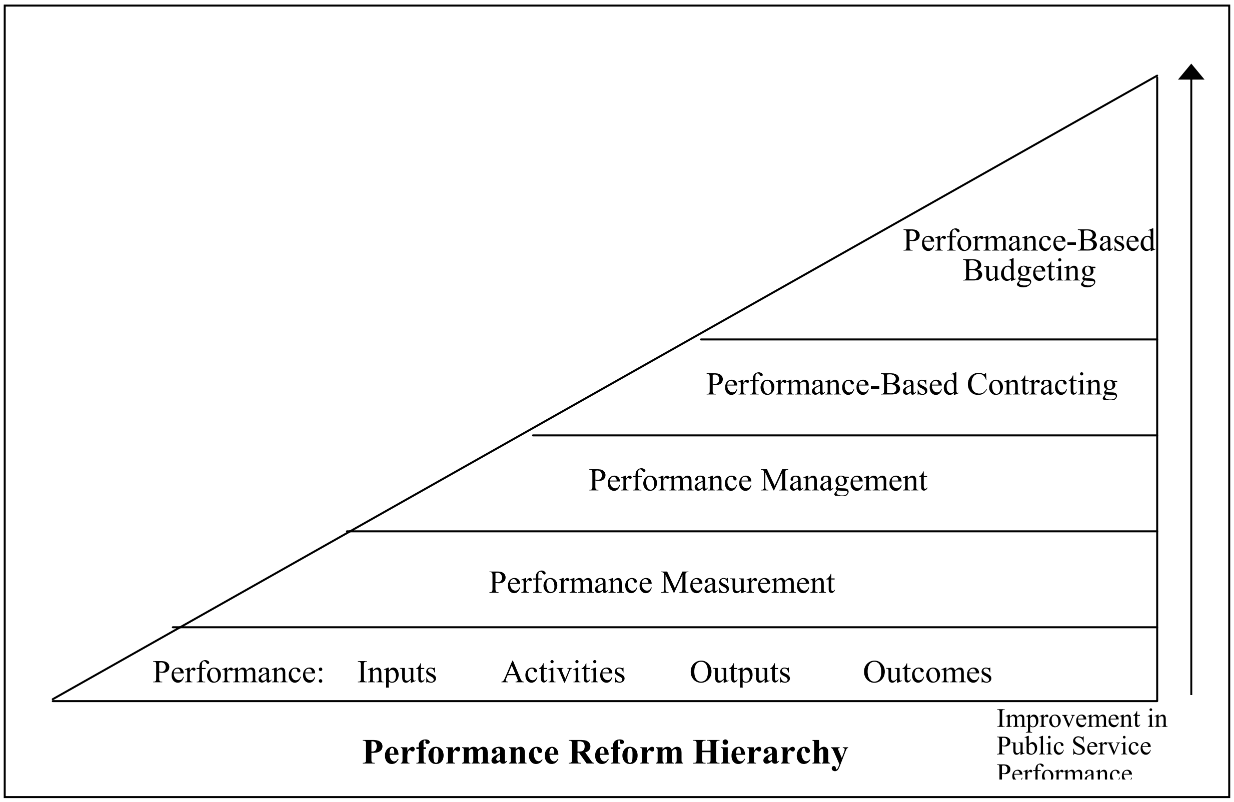

Figure 1

Figure 1 is a graphic depiction of what has just been discussed. The bottom row of the figure shows that the performance of service providers has several different dimensions. Significantly, those dimensions – inputs, activities, outputs, and outcomes -- can be turned into a so-called logic *model*, which provides a schematic representation or map of what is required to produce the desired outcomes. The ascending column indicates that systematic

[10] "Getting Performance Measures to Measure Up" in Quicker, Better, Cheaper?: Managing Performance in American Government, Dall Forsythe, ed., SUNY Press Albany, 2001.

efforts to improve performance consist of several different, causally related types of reforms or sets of activities. The Figure's arrangement of those reforms into a hierarchy highlights two points. First, starting with performance measurement at the bottom, each set of activities is a foundation for the next. Second, the reforms build in complexity: Measuring performance requires certain skills and certain actors; performance-based contracting requires those same skills and actors, plus more.

Keeping this hierarchy in mind may be helpful in examining New York's experience with performance-based measurement, management, and contracting. The paper now turns to that experience.

The New York Experience

Experiments in Performance Management

The Mayor's Management Plan and Report System

During the period of its recovery from the fiscal crisis of the early 1970s, the City of New York created a planning and management tool called Mayor's Management Plan and Report System (MMPRS). First used in 1977, the system still exists, with its major manifestation being the twice-yearly publication of "The Mayor's Management Report" (MMR).[11]

According to the "Mayor's Management Plan and Report System Manual," which was issued in 1986:

> *The MMPRS is carried out by individual agencies under the direction of a designated Management Plan Coordinator, and monitored and administered by the Mayor's Office of Operations. The MMPRS allows for development of an annual agency plan, including a review of agency* ***mission*** *and* ***programs*** *which define the job of the agency,* ***performance plans*** *which determine how well and how much of the job is to be done, and planned* ***improvement projects*** *which detail efforts being taken to upgrade service delivery or operations management.*[12]

In fact, as several studies documented, until the current mayoral administration, little of the system's potential as a management tool was realized. In one sign of the under-use of the potential, colloquially the system is referred to as the "Mayor's Management Report," or MMR, instead of the MMPRS, because little of the prescribed process has been operational citywide except the Mayor's Management Report.[13]

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[11] In a significant advance in providing government transparency to the public, the current mayoral administration of Michael Bloomberg has put the MMR—and other agency performance data-- on the NYC.org website.

[12] The Mayor's Office of Operations produced a guide ,"Mayor's Management Plan and Report System Manual," in 1986. Consistent with the City's low level of investment in training managers to use the MMPRS, by 1989, Smith's study of the MMPRS had found that virtually no actor interviewed, including staff in the Mayor's Office of Operations itself, had ever heard of this highly informative manual.

[13] Dennis C. Smith ,"Performance Management in New York City: The Mayor's Management Plan and Report System in the Koch Administration." Paper presented at the 15th Annual Research Conference of the Association of Public Policy and Management (APPAM), Washington, D.C., October, 1993.

Thus, the New York City government, which had pioneered the development of performance measurement in large cities, with rare exceptions, was not using those measures in any systematic way to manage performance.[14] The important lesson of this experience is the following: Without an explicit commitment to make it happen, performance measurement, while arguably useful in its own right, does not automatically produce systematic performance management.

In an example of good intentions without enough will to translate them into action, the New York City government had pioneered the development of performance measurement in large cities, but then, proceeded not to use those measures in any systematic way to manage performance.[15] Among other limitations, city agencies chose to measure and report on outputs and activities, not outcomes, the important lesson is that without an explicit commitment to make it happen, performance measurement does not automatically produce performance management.

It is interesting to see how New York's MMPRS experience has been paralleled at the federal level. Studies conducted by the General Accounting Office (GAO) suggest that like MMPRS, the enormous effort to implement the federal Government Performance and Results Act (GPRA) by 1999 was focused on measurement rather than management, and had largely not changed results.[16] Typifying GAO findings on GPRA implementation, a GAO report issued in May, 2001 observed that many federal agencies had not succeeded in developing an

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[14] The process of public sector performance measurement has reached a new level of refinement in New York with the publication by the Fund for the City of New York of an independent study of the quality of streets and roads, serving as a check on the performance measures reports in the MMR. New York Times. October 19, 1998, p.1.) 1.

