Ms Tess Bishop
Head, Care and Support Economy Taskforce
Department of the Prime Minister and Cabinet
PO Box 6500
Canberra ACT 2600

26 June 2023

Dear Ms Bishop,

Thankyou for the opportunity to provide a submission in response to the draft National Strategy for the Care and Support Economy.

Social Ventures Australia (SVA) is pleased to see government engaging in this important work, acknowledging the vital role the care and support sector plays in Australia's economy and society. As the draft Strategy notes, funding high-quality care and support provision is an investment in social infrastructure with long-term benefits.

We endorse the three goals outlined in the draft Strategy, but are concerned that the strategy does not consider a dimension that will be critical to achieving them – the incentives and constraints that the sector faces, particularly the challenges faced by not-for-profit (NFP) employers in the sector that arise from the way they are funded and regulated by government. Our aim in this submission is to share our insights on this issue and recommend a path forward to strengthen the Strategy by including them.

NFPs are significant players in the care and support sector and deliver services across the four areas identified by the Taskforce as being the focus of this strategy – early childhood education and care, disability support, veterans' care and aged care. In each of these areas they operate in 'mixed markets' with for-profit, and in some cases government-run organisations. In many cases, NFP providers take on the 'hard cases' which are not profitable for for-profit service providers, because they believe in the mission and purpose of their work. NFPs also generate additional value for government because they enable it to leverage philanthropic funds and facilitate relationships that foster community connectedness and resilience, as well as maintaining a focus on quality rather than profit. For example, analysis of the ECEC sector indicates that not-for-profit providers are more likely than for-profits to meet and exceed National Quality Standards, to be located in disadvantaged communities, and to have lower hourly average fees and pay above award wages.[1] The Australian community would be worse off without the presence of NFP service providers in the care and support economy.

SVA agrees with much of the analysis in the draft Strategy about the challenges facing the sector's workforce, including the problem of ensuring the sector provides decent jobs that enable quality care. However, the Strategy does not fully address the underlying causes of these challenges. SVA believes that the nature and structure of government funding for NFP service providers makes it difficult or

[1] See Social Ventures Australia (SVA), *Submission to the Productivity Commission inquiry into early childhood education and care*, SVA, 2023, p7, accessed June 2023

impossible for achieve the goals and objectives included in the draft Strategy – even though the majority of the sector would likely agree with their aims.

This arises because NFPs have fundamentally different structures to either private businesses or government entities, and have far less flexibility in their financial strategies. There are three dynamics that are particularly relevant here:

1. **Inappropriate funding structures:** Many government contracts contain features that work against the goals outlined in the draft Strategy. For example, short term funding agreements, renewed via competitive tendering processes, create significant uncertainty for NFPs that make it difficult for them to invest in their own long-term success. To take an obvious example – a NFP organisation delivering government-funded services on a two-year funding contract cannot realistically employ service delivery staff on an ongoing basis. If the contract is not renewed, the NFP will not have the funds to pay these staff, and has limited options to access funds elsewhere. Other problematic features include restrictions on what funds can be spent on, which can prevent investment in innovation, training and leadership development even if it would improve job quality and care quality; and inadequate indexation provisions to reflect inflation and other external cost pressures.
2. **Challenges raising capital**: NFPs have particular challenges in raising capital.[2] Unlike businesses, NFPs can't raise equity from shareholders. Most aren't in a position to take on debt to help them smooth their income, adapt their business model or invest in rebuilding. Although on paper some large charities appear to have a large asset base, many of their assets are necessary for them to pursue their purpose, such as a hospital for a health charity, or a campus for an educational institution, and cannot be used as a source of funds. Moreover, charities cannot easily take out loans against these assets, because their constrained and inflexible revenue streams can be unattractive propositions for lenders. Charity boards may also be understandably reluctant to take on the risk of debt due to the uncertainty of future revenue sources to repay these debts and the organisational risks and personal liabilities they may face. Without access to capital, it is difficult for NFPs to invest in their own future capability and growth, and to smooth out peaks and troughs in their finances.
3. **Chronic underfunding of the full costs of service provision:** SVA research, conducted in partnership with the Centre for Social Impact and Philanthropy Australia, demonstrates that Australian NFPs are consistently underfunded to deliver the full cost of services. Our *Paying What It Takes* report showed that around 33% of Australian NFPs' expenditure is on 'indirect costs' – including training, IT and quality assurance.[3] However, the majority of funding agreements – whether from governments or philanthropy – cap the amount that may be spent on indirect costs. This challenge is compounded by the fact that NFPs often run on thin margins with limited reserves.[4] US research has shown that one of the key drivers of this financial vulnerability is insufficient funding of not-for-profit indirect costs.[5] This is called the 'non-profit starvation cycle', in which funders having inaccurate expectations of how much overhead is needed to run a NFP means these organisations underrepresent their costs. This leads to a sector starved of the necessary core funding required to create resilient NFPs delivering long-term impact on complex social issues. Our research indicates that similar dynamics are operating in Australia.

