UNLOCKING THE VALUE OF A JOB:
Market design in employment services

David Hetherington
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Executive Summary

The Federal Government’s Job Network is no longer fit-for-purpose. The program has been successful, but its economic backdrop has changed. Job Network was established to place large numbers of unemployed people into scarce jobs. Its role today is vastly different - preparing a smaller number of (often) disadvantaged individuals for a wide variety of jobs. Its focus must similarly change: the primary task must be to build ‘employability’ rather than to act as a job matching service.

The Federal Government must redesign the employment services market to reflect today’s reality. Incentives should be restructured to better align the interests of jobseeker, Job Network provider, employer and taxpayer. Performance information should be made freely available to inform choice and raise quality. Contract structures should be reconsidered to enable flexibility and encourage localised innovation. Above all, the government’s investment in the Job Network should be predicated on the full value of a job.

This paper argues that a job’s value exceeds its nominal wage, and includes health, justice system and intergenerational benefits. Critically, this value is shared between worker, employer and the community. Our analysis shows that a $40,000 job generates total value of over $46,000, and that around $21,000 of this is public value. By contrast, the maximum amount invested by Job Network in that job is $6,600. Consequently, we argue that a significant increase in investment in the most difficult Job Network cases is warranted. This investment would deliver superior economic returns and continue to build Australia’s human capital.

The specific recommendations of the paper are:

• Restructure payments to providers. Instead of milestone payments at 13 and 26 weeks, pay a smaller up-front payment to providers, followed by a monthly trailing commission for up to 3 years of ongoing employment. Job Network providers would use this additional payment to build employability through evening classes or periodic weekend programs.

• Pay more for the service of moving the long-term unemployed into work. Evidence shows that these cases take time, and this time requires money. Instead of capping payments at $6,600, we should be willing to invest up to $23,000 (half the annual value of a job) in generating a $40,000 job.

• Quarantine a share of the existing Job Network budget to allow community joint ventures to tender for seed capital. We must move beyond the one-size-fits-all approach which pays providers from a simple fixed schedule for placing an individual into work. We need to encourage innovative local enterprise models, which allow existing operators to work creatively with secondary providers of skills, training, housing support and drug counselling.

• Publish KPI3 scores on Job Network provider quality and include these scores in the Star Ratings system. This would allow clients to make an informed decision when choosing between providers and raise overall service quality within the system.
Section I: Redesigning the Job Network

Throughout the 1980’s and 90’s, the world looked to Australia as a hub of policy innovation. Superannuation, HECS and the Pharmaceutical Benefits Scheme were all considered groundbreaking public programs. The Howard Government upheld this tradition with its announcement in 1996 of the creation of Job Network, which outsourced provision of employment services to the private and non-profit sectors.

Job Network positioned the Federal Government as purchaser, rather than provider, of employment services and created a competitive market for these services. The underlying rationale was to “create a new incentive framework… with the intention of rewarding job assistance providers primarily for successful placement of jobseekers, while additional incentives would be introduced for placing the most disadvantaged among them.” (OECD, 2001: 89)

On most measures, the scheme has been a notable success. In 2005-06, it placed almost 640,000 Australians into jobs, at a unit cost considerably lower than previous programs (Brough, 2006). Today however, Job Network is no longer fit-for-purpose. The scheme dates from the 1990’s economic recovery, when the policy problem was how to link up an abundant supply of job-ready job seekers with the shortage of available jobs. In today’s economy, the problem is not finding jobs; it’s finding labour – so creative matching is critical.

What’s more, an increasing share of Job Network clients is long-term jobless who need to build employability as much as they need job matching. Despite this, the system is still structured around an incentive scheme targeted at placing people in jobs for a maximum of six months. There is no underlying assessment of the value of a job and the level of public investment this warrants.

It’s not about market versus state anymore. The real debate is about how to design the market

Some commentators see the solution as more of the same. Saunders (2008) focuses on the dilution of the ‘work first’ principle in the Job Network system. He raises concerns about the motivations of non-profit Job Network providers, and whether their charitable origins mean they are too soft on job seekers who do not meet participation criteria. He worries that these providers will convince the Rudd government to decouple access to welfare from the requirement to work. This is a classic 90’s debate – rights, responsibilities, and work-for-the-dole.