[15] The *New York Times* reported in 1998 (October 19, p. 1) that the Fund for the City of New York had published an independent study of the quality of streets and roads, serving as a check on the performance measures reports in the MMR. While in a sense this publication marked a new stage of refinement of MMPRS in New York, significantly the report was issued by a private, not a government agency, underscoring how the government itself had fallen short of its own efforts to pursue MMPRS goals.

[16] GAO, "Managing for Results: Opportunities for Continued Improvements in Agencies Performance Plans," July, 1999.

organizational culture that stresses achieving the results the agencies had committed themselves to producing.[17] In another sign that performance management had not fully taken hold in Washington, when policy analyst Donald Kettl, a leading student of GPRA, testified to Congress about the value of performance measurement in reducing the "performance deficit" and about the importance of Congress using the measures that were produced, there was no discussion of Congress insisting that federal agencies use their measures in managing.[18]

COMPSTAT

In contrast to disappointing efforts to use GPRA or MMPRS to promote reform, another New York experiment – the management revolution at the NYPD (New York City Police Department) known as COMPSTAT and its partial spread to other city agencies -- has been much more fruitful. The reform began at the start of the Giuliani mayoral administration, when the NYPD's leadership, under enormous political pressure to reduce crime and increase public safety, decided to convert its well established system of *measuring* performance into the new COMPSTAT system of performance management. Previously, the NYPD, like all New York City agencies, had not primarily or consistently focused on outcomes. Instead, its attention had been devoted to other dimensions of performance such as numbers of officers on patrol (an activity) or police response time to calls for service (an output). Furthermore, tabulations of these measures were mainly distributed first to top officials, and only then more broadly, after a significant lag time.

COMPSTAT radically transformed the way the NYPD handled performance information. Big changes were made in what information was given to whom and when, and in how

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17 GAO, "Managing for Results: Federal Managers' Views Vary Widely on Key Management Issues," May, 2001.

18 Testimony delivered in 1996. Kettl comes closest to addressing this issue when he recommends that performance measures be related to strategic plans required of agencies, but in describing the elements of strategic plans, he does not refer to the need to explicate the logic or theory of programs and thus the need for the strategic plans to track progress along causal chains. According to Kettl, "Good strategic plans have six steps: Define the mission... Frame the goals... Set the objectives.... Assign responsibility for achieving objectives...Specify output/outcome measures.... Compare results with goals." The steps of strategic planning are clearly articulated, but what is missing is the expectation that each step is logically related to the next.

individual precincts were held accountable for what the performance data revealed. Under COMPSTAT, precinct commanders received timely data on crime and quality of life complaints (outcomes). -The Department began engaging in detailed and systematic tracking of its response to those complaints. The aim was to accelerate both the learning process and dissemination of lessons about what did and did not work. Another important ingredient of COMPSTAT was that commanders were periodically called to account for the level of success their precincts achieved.

Finally, undergirding these reforms were dramatic changes in the technology for managing and collecting information. As recounted in Smith with Bratton (2001) and elsewhere **[cite others]**, in 1994 at the start of the Giuliani administration, the NYPD had an enormous and highly developed, computerized data base of performance indicators, and a sophisticated analytic staff, but the computerized system was entirely mainframe, and administratively centralized at One Police Plaza. There was no information network nor were there any personal computers in the city's precincts, which were responsible for a huge proportion of the Department's work. Changing that fundamental structure to a networked, decentralized system was a first order of business in creating COMPSTAT.

As shown in a formal model of COMPSTAT elaborated by Smith and Bratton and as stressed in the NYPD's own exposition of how COMPSTAT works, four principles are key to the system's success: (1) accurate and timely intelligence, (2) effective tactics, (3) rapid deployment of personnel and resources, and (4) relentless follow-up and assessment.[19] As the Smith and Bratton model also shows, there are also a number of other necessary elements associated with COMPSTAT that usually are given less attention. They include: sharing intelligence, having the capacity to analyze timely intelligence at different operational levels, devolving discretion to act on timely intelligence, developing experience-tested strategies for achieving results, and holding

[19] Howard Safir,, The COMPSTAT Process, prepared by the Office of Management Analysis and Planning, the Police Department of the City of New York, n.d.

people accountable for acting effectively. All of these strategies can be seen as parts of causal or logic models of interventions that can be used to track performance. In other words, they can be arranged into a set of implicit "if-then" assumptions: If intelligence is shared, it leads to devolving discretion to act on timely intelligence, and if that discretion is devolved, it leads to developing experience-tested strategies for acting effectively, and so on, with the last element in the causal chain being "improved performance." This causal thinking is a key to successful performance management.

The dramatic reduction in crime associated with the NYPD's use of COMPSTAT was an inspiration to Commissioners in other city agencies, notably Corrections Commissioner Michael Jacobson, who oversaw the development of a management reform called TEAMS, and City Parks Commissioner Henry Stern, who used PARKSTAT, a version of COMPSTAT, with impressive performance improvement results similar to the ones effected by COMPSTAT. [20] By the end of the Giuliani administration there was talk and some effort to apply the COMPSTAT lessons still more broadly to the management of additional city agencies. This approach, called CAPSTAT, became explicit policy at the outset of the Bloomberg Administration. As a result, for the first time since MMR had been created in the late 1970s, the City effected a significant reform in its MMR practices, centering on a commitment to concentrate on measurement and management of results

Part of the reform was to require all agencies to shift the focus of their measurement away from inputs and activities and toward outcomes. Furthermore, under CAPSTAT and related changes in the MMR, performance reporting became much more visible and transparent. In addition to the twice yearly publication of the MMR, the city began to offer regularly updated reports on agency performance on its NYC.gov website. Thus, it is now possible for ordinary New Yorkers to go online and view reports of the performance of city agencies, including police precincts and schools, in their neighborhoods. Moreover, an effort is made to design this information in ways that make it easy for users to understand.

As the city agencies have felt the pressure to measure success in producing desired outcomes, there have been ripple effects for the nonprofit groups that are given contracts with these agencies. For example, if the city agencies funded to move poor citizens from welfare to work can no longer report only how many people they counseled or trained, but instead must track how many of those people found jobs and held them, then it is not enough for the subcontractor agency to report on completion rates for training programs. Similarly, if the child welfare agency must report not just the number of children it serves, but also how many are safely returned to their parents or move from foster care to permanent placements, the agency's contracts with nonprofit agencies cannot pay solely on the basis of numbers served or services provided. As a result, many city agencies have been moving toward performance-based contracts (PBCs) that focus on outcomes. We now turn to a discussion of the promise and pitfalls of this important shift in practice.

Performance-Based Contracting in New York City

People who think of bureaucracies as adhering to set rules might be very surprised to find out how often there is no one standardized procedure that New York City government agencies must follow. One area of procedure that shows this lack of uniformity is the rules for how to contract services. Vendors must meet certain requirements of the New York City Charter, such as registering with the New York City Comptroller's Office. But beyond those basic rules, practices vary widely.

