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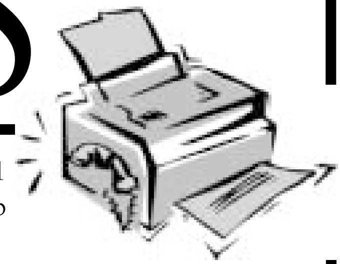

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July 20, 2004

Private Agency, Private Gains

With its references to mysterious personal assistants, working vacations in Florida, and under-reported income tax, provincial auditor Jon Singleton's report on the Hydra House social service agency was about as salacious as a document produced to meet generally accepted accounting principles can get.

Hydra House is a for-profit, privately owned social service agency that was established in the mid-1980s. With approximately 10 facilities in Manitoba, it provides residential services to people with disabilities of all ages, and specialized foster care. Almost all its revenue comes from fees paid to it by the Manitoba government.

Singleton concluded that there had been a number of instances where the public funds that Hydra House received were "not used for the direct care and maintenance of Hydra residents, but instead were used for the benefit of Hydra executives and others." In particular, over a six year period salaries, bonuses, and consulting fees in excess of $3.8 million were paid to up to five Hydra executive positions, while thousands of dollars were spent on personal benefits for these managers.

As a private agency Hydra House was able to generate significant profits. But it is also apparent that the Manitoba government was not able to share in the benefits.

The Hydra House story dominated the newspapers for several days, but aside from leaving one with the impression that public money was, in some manner, wasted, newspaper readers could be forgiven if they felt uncertain as to just what went wrong.

Doing what comes naturally

The auditor's report shines a very revealing light on how a for-profit social service operates. Advocates of privatization always argue that the private sector is able to provide services at a lower cost than the public or non-profit sector. It can do this because private businesses have an incentive to cut costs, as doing so can lead to higher profits, which are theirs to do with as they please. In this case, profits were used—among other things—to:

- pay Hydra executives salaries that were 58% higher than they would be in the non-profit sector;
- send a Hydra executive to Florida for two weeks to provide the company owner (who maintained a residence in Florida) with an update on company operations;
- spend over $17,000 for furniture and appliances that were delivered to the residence of the personal assistant of the owner;
- pay the personal assistant's cable bills;
- repair the personal assistant's trailer;
- donate $19,200 to a private Winnipeg high school.

Singleton concluded "the salary amounts paid to the personal assistant [who spent four to five months a year in Florida] were not reasonable in relation to the duties performed." Indeed, Singleton had considerable trouble puzzling out what it was the assistant did.

The auditor took the position that the money provided to Hydra House was supposed to be used substantially for the direct care and maintenance of the children and adults under its care. However, he also recognized that there was nothing to prohibit the company from turning a profit or spending the profit on benefits for the owner, his assistant, and the assistant managers.

Unanswered questions

How did the company manage to create a surplus at a time when most social service agencies are struggling to make ends meet? Critics of privatization usually argue that privatized firms usually succeed by cutting the quality of service and cutting wages.

While the auditor did not assess the quality of care at Hydra, he reported that "general discussions with staff of the Department [of Family Service] and other government agencies that provide funding to Hydra indicated that they were generally pleased with the quality of care being provided by staff of Hydra." Subsequent newspaper reports indicate that the Association for Community Living received three complaints about the agency over the last four years, while a former employee has complained about the state of one of the residences to the media.

The Canadian Union of Public Employees, which represents workers at Hydra House, claims that management was always pleading poverty, even when it was running profits and receiving unneeded deficit reduction funding from the province. The last union contract provided the workers with a 6.5 percent increase over three years. While Singleton concluded that Hydra managers are making far more than similar managers in the non-profit sector, he did not provide a similar comparison for Hydra employees. However, according to CUPE, Hydra workers make less than similar workers at other unionized social service agencies.

Finally, because the province negotiates differing funding agreements and different per diem rates for clients with each social service agency that it deals with, it may turn out that Hydra House's real skills were not in delivering care for less, but in negotiating better deals.

Capturing the benefits

In any case, it is clear that as a private agency Hydra House was able to generate significant profits. But it is also apparent that the Manitoba government was not able to share in the benefits of privatization—and advocates of privatization always say that privatization will lower government costs. From the taxpayers' perspective, there was no benefit from dealing with a private agency.

Singleton is recommending that the government negotiate detailed agreements with service providers and make sure that they provide the information the government needs to determine if the company is making an excess profit. Singleton's report also provides telling detail on why the government has to monitor for-profit agencies so closely. It turns out that the company was not reporting many of the benefits that the company managers were receiving to Revenue Canada. When such benefits are unreported, employees can usually get away without paying taxes on them.

The story of Hydra House underscores an often-overlooked argument against privatization: that for the government to capture the benefits, it must hire an army of auditors and accountants to watch over the shoulder of private service providers who, because they are for-profit agencies, have an built in incentive to hide the size of their profits from the government. It would be far better, and more efficient, to have these services delivered by the non-profit sector.

—Doug Smith

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