The public debate has moved on. Most of us accept the role of a market in helping the unemployed into work. It’s not about market versus state anymore. The real debate is about how to design the market – how to set the rules of the game to encourage behaviour that advances public policy goals.
Saunders argues that Australia has led the world in market design in employment services. True, but design flaws remain. What’s more, as the economy changes, the market must change too.

So how do we design the employment services market better? What needs to happen to align the interests of job seekers, potential employers and the taxpaying public? The starting point is that, in this market, government is really ‘buying’ a service from employment agencies - the service of moving new people into work. That’s what government is paying for. So it makes sense to begin by asking what that service is worth to government – what is the value of moving a person from welfare to work?

Section II: The value of a job

The government as designer must clearly establish the value of a job. Good economic policy should take into account the full economic benefits outside the immediate transaction – the ‘externalities’, in economic jargon. Not just the narrow financial value of getting someone into work, but the wider social value that creates. This is a ‘full-cost economics’ approach to policy development – one which accounts for the complete range of private and social costs/benefits of a market’s activity (see Hetherington and Cooney, 2007).

There are obvious economic benefits to placing an individual into work: income for the individual, tax receipts and reduced welfare payments for the public. The intangible social benefits, though, are potentially far greater. These have the dual advantages of decreasing taxpayer outlays and improving quality of life. Evidence suggests that a person in employment will enjoy better health. Mathers and Schofield (1998) show that unemployed Australians between the ages of 25 and 64 are twice as likely to report being in poor or fair health (in contrast to good or excellent health), and report 30-40% more chronic serious illnesses than their working compatriots. These differences could not be explained by higher levels of smoking, drinking, inactivity or obesity.

Other studies show that unemployment increases likelihood of contact with the justice system. In a review of regional indigenous communities, Weatherburn et al. (2006) find that unemployed residents are 54% more likely to be charged with a criminal offence and 88% more likely to be imprisoned than employed residents.

Critically, there is an intergenerational multiplier effect at play here: the children of a newly employed person are now more likely to be employed and enjoy these same benefits. We believe these benefits, private and social, represent the total value of a job and determine how much government should invest in order to...
place an unemployed person into work. What does this mean in practice? Say we place a single, childless worker in a job paying $40,000 a year. The worker enjoys a net annual gain of $25,201, made up of wages and superannuation minus benefits withdrawn. The public gains $20,550 in tax receipts, welfare savings and reductions in health and justice expenditure. All up, this is a net gain of $45,751, or $3,813 for every month the worker stays employed and importantly, it is cumulative, rather than one-off, value creation. This value is illustrated in Figure 1.

It is important to note that this is an extremely conservative estimate of the value of a job. By assuming a childless worker, we have not included the intergenerational benefits which accrue to children. Under conventional finance theory, these would be discounted near to zero as they occur well into the future, but from a social perspective, their value should not be ignored.

Additionally, we assume that there are net returns to the employer from hiring the individual (otherwise they would not do so). Although we have not attempted to quantify these, they should be included in the total social value of a job. Interestingly, these workplace returns do not accrue in work-for-the-dole situations where the activity would not otherwise be undertaken by the private sector. Work-for-the-dole programs alone do not break the cycle of welfare dependency, or deliver the full suite of benefits outlined in this paper. If they are not improving an individual’s employability, it is difficult to see the intrinsic value of these programs.

This analysis suggests that moving a single, childless worker into a job paying $40,000 per year creates a combined public and private value of almost $4,000 per month (based on a conservative estimate of the combined benefit of increased private income, higher tax receipts, lower welfare costs and other social goods).

To capture this value, the design of the market must change, and there are four specific areas where action is needed.
Section III: Employability, not just matching

First, the structure of payments should be redesigned so that providers are rewarded for activity that builds employability, rather than simply for job matching. In an environment of increasing economic uncertainty, matching will remain a critical element of the system, but employability must be the current design priority. This involves an explicit acknowledgment that the primary function of the employment services market today is to develop human capital – the skills and capabilities that allow individuals to contribute in a modern workplace. Matching workers with jobs is a secondary function: in an environment of labour shortage, employers and recruitment agents are more than capable of doing this themselves.

However, under the current system, Job Network providers are paid for placement rather than employability. The most common measure of a successful outcome under the Job Network system is continuous employment for 13 or 26 weeks, and payments to providers are made on this basis. But even 26 weeks is hardly a permanent job: the incentive is targeted at initial job placement rather than ongoing employability.