In a report on contracting, "No Small Change: Opportunities for Streamlining Procurement in New York City," the Citizens Budget Commission pinpoints one important aspect of this lack of uniformity. The report, which describes the role of the city's Chief Procurement Officer who heads the Mayor's Office of Contracts (MOC) as the manager of the city's procurement process, criticizes MOC:

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[20] Smith, 1997; Smith with Bratton 2001.

Since … [MOC's] … formation it has not acted as a comprehensive manager of procurement. Instead, MOC has taken on a narrower role as gatekeeper of large contracts and those that are let through special case methods. MOC's role as the Mayor's oversight agent rather than a service, support and planning unit for city-wide purchasing has resulted in no agency with the authority or mission to be a comprehensive manager of procurement.[21]

Consistent with this observation, when the City responded to pressure to add information about contracting performance in the FY 2000 Mayor's Management Report, the information that agencies provided was not based on standardized measures. A review of one table in the report highlights the problem. The table lists the number and total dollar value of new contracts entered into during FY 2000 by 35 agencies. It also presents the percentage of each agency's contracts that the agency considered "performance-based" and similarly, the percentage of total dollars spent on contracts that the agency defined as spent on PBCs.[22] For both categories, percentages that were reported ranged from 0 to 100 percent, with considerable variation in between. But further scrutiny of the table suggests a still more troubling variation – in agencies' different conceptions of a performance-based contract.

- Some agencies counted any contract as "performance-based" if it specified expected activities and outputs as the way of fulfilling performance obligations, without spelling out any financial or other direct consequences of success or failure to perform.
- Others also took the approach of considering activities or outputs sufficient to meet performance goals, but called contracts "performance-based" only when there was some contingency of payment, including bonuses or penalties, related to performance at specified levels.

[21] Citizens Budget Commission, "No Small Change: Opportunities for Streamlining Procurement in New York City," 2002. The Mayor's Office of Contracts is under new leadership and has recently shown signs of taking a leadership role in systematizing performance-based contracting. See Citizens Budget Commission. New York City Procurement: A Blueprint for Change," October 21, 2003.
[22] The more recent Mayor's Management Reports do not include these PBC indicators, a fact criticized in a New York City Comptroller's study, "How are we doing? Enhancing accountability through the Mayor's Management Report, February, 2002." Without acknowledging-the problems with the indicators that had been used, it recommends their reinstatement.

- Some used a more restrictive definition: All or a significant amount of the payment depended on achieving agreed upon *outcomes* and/or *milestones* that were closely linked to those outcomes.

Thus, this closer inspection of the MMR table indicates that lacking standard definitions, MMR told its readers virtually nothing about the overall state of performance-based contracting in New York.

To help produce a clearer picture of how agencies are approaching performance-based contracting, a team of graduate students from the New York University's Robert F. Wagner School of Public Service[23] surveyed 10 New York City human service agencies about their practices in this area. [24] Conducted in the spring and summer of 2003, the survey questions asked agencies to distinguish between:

- an exhortation to perform,
- measures of performance, and
- payment systems based on reported performance.

Similarly, the survey helped agencies to define performance as either:

- *activities* designed to further objectives consistent with an agency's mission;
- *outputs* that resulted from those activities but that were still short of actually changing the condition of the client served, and
- *outcomes* - defined as a measurable intended change in the condition or life of the client.

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[23] Shawn A. Campbell, Carol (Ka Lam) Hui, and Claire Walden.

[24] The students were participating in the Wagner/Seedco Public Sector Performance Management and Improvement Project, in partnership with the Office of the Deputy Mayor for Operations? and the Mayor's Office of Contracts.

Instead of asking, for example, "Is payment linked to performance?" the survey asked, "What percentage of payment is based on outcomes, on outputs, and on activities?"

Like the MMR responses, answers to this part of the survey show wide variation in the extent to which agencies use different practices, but this time, even though there are almost certainly discrepancies between what agencies say and actually do, the picture of their practices in the area of performance-based contracting is considerably sharper. The results showed that some agencies were making consistent use of PBCs tied to outcomes. Notably, the Administration for Children Services - which, as will be discussed shortly, has transformed itself, on paper, at least - into something of a model of performance management practices -- reported that 100 percent of its payments for foster care services were based on outcomes (although, as will also be discussed later in the paper, the agency actually appears to rely, probably for good reason, on a mixture of process and outcome indicators in determining its payments). Other agencies responded that only between 10 and 20 percent of their payments hinged on outcomes, and still others said that 2 and 3 percent of the payments - in the form of bonuses and incentives - were outcome-based. Despite the Bloomberg administration's shift toward measuring outcomes in PBCs, one agency said its payments were 100 percent based on activities (in effect, totally line item).

Finally, one of the largest city agencies responded that almost all of its contracts were a combination of line item and outcomes, outputs or activities. However, the agency could not provide even an estimate of the percentage of each element of performance considered in its payment process. It also reported that its contracts tend to shift from line item budgeting for the start-up year to payment for the achievement of milestones later in the contract. In all, these survey results suggest that efforts to pinpoint and standardize what is meant by "performance" in a PBC are in their infancy in New York City.[25] Given the gap between reported and actual practice in using the short-lived PBC measures in the MMR, the survey results, while helpful, should be read with some caution. It is probably wise to await more detailed examination of PBC implementation to draw firm conclusions about how agencies actually use indicators to determine compliance with PBCs.

The survey also queried the agencies about their efforts to take the concerns of their vendors into account in designing the measures to be used in PBCs. Most agencies reported that they do take note of vendor perspectives as they construct measures and milestones.[26] But their willingness to do so does not mean that that performance-based contracting is without significant sources of vendor-contractor tensions. Fundamentally, the tension stems from the financial risks that vendors face when they enter into these contracts. Some service providers have ignored those risks; others, to their credit, are more realistic, factoring the risks into their decisions about whether to accept the contracts, and in some cases -- particularly in today's difficult economic climate -- simply concluding that the stakes are too high. As a result, some city agencies have had the experience of receiving *no* agency proposals when they issue RFPs for PBCs.

In an illustration of this same trend in a location very different from New York City, a recent study of the impact of performance-based contracting on nonprofit organizations in Kansas reports that, "Ultimately there will be too few nonprofits to maintain sufficient competition to control costs. Between the first and second rounds of bidding the total number of proposals received for adoption and foster care services dropped from 18 to 10. Those ten proposals came from six agencies, one of which, Lutheran Social Services, is no longer in existence."[27]

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[25] One sign that the City is now concerned with how to nurture and develop this "infant" is that it has engaged with the NYU/Wagner School and Seedco's Performance Management and Performance Improvement Project.

[26] Vendors, it must be noted, have long had a plethora of complaints about the way New York City does its contracting business, quite apart from issues raised by performance-based contracts. These complaints, about problems such as delays in payments and cumbersome reporting requirements, predate and are compounded with new difficulties introduced by performance-based contracting.

[27] In Kansas, "[w]ithin five years, one prominent faith-based foster care contractor (United Methodist Youthville) had exhausted an $18 million endowment and declared bankruptcy and the adoption contractor (Lutheran Social Services of Kansas and Oklahoma) had gone completely out of business." Nancy McCarthy

When service providers do accept contracts, one very important source of tension is the distribution—and timing -- of payments across activities, outputs, and outcomes: How much of the total reimbursement for contracted work will be made for what dimension of performance and when?