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[2] SVA and Centre for Social Impact (CSI), Partners in recovery: why charities need tailored support, *Partners in Recovery*, SVA, 2020, accessed May 2023
[3] SVA and CSI, Paying what it takes, 2022, SVA, accessed June 2023
[4] SVA and CSI, Partners in recovery: why charities need tailored support
[5] AG Gregory and D Howard, 'The nonprofit starvation cycle', *Stanford Social Innovation Review*, 2009, accessed May 2023.

These three factors make it difficult for NFPs to make the necessary strategic changes to provide quality jobs, support innovation and respond to emerging community needs. While for-profit organisations generally have the freedom to shift funding from other sources and to raise capital to invest in their future success, these options are often not available to NFPs despite the additional positive benefits that NFP providers generate for communities.

If government wants to strengthen the care and support economy, it needs to reconsider the way it funds service delivery. For example, it could:

- Adequately fund indirect costs in its contracts with NFPs
- Switch to more effective contracting and commissioning processes that create longer-term certainty for NFPs, do not unnecessarily restrict NFP flexibility, and which fully account for all the value/outcomes created by NFPs.
- Apply appropriate indexation to reflect increased costs faced by NFPs over which they have no control (such as inflation, and government-imposed costs such as superannuation guarantee increases)
- Avoid creating 'unfunded mandates' where NFPs are required to bear the cost of decisions made by government. Governments already do this for some direct costs – for example, in providing additional funding to service providers whose employees are granted significant wage rises by the Fair Work Commission.[6] If government introduces requirements that impose additional indirect costs on NFPs, such as new regulatory requirements that may necessitate additional back-office capacity, then it should also fund those mandates.
- Ensure that public communications about the importance of NFPs and the care economy do not include false dichotomies about direct and indirect costs.

These dynamics are explored in much greater detail in two research projects we have conducted, previously shared with the Taskforce, on the financial challenges facing the NFP sector:

- The *Partners in Recovery* project, in partnership with the Centre for Social Impact. This project tracked the financial health of the charity sector through the COVID-19 pandemic, and investigated a range of issues related to charity capacity, capability and viability.
- The *Paying What It Takes* project, in partnership with the Centre for Social Impact and Philanthropy Australia. This project explored the issue of underinvestment in NFP capability by funders, with particular attention to understanding indirect costs of delivering their work.

Ultimately, the three goals of the strategy will be unachievable without sustainable funding structures that recognise the full cost of service delivery:

- **Goal 1: Quality care and support** - NFPs will not be able to recruit and train a workforce that is able to deliver quality care and support, and will have fewer resources available to monitor and measure quality of outcomes
- **Goal 2: Decent jobs** - NFPs will not be able to offer decent jobs in which pay and conditions reflect the value of care and support work, work is conducted in ways that promotes good job quality and worker satisfaction, there are pathways for skilling and career progression, and improved leadership and management capability in the sector
- **Goal 3: Productive and sustainable** NFPs will not be able to deliver services on behalf of government as efficiently and effectively, and will face challenges in sharing, adopting and

[6] See, for example, the provision of increased funding to the aged care sector in recognition of the Fair Work Commission's decision to grant sector workers a 15% pay increase.

adapting innovations because they will be unable to invest in the required leadership, skill development and digital technologies.