The problem with lump sum payments at milestone periods is that the provider has no financial interest in the client staying employed for more than a few months. Yet the policy goal is ongoing employability, not just the initial job placement. How can the design be improved to deliver this?

One simple way is for government to pay a smaller up-front payment, followed by a monthly ‘trailing commission’ for up to 3 years of ongoing employment. In exchange the provider would deliver ongoing training and support services, continuing to build employability. Under this system, the interests of client, provider and public are more closely aligned.

There is a good analogy in the financial services sector. An independent financial adviser (IFA) receives an upfront fee from a fund manager for a product sale, and then a small commission for each month the investor holds her funds in that product. The fund manager doesn’t want to pay the full commission upfront since this removes the IFA’s interest in the client relationship. With a trailing commission, the IFA has a stronger incentive to offer quality customer service to ensure that the investor doesn’t take her funds elsewhere.

In the Job Network system, for a case of moderate difficulty where the jobseeker has been out of work between 13 and 24 months, the government pays $1,650 for employment sustained over 13 weeks, and an extra $825 at 26 weeks. If we value a job at around $4,000 a month, then it makes sense to pay less upfront, with an additional payment for every month employment is sustained.
Job Network providers would use this additional payment to build employability, by developing vocational skills, oral and written communications, bookkeeping know-how, or ability to work in groups. This could occur in evening classes or a weekend program one day a month.

We propose a structure where the provider receives $975 in the first month of employment, and $300 each month for the next five months. The payment would then drop to $200 in months 7-12, $150 in months 13-24 and $100 in months 25-36 (the profile for Year 1 is outlined in Figure 2 below). The result is that the provider receives exactly the same amount ($2,475) for the first six months compared to the current scheme, but then gets an additional payment for the next 30 months to invest in employability. Since government gains over $1,400 each month in public benefits, it’s a worthwhile investment to pay a provider to help the worker remain in work.

This change would require a transition period to allow providers to manage their cashflow, but over time it will more closely reflect the provider’s expenditure across an individual case. Most importantly, it rewards them both for matching (in month 1) and for ongoing employment (in subsequent months).

To test this approach, the Government should implement trials in a handful of locations, with a cap on total payments over a period of three years. It’s the best way to understand what works, and what doesn’t.
Section IV: Investing in human capital where we need it most

Secondly, we need to invest more to move the long-term unemployed into work. This is a market where the government sets the price as well as buying the services, so maybe it’s no surprise that over time, the price paid for employment services – in particular, for the hardest cases – has been too low.

Finding jobs for long-term jobless people is difficult and costly. They often have low skill and education levels, and many experience housing problems, relationship difficulties, and mental illness. The cost for Job Network providers is also higher and so they are tempted to ‘cherry pick’ higher qualified candidates, rather than invest too heavily in hard-to-place cases. The temptation is to ‘park’ the hard cases in ongoing welfare programs.

Yet there is enormous public value in moving the long-term unemployed into work. The social, health and intergenerational benefits are multiplied. Existing contracts make some extra provision for dealing with the most difficult cases, but we need to go further. We should invest more - considerably more - to Job Network providers to help these people move into work.

This is not just about more interviews and better job-readiness training. Job Network providers should be contracted to widen their suite of services to allow them to address housing problems, mental illness and substance abuse alongside job search and training. This integrated case management process represents a high-return investment for taxpayers as it addresses the underlying causes of long-term unemployment, as well as the job search process.

The integrated case management process represents a high-return investment for taxpayers

The value of a $40,000 job is $4,000 a month, yet under the Jobs Network, even placing the hardest cases of long term unemployed people is valued far less than this. The government will buy this service for just $4,400 when employment reaches three months, with another $2,200 at six months.

That’s just over a tenth of the full value of a new job in the first year alone. People who are job ready don’t need extra provisions. But those who are not job ready, whether due to mental illness, housing concerns or limited education, cannot be successfully treated as though they simply have an unemployment problem – this will always fail to reach the desired goal of long-term employment. These people need extra support in order to secure and maintain employment.
One of the keys to helping the hardest cases is time. The case studies of Jo and Mary (see box overleaf) show that continued in-work assistance over extended periods is vital to building employability. Where this assistance is disrupted, the impact can be severe. An investment in time is a critical success factor and as we know, time equals money. So rather than spending 10% of the value of a job to place the most difficult cases into work, we need to invest more. If we apply the trailing commissions approach to the most difficult cases and invest up to 50% of job’s value in supporting them through the first three years, we still see an enormous social return and we dramatically increase the probability of employment beyond six months (see Figure 3 below).