The survey, which also asked city agencies about "the management problems that human service vendors face when implementing performance-based contracts with your agency," sheds further light on problematic aspects of vendor/city agency relationships. In a result that might surprise some vendors, who claim that City agencies are unaware of the challenges they face in entering into PBCs, the agencies' list of perceived problems was quite long. City officials cited problems of inadequate training of staff, the newness and difficulty of measuring outcomes, underdevelopment of client and financial information management systems that service providers need to operate under performance-based contracts, cash flow crises and financial uncertainty, and multiple and even conflicting requirements of multiple contracts that vendor agencies commonly enter into. While the perspective of agencies on vendor problems is useful, the vendors' experience needs to be assessed directly. A survey of vendors is planned for spring, 2004.

Earlier this paper noted Steven Kelman's stress on the skills needed to successfully execute a governmental system heavily based on contracts. The results from the MMR and the survey that have just been reported suggest that despite the prominent and established place of contracting out in the city's human service delivery system, there is little evidence that priority has been placed on acquiring the capacity and competencies that Kelman thinks are prerequisites for smoothly functioning contracting systems, and especially systems that use PBCs.

Snyder and Marcia Allen. " Managing the Uneasy Partnership between Government and Nonprofits: Lessons from the Kansas Child Welfare Privatization Initiative," presented at the Association of Public Policy and

Notwithstanding the progress that has yet to be made, the survey did point to one positive aspect of contracting in New York -- the degree to which the measurements government agencies use in their contracting process are aligned with the indicators of agency performance presented in the MMR. In response to a question about that alignment, most agencies said that the performance measures used in their contracts appeared in the section of the MMR devoted to their work. This result contrasts with a finding from an MMR study conducted a decade ago, which showed that for most agencies there was little or no connection between measures tracked in the MMR and those central to internal agency management. The 2003 survey results reflect the current Bloomberg Administration's effort to focus on outcomes — and to have City Hall and the government agencies on the same page when they articulate critical measures of performance.[28]

Management (APPAM) 25th Annual Research Conference, Washington, DC, November, 2003.

[28] This shift has been a notable component of the Mayor's Office of Operations' reform of the MMR, the most penetrating reform that has occurred in MMR's 25-year-long history.

The Conceptual Challenges Facing New York

Before we turn to the experiences of specific New York City public and private agencies, it may be useful to consider some of the very real dilemmas that come with the territory of performance-based contracting. To start, contracts involve the enumeration of specific deliverables, and government sometimes has difficulty deciding on its objectives or on what outcomes it really wants to achieve. Sometimes, politics is the problem. For example trying to provide a fair share of decent shelters becomes an extremely difficult political issue, so government retreats into process as an alternative. In other words, rather than specifying the outcome of the number of shelter beds created in each designated community, the government limits itself discussing how many families flow through each individual shelter.

Sometimes there are real substantive or policy disagreements – for instance, in the child welfare system, between keeping families together and the safety of children when there are drugs in the home. And sometimes there are different standards for different folks – for example, one for middle-class drug users who pop pills or abuse alcohol and another for low-income crack/cocaine or heroin addicts. Finally, even when government reaches consensus on an outcome – for example, putting welfare recipients to work -- there is not necessarily agreement about how to get there. Do some people need more training and education, or should everybody be required to get a job, no matter how poor its quality and its potential for helping the worker achieve economic self-sufficiency? Should there be differential rewards for nonprofits that serve people with different levels of work-related disabilities or different levels of needs -- for example, recovering substance abusing ex-offenders vs. laid-off skilled mechanics)?

In all, government usually has difficulty reaching decisions about outcomes, and this lack of clarity muddles the contracting process. But in the face of these difficulties, many PBCs do set reasonable performance goals. Typically, these goals are a mixture of process and outcomes. A good example would be a Department of Employment (DOE) contract that sets goals for the number of people the contractor enrolls, the number who get through the treatment (work readiness training, skills training, or remediation), the number who get jobs, and the number who retain employment for a certain length of time. Some would argue that under some circumstances, all four of these items can legitimately be considered outcomes. In fact, we argue that there is more analytical clarity when some are defined as activities (in this case, enrollment), other as the outputs those activities produced (people who get through the treatment), and still others as the outcomes that warranted the program in the first place (getting and keeping jobs). But regardless of the nomenclature, it seems like a good idea for DOE to specify all these performance indicators, because all are important in assessing the work of the nonprofits. Giving more weight in rewarding performance to outcomes than activities, while clearly not always the practice, also makes sense.

The contracts of the Human Resources Administration (HRA) tend toward tying payment to outcome performance (getting welfare recipients into jobs), but not when it comes to providing AIDS services where the outcomes are conceptually murkier. Most other New York City social service contracts (those issued by the Departments of Homeless Services – DHS -- and by Youth and Community Development, the Department for the Aging, and the Administration for Children's Services -- ACS) do try to establish performance outcomes but do not consistently tie them to payment. They traditionally have linked payment to an output like the act of caring for children in foster care, rather than achieving an outcome like reunification or adoption. This is entirely understandable. What is the outcome for a child in foster care? Adoption, reunification, creating a stable environment, staying in school, getting proper medical care, not going to jail? As will be shown in the discussion of ACS that follows, the agency's answer is in essence "all of the above." In short, outcome-driven social service contracts are usually complicated animals, and we really do not have the sophistication to tie payments to performance except in a very rudimentary way. Thus, to ensure that the perfect not be the enemy of the good, it may be best to settle for hybrid contracts – contracts that reward outcomes but that also give performance bonuses for certain line items, or process milestones.

Another dilemma is how to determine the government's obligation when contractors fall short of performance or outcome goals. Should government *punish* the nonprofits if they have made a legitimate effort (measured by activities and outputs), or should it provide technical assistance in an effort to improve performance? ACS does the latter -- at least at first -- DOE the former, and DHS does both. And how is superior contractor performance rewarded? A classic ACS and Medicaid strategy is to reduce the payment rate when contractors exceed targets. The theory is that the government must have established the wrong payment points in its outcome analysis. HRA, which places so much emphasis on the outcome of getting and retaining a job, places substantial restrictions on the level and uses of "profits" that are allowed for superior performance under its performance payment contracts. That nonprofits should be run more like businesses, is the rhetoric - but not be *too* business-like is the underlying assumption. Interestingly, there are no examples of government increasing payments if the contractor falls below expected outcomes because the outcomes themselves were unrealistic. This is the kind of contract design "adjustment" activity a New York City government office (the Mayor's Offices of Contracts or Operations, or the Office of Management and Budget) should look into, but thus far this has not happened.

Case Studies of Experiences with Performance-Based Contracting

The paper now turns to a series of case studies designed to flesh out the picture of agency practice presented by the survey. Case studies are especially useful for illuminating the experience of nonprofit agencies, since it has not yet been possible to field a survey to cover the experiences of the nonprofits contracting for human services. This is because the number of these agencies is -- while knowable -- not known at this time, but clearly variable and large. But even in the case of the more manageable and known number of government agencies responsible for human services, which the Wagner School was able to survey, additional light can be shed on New York's experiences with performance-based measurement, management, and contracting by taking a close-up look at how particular city agencies have navigated these complex practices. It should be noted that while the primary focus of these case studies is on performance-based contracting, they also touch on a number of agency experiences with the two practices that are intrinsically tied to this kind of contracting -- performance measurement and management.