To better achieve the vision, goals and objectives of the Strategy, we recommend that:

1. The Strategy document should acknowledge the critical role of the NFP sector as an employer in the care and support economy, as well as the constraints the sector faces as a result of the way government funds it.
2. The Action Plans for the various priority areas in the Strategy should explicitly include reference to addressing the challenges the sector faces as a result of the way government funds it. In particular, the Action Plans for Workforce, Innovation, and Pricing and Market Design will be critical here.
3. Entities within government with explicit responsibilities related to the NFP sector, including the Assistant Minister for Charities and the Australian Charities and Not-for-Profit Commissioner, as well as departments and Minsters overseeing funding contracts in relevant sectors, should be engaged in the development and implementation of the Strategy.
4. In implementing the Strategy, the government establishes a Care and Support Sector Sustainability Fund, which could provide non-ongoing funding to NFPs to investing in building their own capability and capacity for future productivity and innovation. We attach a short proposal for such a fund, and would be happy to share further detail if of interest.

We would welcome the opportunity to discuss any of the matters raised here with the Taskforce.

Yours sincerely,

Patrick Flynn
Director, Public Affairs

About SVA

Social Ventures Australia (SVA) is a not-for-profit (NFP) organisation with the mission to alleviate disadvantage, towards an Australia where all people and communities thrive. We influence systems to deliver better social outcomes for people by learning what works in communities, helping organisations be more effective, sharing our perspectives, and advocating for change.

This submission draws on our 20 year history as an intermediary in the social purpose sector, working with a wide range of NFPs through our Consulting, Impact Investing, and Programs arms, as well as our more recent research on strengthening the sector via our *Partners in Recovery* and *Paying What It Takes* projects.

Attachment: Establishing a Care and Support Sector Sustainability Fund

Recommendation

In adopting the National Care and Support Economy Strategy, the Australian Government should establish a one-off, time-limited *Care and Support Sector Sustainability Fund* to support not for profit organisations (NFPs) to undertake strategic and operational transformation so they can continue to strengthen Australia's economy and society via their participation in the care and support economy.

Rationale

NFPs face constraints specific to their regulatory and operational environment that can make it nigh on impossible to undertake the changes needed to achieve the goals in the Strategy. Their situation is uniquely challenging compared to that of for-profit businesses.

- Most NFPs do not have much financial margin or access to flexible untied funding. They are unable to redirect funds to invest in capacity building and organisational transformation even when there are clear long-term benefits to doing so.[7]
- They also cannot easily access capital to invest in their own future success, while businesses can offer equity or take loans with the expectation of future financial return.[8]
- Many of the policy supports available for businesses – such as accelerated depreciation and other tax relief – do not provide any assistance for NFPs as they do not pay company tax.
- NFPs are often driven by their mission to take on service delivery even when funding is inadequate, as part of their commitment to improved social outcomes.
- The Australian Government has recognised its role in supporting businesses and other organisations who face specific barriers to productivity and success. Examples include support for research commercialisation; export market development grants; and subsidised access to commercial expertise.[9]

Other governments in Australia and internationally have recently established capacity-building funds for the NFP sector in recognition of these challenges.[10]

Proposal

The *Care and Support Sector Sustainability Fund* will improve the productivity and effectiveness of NFPs by providing up-front support for them to invest in long-term transformation. This will position them to deliver the goals and objectives outlined in the draft Strategy.

Developing business and operational models, and implementing the resulting changes to organisational capability and business processes, takes time and capacity that NFPs may struggle to access up-front even though the medium-term benefits are clear. Resource-constrained organisations often do not have capacity to reflect on whether such improvements could enhance productivity, but case studies of those

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[7] SVA and CSI, Partners in recovery: why charities need tailored support
[8] SVA and CSI, Partners in recovery: why charities need tailored support
[9] SVA and CSI, Vital Support: building resilient charities to support Australia's wellbeing, *Partners in Recovery*, SVA, 2021
[10] See, for example, NSW's Social Sector Transformation Fund, Canada's Community Services Recovery Fund, and Singapore's Community Capability Trust

who have undertaken such changes are compelling.[11] They may also need support to identify and source new revenue streams and/or sources of capital, and improve financial management capability.