Existing contracts do make some extra provision for dealing with the most difficult cases, but this must go further. Simply, the Government must be prepared to invest more – much more – in Job Network providers for this valuable service.
CASE STUDY 1: The need for flexibility

Jo has a psychiatric illness. He was enrolled in a Job Network program but suffered a severe health relapse and was unable to work for over six months. In the meantime, Job Network’s requirements had changed and although Jo re-entered the system, the new framework under which the provider was obliged to operate differed greatly from Jo’s original program. Even though his participation agreement was suspended when he became ill, Jo ultimately had to leave the provider. Jo struggled over the next 12 months. The provider’s staff kept tabs on how he was coping, sending him newsletters to make sure he still felt connected, but Jo ended up in hospital interstate where he knew no-one. It took him another six months to recover and he eventually returned to the provider.

Under existing requirements, Jo must go through an assessment process again to access the provider’s service. He is required to go back to Centrelink where his past experiences have not been good. He has decided that he won’t access the specialist employment service (DEN). Instead he will utilize one of the other employment options, an integrated model focused on labour hire and temporary staff services. This is not related to any government funding and therefore not restricted by contractual obligations regarding assessments. Jo is working now and has regained the self-esteem and independence that go along with a regular income. The burden on his parents is greatly reduced and in turn their health has improved as they are worrying less about him. If Jo becomes ill, the provider can replace him with little impact on the employer and no sense of guilt felt by Jo.

CASE STUDY 2: The importance of time

Mary has learning difficulties and became a client of a Youth Services program. She accessed the program through the Futures For Young Adults, an initiative of the Victorian government. This program focuses on transitioning young people with disabilities from school into independent living skills training and then into work. This worked well for Mary as she progressed from the Youth Services program into work experience and then into a position in one of the Job Network provider’s businesses. She worked for them for three years and has now progressed into a position with a large supermarket.

One of the most important factors in Mary’s success has been time. She had the time to develop confidence, the time to develop interpersonal and communication skills and the time to experience work within a supportive and caring environment - she was afforded six years in which to achieve this.

Unlike Jo, Mary had the opportunity to try things without the added pressure of achieving within a limited time frame. In both these cases, the pressure on the provider’s resources was extraordinary, but the results are testament to what can be achieved. Everyone can work and contribute - but not without adequate resources to support them. Time is a drain on resources but everyone progresses at a different pace. Jo and Mary are evidence of the benefits of patience and an organisation’s willingness to develop options that don’t quite fit the accepted service delivery models currently funded by Job Network.
Section V: New partnership structures

Thirdly, we must move beyond the one-size-fits-all approach where providers are paid from a simple fixed schedule for placing an individual into work. In its place, new incentives are needed to encourage choice, flexibility and innovation. We propose that the system should support innovative community enterprise models.

Consider an area like Dandenong, on Melbourne’s eastern fringe. It’s a centre of manufacturing and light industry. Here, employers are scrambling to fill vacancies in logistics, materials handling, truck driving - all sorts of skilled and semi-skilled work.

Yet just a few kilometres away are suburbs like Doveton and Noble Park. They’re centres of welfare where newly arrived migrants, single parent families and others go without work. This is a solution waiting to happen. For example, a local welfare organisation sets up a new local enterprise to build local skills - anything from truck driver training to drug counselling. Potential employers would directly invest with seed funding or start-up capital. Local government relies on flourishing businesses for rates income; housing authorities gain higher rents if more tenants are in work. These organisations could also invest in the enterprise, with capital and infrastructure.

In a real-world example, a major retail bank partnered with a Job Network provider by sponsoring a ten-week work experience program for ten unemployed refugees. The bank went on to hire six of these refugees into full-time work. Two subsequently found further training, and the other two found full-time work elsewhere. This was surely cheaper and more effective for the bank than general recruitment - at the same time as generating positive economic and social benefits for the wider community.