Government Agencies

The Administration for Children's Services (ACS)

When the Administration of New York's previous Mayor Rudolph Giuliani was confronted with yet another tragic death of a child "known" to the city's child protective services department, the Mayor decided to move child welfare functions from the Human Resources Administration, which has many other human service responsibilities, to a new agency. In 1996 he created ACS, and appointed Nicholas Scopetta, a lawyer with an extensive background in criminal justice administration, to lead it.

The need for reforming child welfare services at that point was clear. ACS was operating under court oversight because of evidence that it could not perform many of its critical functions of protecting children adequately.[29] Pointing to the agency's problems, the authors, in a paper written on the fate of policy analysis in the mayoral administration of Giuliani's predecessor David Dinkins, had cited child welfare as an extreme example of city agencies attempting to manage a complex and critical service while, in effect, flying blind.[30] The City had attempted to implement a plausible, even laudable, but not fully tested reform called "family preservation" in a system serving tens of thousands of children and families, with no computerized case records.[31] Not only had there been a total lack of the targeting

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[29] Ross Sandler and David Schoenbrod. Democracy by Decree: What Happens When Courts Run Government. Yale University Press, 2003.

[30] See Grinker and Smith, "HRA Adrift: Social Spending Without Direction."

[31] Family preservation is a program that views very expensive short-term intensive services designed to avoid foster care placements in high-risk families as a good investment, given the much higher multiple costs of moving children to foster care, and then trying to move them back home or to adoption. The rub, of

and tracking required for such a policy to have a chance of success, but there had been little evidence of an appreciation of the analytical challenges involved in introducing targeting and tracking into the system.

In the reform of child welfare services, launched early in the Giuliani administration, ACS Commissioner Scopetta drew on the COMPSTAT changes, which he knew well. He called upon some of the same management consultants and used some of the same methods that William Bratton had introduced to the NYPD.[32]

Like the NYPD, the newly created ACS in effect started at the bottom of the performance management "evolutionary chain" – or to use terminology presented earlier in this paper, at the base of the hierarchy of complexity -- by developing a computerized record and tracking system. But what was notable about the ACS effort is that it embraced not only this threshold change but the other key dimensions of public sector performance reform. ACS measured outcomes and began a conversion of the agency's management and contracting system, leading to the use of a wide range of interrelated performance improvement strategies and tools.[33] The Commissioner's understanding of how the different dimensions of reform connect to one another is becoming more typical of City agency leaders interested in management improvements, and it stands in contrast to earlier styles of reform in New York, which were much more likely to focus on only measurement, or, at most, managing with the activity and output measures.[34]

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course, is that only 1 in 10 children who are at risk will actually have to be taken from their families, so that it is necessary to correctly predict which child out of every 10 will need family preservation services to avoid this outcome.

[32] Like Bratton, he also secured foundation funding to compensate the consultants and aid the process of reform.

[33] Protecting the Children of New York: A Plan of Action for the Administration for Children's Services, December 19, 1996.

[34] This discussion of ACS draws on a paper by Kaitlyn Falk and Hayley Wasko. "Performance Management at the NYC Administration for Children's Services: A survey of performance management practices in New York City's foster care system," 5/09/02. The paper was written for Policy Formation and Analysis in New York City, a course taught by Dennis Smith at the NYU/Wagner School.

Of course, while performance measurement and performance management *were* new elements of the ACS agenda, contracting was not. As suggested earlier, contracting for foster care, in particular, is one of the oldest public/private partnership traditions in New York, and it has remained a very important part of the city's child welfare practice. One study reports that in 2000 90% of the nearly 29,000 children in out of home placements in New York were in the care of [35]contract agencies. Thus, when ACS began to write PBCs, large numbers of child-serving agencies felt the ripple effects of this new approach to contracting. Today ACS gathers data from 52 contracted foster care agencies, analyzes their trends in performance, and takes action, either through (1) requiring corrective action for necessary improvements in services, (2) termination of contracts, when outcomes are unsatisfactory or (3) rewards. And in keeping with the trend among City agencies discussed earlier, often the performance outcomes ACS examines for the contracts with these human service providers are the same performance outcomes it reports in the MMR.

To get a fuller picture of what ACS performance-based contracting looks like, it may be helpful to examine some of the tools and systematic approaches the agency uses. The following table shows desired outcomes and measures of each outcome ACS seeks for itself and its contractors. In the left-hand columns, the first seven items show system performance / change[d] objectives, while the matched right-hand columns articulate the ultimate outcome the system would like to bring about in operational terms. The top five child welfare process indicators are key sets of activities undertaken by ACS to achieve its performance objectives, and again, each activity is linked to an outcome. In all, the outcomes in the table create a framework for shaping both the agency's own work and what it seeks in contracted services.

[35] Fred Wulczyn and Nancy Martin, Linking Permanence and Finance in Child Welfare: ACS Safe and Timely Adoptions and Reunifications (STAR) Program, Presented at The National Association of Welfare Research and Statistic. Baltimore, Maryland August 21, 2001.

Administration for Children Services Outcome Measures[36]

1. Increase Effective Preventive Interventions	A child who can be served safely at home should not come into care.
2. Faster Permanency (Reunification and Adoption)	A child should be reunified with a safe family as quickly as possible. [Children with a goal of reunification should be reunified within 15 months, and children with a goal of adoption should have their adoption finalized within 27 months]
3. Low Replacements	A child should not have to move while in care [except to meet the service needs of the child and/or sibling reunification]
4. Low Re-entry into Foster Care from Reunification and Adoption	A child who is reunified or adopted should not reenter care
5. Low Re-abuse of Children who come into Contact with the Child Welfare System	A child served by ACS protective, preventive, foster care and adoption services should not suffer new abuse form their caretakers, whether parents or foster parents
6. Reduce the Number of Children Aging Out of the System to IL	Every child leaving care should have a permanent family
7. Ensure Effective Delivery of IL Services	Every child aging out of care should have a high school diploma or GED, be enrolled in higher education or have a job, and have a place to live
Top 5 Child Welfare Process Indicators	**ACS Goal**
1. Community-based Services	Every child and family should receive services in their own community
2. Neighborhood-based Placements	Excluding a kin placement and safety exception, every child should be placed with his or her siblings in their own community and stay in the same school
3. Case Conferences	Case conferences should be held at all critical points and fully attended
4. Service Plan Reviews	All SPR's should be fully attended and timely documented in the UCR
5. Reimbursements	All state/federal reimbursements should be maximized

ACS is developing and perfecting two tools to help keep its focus on the outcomes that were just examined. The tools are the EQUIP (Evaluation and Quality Improvement Protocol) program and the STAR (Safe and Timely Adoption and Reunification) program.

[36] ACS Status Report III, 129.

EQUIP, first used in fall, 2000, systematically measures the performance of ACS contract *agencies.*. Use of EQUIP is designed both to ensure that the contracts are all driven by a set of common goals set forth in the ACS 1996 reform plan and to help ACS rate its own performance. Table 2 shows the scoring breakdown used for EQUIP.

Table 2.