Priority areas for investment

The Fund would be open to a range of types of transformation and industry restructuring that are needed to pursue the goals of the Strategy, including:

- **Business, workforce and operational model adaption** - Many NFPs are identifying that their business, workforce and operational models are no longer sustainable in a with-COVID and post-COVID world, especially when combined with other forces such as an increased expectation of client-centric service delivery.
- **Leadership development and workforce capability** - Leadership and workforce capability has a direct impact on organisational performance, outcomes and impact. The sector often does not have the resources to access the kinds of leadership development that the for-profit sector takes for granted, even though building leadership capacity is a highly leveraged investment because it impacts the whole organisation.
- **Outcomes measurement and data analytics** - Only 44% of surveyed not-for-profits have systems that enable them to understand their impact.[12] Improving this capacity would provide an ongoing benefit to funders, including government, as well as service providers who would be able to better understand the impact of their work, and direct resources towards 'what works'.
- **Technology and cyber security** - Technology transformation could significantly improve efficiency and effectiveness in many NFPs, but under current funding frameworks they do not have the up-front resources to invest in such reforms.[13] Current technology arrangements may also pose significant cyber security concerns, especially for larger service delivery NFPs, posing material risks to organisations and the individuals they serve.

Nature of support

The Fund would offer an integrated package of support to NFPs who can demonstrate a need for organisational transformation. Support would be provided as a combination of:

- **Capability support** – the Fund would use a voucher model to enable NFPs to access professional support aligned to the transformation need of the charity. This support will enable them to generate the maximum possible value from the funds provided. Vouchers could be redeemed from an approved panel of suppliers, composed of entities with specialist knowledge of supporting NFPs that are transitioning. To build sector capability, priority should go to organisations oriented towards community benefit (e.g. charities, not-for-profit organisations, social enterprises, B-Corporations). For-profit service providers with demonstrated sector expertise could be considered for participation, especially if they are willing to provide support on a pro-bono or low-bono basis.
- **Cash** – direct grants to implement the change identified via the capability support. This might be required for investments in technology (including technology that can be shared by multiple NFPs) and other capital expenditure; for enabling staff time and capacity to implement reform; or to cover the up-front costs of change in governance or operational approaches.

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[11] See, for example, G Turnbull, '*Process efficiencies help non-profits achieve more impact*', *SVA Quarterly*, 27 October 2016
[12] Infoxchange, *Digital technology in the not-for-profit sector,* 2020
[13] Infoxchange, *Digital technology in the not-for-profit sector*. As of late 2020 only 46% of surveyed not-for-profits were using cloud-based systems, which posed major barriers to shifting to remote work during the Covid-19 crisis. Further, 49% of not-for-profits reported that funding and costs are the major barriers to making better use of technology.

Importantly, support would not be intended to provide working capital or cashflow support, or to subsidise day-to-day operations. Instead, it recognises the legal and operational constraints that NFPs face in being able to invest their usual funding streams into capability development.

In recognition of the importance of self-determination for Aboriginal and Torres Strait Islander communities, and the importance of supporting Aboriginal Community Controlled Organisations (ACCOs), a portion of the Fund should be dedicated to specifically supporting Aboriginal and Torres Strait Islander NFPs. The arrangements for these funds should be co-designed with relevant communities.

Funding

A Fund of $100 - $200m would support 2,000 - 4,000 NFPs to transform their operations. Depending on the size and scope of the organisation, they could receive between $10,000 and $250,000 in cash and capability support. Contributions from corporate or philanthropic sources to the Fund could further increase the size and reach of the Fund's impact. Phasing of the funding could be flexible depending on budget constraints and fund size but would be time-limited.

To maximise overall value for money achieved by the grants, a further $10-$30 million would be required for operational costs to provide co-design support for applicants; facilitate collaboration between NFPs; and monitor and evaluate impact.