Under these models, a form of ‘social procurement’ can emerge. Instead of providing top-down services, government becomes the buyer of a community organisation’s capacity to help hard-to-place people to build the specific skills the economy needs. Instead of just selling job matching, welfare organisations must be able to sell this kind of clever service to the Federal Government acting as the buyer. And if the price is right, they’ll be able to expand these services and get more people off welfare and into work.

Finally, it is not just the quantum of money that matters, but the flexibility of payments to providers. Currently, the Job Network budget is allocated through a one-size-fits-all approach which pays providers from a simple fixed schedule for placing an individual into work. Instead, the government should quarantine a
share of the Job Network budget for local enterprise models. Job Network providers would partner with local businesses, councils or community organisations to tender for start-up capital. Tenders would be awarded to the most compelling business plans, and government would match the capital invested by stakeholders, with a ceiling of $250,000 per venture.

This approach enables creativity, flexibility and adaptation to local circumstances. It will uncover those models which work best and are suitable for replication across other sites. Critically, the approach provides both incentives for new entrants, and incentives for existing operators to work creatively with secondary providers of skills, training, housing support and drug counselling.

Section VI: Better information, greater choice

Markets fail when participants lack full information about the quality, availability or cost of the services on offer. Employment services are no different – the better the information about alternative providers, the greater the ability of job seekers to choose a provider that matches their particular needs. In theory job seekers are able to make a choice amongst Job Network providers, but many individuals find this process difficult and confusing, and most opt for Centrelink to make the choice for them (McNally, 2003: 14). Market design can overcome this failure by providing freely available, standardised information on historical behaviour, preferences or processes within the market.

The better the information, the greater the ability of job seekers to choose a provider that matches their needs

In part, this occurs already. Clients have access to providers’ scores on the Star Ratings system, a composite measure of the rate of outcomes for Intensive Support job seekers and the rate of overall job placements for eligible job seekers. However, perhaps the most critical information parameter remains hidden. One of the Key Performance Indicators on which providers are measured is a quality rating based on exit reports from clients and site visits by DEEWR (KPI 3). Yet this feedback is not incorporated into the Star Ratings system, and therefore not available to clients when choosing between providers.

This information deficit can be easily overcome. Job Network clients should be given access KPI 3 scores to enable them to reach an informed purchase decision. This enables clients to engage the provider that best suits their needs, and as importantly, gives providers added incentive to deliver high quality service to build their client and revenue base. A simple change, but one which will improve overall quality within the market and further align provider incentives with policy goals.
Section VII: Conclusion and recommendations

There are signs the new government in Canberra understands all this. In his book *Postcode*, Wayne Swan, now Federal Treasurer, outlined ideas to “extend Centrelink’s role beyond the simple task of distributing income support payments, to ensure it works in partnership with Job Network and welfare agencies on initiatives that generate new jobs” (2005: 213).

No-one knows exactly which approaches will work, but with a new government hungry for ideas and a new round of contracts in 2009, we have a golden opportunity to experiment with innovative design solutions. Given this opportunity, not changing is not an option. An argument that the Job Network shouldn’t move forward is an argument that Dandenong’s employers, and Noble Park’s families, should just give up and settle for a low-skill, low-wage future. Or even worse, that Dandenong should import labour from elsewhere in the country and the world, while Noble Park’s families fall further behind.

The old way: accept failure, cut wages, leave people behind. The new way: aim higher, invest in human capital, and combine prosperity with fairness.

**Recommendations**

- Restructure payments to providers. Instead of milestone payments at 13 and 26 weeks, pay a smaller up-front payment to providers, followed by a monthly trailing commission for up to 3 years of ongoing employment. Job Network providers would use this additional payment to build employability, by developing vocational skills, oral and written communications, bookkeeping know-how, or ability to work in groups.

- Pay more for the service of moving the long-term unemployed into work. Evidence shows that these cases take time, and this time requires money. Instead of capping payments at $6,600, we should be willing to invest up to $23,000 (half the value of a job) in generating a $40,000 job.

- Quarantine a share of the existing Job Network budget to allow community joint ventures to tender for seed capital. We must move beyond the one-size-fits-all approach which pays providers from a simple fixed schedule for placing an individual into work. We need to encourage innovative local enterprise models, which allow existing operators to work creatively with secondary providers of skills, training, housing support and drug counselling.

- Publish KPI3 scores on Job Network provider quality and include these scores in the Star Ratings system. This would allow clients to make an informed decision when choosing between providers and raise overall service quality within the system.
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