ACS Evaluation and Quality Improvement Protocol Scoring System

Tool	Measure	Score	EQUIP Score
Process	Unified Case Record Completion	4.55	30.3%
	Timeliness of Foster Parent Training	4.03	
	Timeliness of Foster Home Recertifications	4.03	
	Adoption Finalizations	6.06	
	Frequency of OCI Indicated Cases	3.03	
	Quality and Timeliness of OCI CAPs	3.03	
	Validated Placement Complaints	5.57	
Outcomes & Indicators	Time to Reunifications	7.06	39.4%
	Time to Re-Entry	7.06	
	Time to Adoptions	7.06	
	Independent Living	7.06	
	Neighborhood Based Services	11.16	
Quality (PES)	Care Reading (50%)	Overall PES Score	30.3%
	Site Visit (30%)		
	Interview (20%)		

Each measure is weighted (column 3) in accordance with the goals of the system, signaling to stakeholders the overall priorities of ACS.

Outcomes indicators are given the most weight in the EQUIP score, but significantly the score also includes process indicators. By taking process measures into account, ACS acknowledges the complexity of the service delivery systems that produce the desired outcomes. In other words, as was argued earlier, a good system of performance-based contracting emphasizes outcomes, but not to the exclusion of the chain of inputs, activities, and outputs needed to produce them.

The data collected from contracted agencies and ACS are aggregated by ACS and evaluated on the grounds identified in Table 2. Each agency is then mailed its score and given a chance to appeal. Once the final scores have been resolved, ACS makes decisions based on the results: Low performing agencies are offered technical assistance, or on the occasion of extremely weak performance may have their contracts terminated. Agencies that perform at or above average are renewed and perhaps have had their contracts increased.

The other mechanism ACS is using to improve outcomes is the STAR program. STAR's purpose is to give foster boarding home programs an incentive to ensure that children under their care are either reunified with their families or adopted. The system tracks the time that children cared for by the contracted agencies spend in out-of-home placements, and agencies that reduce the number of days spent retain some of the revenues they would have received for the care. These revenues are flexible funding that the agencies can either reinvest in preventive or aftercare services or use to enhance their foster care services. The STAR data accumulated on length of stays in foster care gives the agencies a meaningful baseline picture of the current duration of time spent in out-of-home placements, against which progress in reducing those time periods can be measured.

The ACS reforms begun by Commissioner Scopetta have continued under Commissioner William Bell in the Bloomberg administration. While ACS is far from claiming total victory for its efforts, its reforms are generally regarded as a success story. A study of STAR by a researcher and an ACS manager who helped design it report "success for children and families as well as for the contract agencies. The data show that agencies used fewer foster care ddays for their care than was predicted by the STAR methodology… The result of this reduced utilization of foster care is a financial benefit of $8 million dollars, which is being redistributed for reinvestment in child welfare services to the agencies responsible for the performance improvement." [37] Reports of abuse and neglect of children declined in FY 2003, and substantiated claims of abuse and neglect have gone down for four consecutive years. Based on the agency's significantly improved capacity, ACS was also relieved of court-imposed oversight, which had been in place for years.

The Department of Homeless Services (DHS)

DHS is now led by Linda Gibbs, who previously served as Deputy Commissioner of ACS. At ACS, Gibbs played a key role in the management reform of child welfare services, and she has pursued a similar agenda for homeless services.

Like ACS, DHS is now heavily dependent on contract agencies to achieve its service goals. As noted in Table 1, 66 percent of the DHS budget is spent on contracts for services. Gibbs did not initiate either the agency's heavy reliance on external service providers or its use of PBCs. That foundation was laid by her predecessor, Commissioner Gordon Campbell, who during the Giuliani administration presided over the conversion of homeless services delivered in government-organized and staffed shelters into a system that relies heavily on the greater flexibility offered by nonprofit providers.

DHS's shift to contracting occurred simultaneously with the introduction of outcome measures of performance, a change that was supported by both DHS and its service vendors. The first steps of the reform process were efforts to create an incentive payment plan to reward high performing contract agencies with bonuses.[38]

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[37] Wulczyn and Martin, pp. 18-19.

[38] Former Commissioner Gordon Campbell and Elizabeth McCarthy tell the story of this transition in "Conveying Mission through Outcome Measurement: Services to the Homeless in New York City. "*Policy Studies Journal*, Volume 8, no. 2, 2000. Their account reflects the theme presented here that policy learning that occurs in the course of the performance-based contracting process can be used to accelerate the overall pace of reform at an agency.

Commissioner Gibbs built on Campbell's accomplishments. Since assuming the leadership of DHS, which now manages 15 City-run and 187 privately run shelter facilities, she has both expanded and upgraded the agency's analytic staff and has used outside consultants in order to help design and evaluate the move to performance-based contracting. The change is reflected, among other places, in the agency's new emphasis on outcomes in the MMR. According to the City Comptroller's Report, "How are we doing?", which was issued at the beginning of the Bloomberg Administration, DHS's section of the MMR contained no outcome measures. In contrast, in the 2003 Preliminary Mayor's Management Report (which, because it is now designed to focus on outcomes, presents far fewer indicators than in the past), least half of the 23 DHS indicators are measures of outcomes.

Earlier this paper traced the progress in New York City government's use and understanding of *performance management* techniques in the human services arena. These techniques essentially began with use of outcome measures by one agency (NYPD), were replicated at others (the Corrections and Parks Departments), and then evolved into a formalized citywide effort to define and measure outcomes (in CAPstat.) The experiences of DHS and ACS show that the learning curve for *performance-based contracting* for human services in New York has followed a similar trajectory.

Having examined experiences of some government agencies, the paper now turns to the other important set of parties to PBCs – the providers.

Nonprofit Provider Agencies [39]

Case Study 1: CASES

Established in 1989, CASES provides people adjudicated in the court system with alternatives to incarceration. The organization, which has a staff of 180 and an annual budget of $12 million,[40] first started shifting some of its program contracts from line item to performance-based contracting in the early 1990s.

Among nonprofit agencies CASES has had a relatively smooth transition to performance-based contracting, with its success due to a number of different factors. First, the organization's CEO, Joel Copperman, was formerly an official in the Mayor's Office of Contracts. Second, CASES has developed a long-term and stable partnership with City agencies, which has established the organization's reputation as a trustworthy vendor of services.

Third, unlike many nonprofit organizations, CASES has a rich data base of performance information and the capacity to use its data to analyze trends. This has been important in enabling the organization to meet contract demands for proof of performance - and particularly in allowing it to adapt to external factors that could obstruct its capacity to deliver on the outcomes specified in its contracts. For instance, when crime began to go down in New York City, CASES was able to spot the trend of a drop in the number of offenders entering the criminal courts. Responding to that shift, CASES adjusted its staffing and other factors to reflect the lower number of criminal offenders who would be eligible for

[39] The following discussions of CASES and Seedco draw upon a paper written by a team of NYU/Wagner graduate students participating in the Wagner /Seedco Performance Improvement Project: Debora Brakarz, Henry P. Briffel, Shawn A. Campbell, Belinda French, Carol (Ka Lam) Hui, Erez Lenchner, Daniel E. Parnetti, and Claire Walden.

[40] CASES website. <www.cases.org>

its services, thus avoiding the mistake of entering into contracts that promised a level of outcomes it could not produce.

Still another factor contributing to the organization's success with performance-based contracting is its large size and the organizational capacity that scale can facilitate. With a relatively large budget and experienced personnel, CASES has been able to minimize the fiscal problems and lack of expertise that make the shift to performance-based contracting difficult for many small community-based organizations.

CASES has found that the emphasis on outcomes in PBCs promotes efficiency. While line item contracts dictate an organization's expenses, often wasting resources to meet activity quotas, performance-based contracting, according to Cooperman, has allowed CASES to have more control and flexibility over its budget and operations. The organization is able to determine how and how many resources should be invested to produce desirable outcomes. Moreover, being able to break down program cycles into shorter intervals (monthly, for instance) also strengthens CASES' cash flow position. Invoices for payment based on a performance can be submitted monthly rather than quarterly.

In a sign that performance-based contracting also offers staff incentives to improve the way they work; different divisions of CASES have become more responsive to one another as they pursue common goals specified in the contracts. For example, the CASES finance and program management divisions now hold frequent joint meetings to track outcomes and discuss issues related to performance.

The CASES experience suggests that when government agencies and service providers use performance-based contracting as a vehicle for collaborating on program goals, both parties benefit. In comparison to line item contracts, PBCs give government more control over outcomes, which can be specified and tracked. Vendors benefit in several different ways. On the most self-interested level, organizations like CASES that develop expertise in managing these kinds of contracts have a competitive advantage over less savvy nonprofits. Fortunately for society at large, when these contracts are well executed, they not only offer financial benefits to nonprofit service providers, they also help the providers build their organizational capacity. The contracts' emphasis on outcomes conveys respect for the nonprofit's expertise in service provision, potentially building the internal morale of the organization and giving it latitude to determine how best to operate efficiently. PBCs also encourage nonprofits to take ownership of the outcomes they produce, meaning that not only the government agency that contracts for the service but the vendor who agrees to provide it is more likely to be invested in the results.[41]

Case Study 2: Seedco

When a community-based organization (CBO) does not have enough capacity and capital to compete for and operate under PBCs, its chances of success can be significantly improved by participating in a collaborative network. This approach is the one used by the *EarnFair*® Alliance, a partnership consisting of Seedco, a national nonprofit intermediary organization, and 11 CBOs that offer workforce development services to people in disadvantaged neighborhoods throughout New York City.

Seedco's mission is to provide financial and technical assistance and management support for the community-building efforts of nonprofit organizations and small businesses. Like CASES, Seedco is led by former senior City government officials with extensive human service management experience. [42]

Working through its subsidiary organization, the Non-Profit Assistance Corporation (N-PAC), Seedco established the *EarnFair* Alliance in 1998. Seedco/N-PAC has negotiated a 100

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[41] Some agencies demand a line item budget even though they are paying on performance, because they fear that they to do otherwise would expose them to severe legislative or oversight agency criticism. This demand sends contradictory signals to the vendors and increases the already heavy reporting burdens imposed on them.

[42] Interview with Laura Seidell, Seedco, December 4, 2002.

percent PBC for workforce development services with HRA, with the CBOs that participate in the Alliance subcontracting with Seedco/N-PAC to deliver the services. Seedco believes that these nonprofits, with their deep knowledge of their communities, are best suited to helping low-income people find and keep jobs. What Seedco/N-PAC offers the nonprofits is a wide variety of supports to enable them to deliver their services in a PBC world.

One important kind of support offered through the *EarnFair* Alliance is some financial protection against the considerable risks of the PBC. The subcontracts Seedco/N-PAC negotiated with the CBOs are 50/50 hybrid contracts. This arrangement enables the CBOs to get a portion of contract proceeds upfront, assisting them with start-up costs and enabling them to solve cash flow problems that could otherwise make it impossible for them to enter into the contracts. As an intermediary organization with a diversified funding base, Seedco has the financial capacity to cushion these costs for the CBOs.

To receive the balance of the payments, the Alliance CBOs must comply with the terms of the HRA contract, which specify that they reach and document milestone targets. These requirements confront the CBOs with significant challenges. They must become proficient at a range of administrative and technical tasks, which include identifying the target numbers to be used as milestones, maintaining and analyzing data, and documenting outcomes.

Seedco/N-PAC offers the CBOs extensive technical assistance and opportunities for peer exchanges to help them meet these challenges. Some of the help is individualized, some is offered through workshops. For example, one recent training session, which focused on case management, helped CBO staff members understand more about such topics as job development coordination, what kind of information is needed for adequate case documentation, and how to conduct assessments and exit interviews – all skills that CBOs need for the documentation of milestones that trigger PBC payments.

The Alliance also has developed some special tools to facilitate the PBC process. For instance, the CBO Alliance members can use Seedco/N-PAC's *EarnFair* Link, a web-based billing and management information system, which allows them to bill efficiently and to conduct timely analyses of their own performance in reaching contract goals. *EarnFair* Link also helps the CBOs develop the documentation they need to demonstrate job placement performance, thus connecting operational requirements to outcomes. Seedco/N-PAC offers staff of the EarnFair CBOs training on all aspects of the system.

SmartStat, another automated, web-based tool created by Seedco/N-PAC, assists CBOs with the analysis side of performance-based contracting. Drawing on data generated from *EarnFair* Link, the CBOs have used SmartStat to create action plans, identify indicators corresponding to outcomes, and create realistic data collection strategies.[43]

Training on the use of SmartStat brings Alliance CBOs together in workshops where they share approaches to problem solving and discuss best practices. In all of this work with CBOs, Seedco illustrates the value added when an intermediary organization serves as a bridge between neighborhood-based CBOs and large city agencies.

In addition to providing direct support to the CBOs, the Alliance has also developed a series of strategies designed to improve the chances that the individual workforce development programs operated by the CBOs will reach their long-term goals of good job retention rates and economic stability for the families they serve. For example, Seedco/ N-PAC has established a limited liability company, the *EarnFair* LLC, that helps the CBOs place clients in jobs. The LLC offers employers a chance to hire workers who have been recruited, screened, and trained by the Alliance, and, who, as will be discussed next, receive a wide variety of supports through the initiative. The LLC also subsidizes wages of the workers whom it refers to businesses during a transitional period of employment. All of these

[43] EarnFair Alliance Quarterly Update, July-September 2002.

services offer employers significant cost reductions, encouraging them to take a chance on the disadvantaged and often inexperienced jobseekers served by the Alliance CBOs.

The diverse benefits and supports offered to the workers placed in jobs with the help of Alliance member CBOs are designed to help them stay in the labor market. Once these workers are placed, many of them can take advantage of a variety of Seedco/N-PAC services such as Individual Development Accounts with matched contributions, free checking accounts, a financial literacy service, a shuttle service to facilitate travel to and from work, back-up child care, and assistance in getting access to a range of public benefits such as subsidized child care and the Earned Income Tax Credit. The Alliance's Family Loan Program makes low-interest emergency loans to families involved in the initiative. N-PAC provides a benefits guide that offers full information on governmental and *EarnFair* programs available to participant workers.

Like CASES, Seedco/N-PAC seems particularly proficient in establishing the contacts with governments – and crucially in Seedco's case, with foundations -- that facilitate the PBC process. Besides negotiating the HRA contract on behalf of the CBOs, Seedco/N-PAC has had good success in securing resources from funders to support various parts of the Alliance package. For instance, United Way of New York City provided a $400,000 grant that helps provide capital to EarnFair CBOs to enable them to take on PBC risks, the Tiger Foundation made a grant to support the EarnLink System, and Citibank waives bank account fees for EarnFair workers. Without these contacts, and without Seedco/N-PAC's expertise and in-depth attention to the needs of the Alliance members, these small CBOs would be far less likely to be able to meet PBC demands.

Case Study 3: The Osborne Association

The mission of The Osborne Association is to serve people in prison and their families, and to facilitate their re-entry into the community after their release.[44] Over the years, Osborne has adapted its services to accommodate the changing needs of its clients, taking advantage of new funding sources as they became more available. For example, with the onset of the crack/cocaine and HIV AIDS epidemics, services to address these problems were added to the Osborne menu.

But until recently, the agency did not provide employment services directly to its clients. In part because of the specialized nature of these services and in part because of the special needs of the Osborne clientele, when clients seemed ready to move on to employment, the agency would refer them to organizations with expertise in employment services. However, with the policy changes associated with the Clinton welfare reforms, which made the provision of many support services contingent on a person's work effort, a program strategy that focused exclusively on helping the Osborne clientele get access to social services became less viable. At the same time, as a result of the pressures to move the indigent population from welfare to work, funding targeted to difficult- to-place workers became more widely available.

In response to these new trends, Osborne began to consider the idea of merging with the South Forty Corporation, a nonprofit organization serving the same population group in the Bronx that Osborne served elsewhere in New York City. Osborne was larger and had more fully developed management systems than South Ferry, but South Forty had expertise in job placement services and a track record in this area. In late 1999, after about two years of board negotiations and due diligence reviews by lawyers and accountants, the two

[44] The information in this case comes from an interview with the long-time Executive Director of Osborne Association, Elizabeth Gaines, and from an audit report: A Report of the Office of the New York State Comptroller, "New York State Department of Correctional Services and New York City Human Resources, Administration, Administration of Osborne Association Contract Billings for Job Placement Services 2001-R-7." (January 23, 2003).

organizations merged. The former executive director of South Forty became one of the organization's two vice-presidents, and was effectively the person responsible for managing the workforce development services. Arguably, the merger was a textbook case of a nonprofit acting like a business, with Osborne acquiring the capacity it lacked and reducing the competition by acquiring another organization that offered the prospect of productive synergy.

Within six months of the merger, Osborne discovered a worm in the apple. A disgruntled former South Forty employee alleged in a letter to the State Comptroller that South Forty had provided fraudulent performance reports to its State and City contractors. Inspectors General representing the relevant City agencies and the State and City Comptroller all began investigations and audits.[45] Because of its merger with South Forty, Osborne found that its payments for contracted services already provided were frozen, and that its contracts with the New York City Department of Corrections were cancelled after work had begun but before the contract had been registered by the City Comptroller.

South Forty's problem predated its merger with Osborne. The agency had separate City and State streams of funding for its employment services, with the City contract providing approximately 20 times the payment per milestone achieved than was offered by the State contract.

Under the line item budgets of the contracts South Forty had been accustomed to entering into with City agencies, when similar services were provided to the same clients through different funding streams, the resources were blended together. When South Forty began to have job development /employment service contracts that made payment contingent on achievement of performance milestones, the nonprofit and its contracting agencies failed to clarify how the contribution of different funds to the milestone would be counted and reported. In part because South Forty managers were accustomed to blending funds**,** they assumed that the government agencies would not require separate tracking of the distinct services provided through and the milestones attributable to the separate funding streams. In the eyes of South Forty officials, the city funding was "supplementary" support to the state funds to help achieve program outcomes. Thus, the agency reported the same outcomes to city and state funders.

At the outset the investigators and auditors viewed this practice as fraudulent behavior; by the end of the process it was deemed unacceptable but more a case of mismanagement than fraud. Among the Comptroller's highlighted findings was the observation that South Forty's information system was not equipped to track the multiply funded services, and neither the state nor city contracting agencies had systems in place to detect multiple billing for the same ex-offenders.

Nevertheless, there was a problem, and by the time a whistle was blown, it had become Osborne's as well as South Forty's. When the merged Osborne Society presented its response to the government's report of the systemic weakness, none of the government funders expressed a willingness to change their financial tracking practices. Instead, each claimed it was some other agency's responsibility. The uncoordinated actions of multiple agencies contracting for the same or related services, or serving the same clients, is a recurring story in human services contracting, but it is a story that is only made more complicated in the riskier world of performance-based contracting. When reimbursement for work already done, rather than non-renewal or selection for future contracts, is at stake, mixed and conflicting signals carry far more risk to the service provider.

After about three years of disruption of contractual relations between Osborne and its long-time government partners (and thus disruption of services to a needy population) and after the investment of enormous amounts of time and energy on the part of the board and staff of the organization and the investigative agencies, and finally, after the expenditure of hundreds

[45] Ultimately the State Comptroller took the lead in the investigation.

of thousands of dollars in legal fees, Osborne is emerging from under the cloud that unexpectedly descended on it. Both Osborne and the government paid a high price for the failure of both public and nonprofit partners to make sure they understood the challenges of performance-based contracting before launching the new practice.

Conclusion

Needy citizens are dependent of a host of nonprofit organizations for vital services, and in New York City and increasingly around the country, government depends on outside contractors and especially nonprofits agencies to deliver those services. Improving the performance of this combined public/nonprofit service delivery system is clearly a laudable goal and probably an essential one, given recurring fiscal stress. The performance improvement hierarchy introduced in this paper shows that performance-based contracting is near the top of the list of strategies that have potential to make a difference

The last decade in New York City has produced some remarkable examples of public sector performance improvement. The CASES and Seedco/N-PAC case studies set forth in this paper are exciting examples of creative and systematic problem solving on the part of both government and nonprofit officials that aims to improve performance-based contracting. Collaborations between researchers and practitioners to capture and disseminate the lessons learned from these and other performance-based contracting experiences are vitally important to sustaining the momentum of reform.

One lesson that has been learned so far concerns the sequencing of performance-based contracting and other changes. The hierarchy graphic set forth in Figure 1 shows that this kind of contracting is more complex than either performance measurement or management, suggesting that mastering the practice depends on first having a handle on these more basic practices. If government agencies or nonprofit service providers attempt to jump levels without developing the necessary foundation, they are risking policy and organizational failure. Since as illustrated by the Osborne case study, performance-based budgeting ultimately depends on a performance management system operating with valid and reliable performance measures, faulty measures can also lead to financial ruin. (The Kansas example of Lutheran Services comes to mind.)

Another suggested lesson from this paper's case studies is that nonprofit leaders who also have worked in human service administration in government have an advantage in successfully navigating the complex boundaries between government procurement practices and the needs of nonprofit service providers. Along these lines, it is important to recognize that performance-based contracting places CBOs, with their relatively small pockets and often fragile staffing and managerial structures, at a distinct disadvantage. Unless both government agencies and smaller nonprofits find ways to work with intermediaries like Seedco, these nonprofits may get squeezed out of the PBC world. The result will be that the rich field of nonprofit service organizations will be drained of much of its diversity and client services will suffer at a considerable cost to both the individuals involved and society as a whole.

ADDENDUM

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