FAIRER FUNDING AND SERVICE AGREEMENT FOR THE COMMUNITY SECTOR

Briefing Paper

March 2015

VCOSS
Victorian Council of Social Service

About VCOSS

The Victorian Council of Social Service (VCOSS) is the peak body of the social and community sector in Victoria. VCOSS works to ensure that all Victorians have access to and a fair share of the community's resources and services, through advocating for the development of a sustainable, fair and equitable society. VCOSS members reflect a wide diversity, with members ranging from large charities, sector peak organisations, small community services, advocacy groups and individuals involved in social policy debates.

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EXECUTIVE SUMMARY

The community sector plays a valuable role in building resilient, cohesive, healthy communities across Victoria. Its diverse make-up helps people facing disadvantage across a wide range of circumstances to find the support they need to overcome challenges and build brighter futures.

In delivering tailored support through a wide range of services and programs, the community sector builds constructive relationships with people who may be marginalised and living in poverty, and gains insights and on-the-ground understanding of the social issues people face. From all this, it is able to give these people a voice, and speak from an informed and authoritative base in advocating for policies that help tackle the causes and ameliorate the effects of poverty.

In an increasingly complex and unequal world, Victorian community sector organisations are facing rising demand for services and increasing complexity in the issues people are facing. It is also facing rising service provision costs, and mandated increases in employee entitlements.

To continue its work strengthening Victorian communities and supporting those facing disadvantage, the community sector needs a Funding and Service Agreement that fairly secures its funding base and sets a range of relevant parameters to work within. With this in mind, VCOSS calls for a new Funding and Service Agreement for 2015-2018 that:

- Fully funds the Equal Remuneration Order

- Provides appropriate funding indexation that enables organisations to meet the rising costs of delivering services to Victorians

- Sets fair and balanced parameters for the next three years, which address highlighted problems with the current agreement.

This briefing paper reinforces previous submissions made to the funding departments as part of a year of negotiations around the 2015-18 Service Agreement. The proposals contained are aimed at setting the basis for a strong and effective community sector that delivers quality services to people in need of support, in partnership with government.

Key messages in relation to the proposals made in this briefing paper include:

EQUAL REMUNERATION ORDER

- The ERO is a legal obligation for organisations and must be fully funded by the Victorian Government.

- The ERO has been funded up until the end of June 2015, but government funding is required beyond this.

FAIRER INDEXATION

- Indexation for the period 2012-2015 did not keep pace with rises in minimum wages and consumer prices. Wages and prices both rose faster than the indexation rate over the 2012-15 period, which, along with a failure to fully fund mandated superannuation increases, has left organisations with an estimated 2.6 per cent real funding cut.

- A fair indexation formula is proposed for the 2015–18 Funding and Service Agreement, which is an annual adjustment linked to changes in wages (National Minimum Wage Order) and prices (Melbourne CPI) with an 80:20 split. This approach is one taken in other jurisdictions.

- What the Victorian government will get for fairer indexation:
  - Community organisations focussing on the best way to help people receiving funded services, rather than scrambling to find staff and service cuts
  - Services for people who need them that are managed through sustainable, long-term investment approach, rather than a short-term cost-cutting focus
  - Community organisations capable of collaborating with government and each other to maintain and implement quality standards and build a more cohesive sector, rather than focussing inward on revenue problems
  - Services with the financial stability required to innovate, and be in a position to explore opportunities to innovate, experiment and evaluate their services.

A FAIR AND BALANCED SERVICE AGREEMENT

- The community sector holds significant concerns about the content and implementation of the 2012-15 Service Agreement. These problems include:
  - The government currently own community service **organisations' service and client records**, which is unnecessary and inappropriate given organisations are independently regulated and governed. Divesting ownership of client records interrupts these organisations' engagement and relationships with clients in need of support.
  - There is a lack stated time periods in **notice requirements** by the department and by organisations in the current agreement which puts them at significant risk in their operations and relationship with government.
  - The **dispute resolution** provisions in the current Service Agreement are problematic, because there is no real ability for organisations to resolve disputes in relation to the agreement clauses.
  - Funding departments are able to vary the current Service Agreement with individual organisations, without the written consent of the organisation, because of the deeming processes. This prevents true negotiation and acceptance of **variations** by organisations.
  - Clauses giving the department the right to unilaterally **suspend, cease or terminate** the current Service Agreement are overly complex, inconsistently drafted and lacking in procedural fairness.
  - The unrestricted license given to funding departments to use an organisation's background and current **intellectual property** is of concern, because while organisations may wish to share their intellectual property, they do not want it taken out of their control.
  - There is uncertainty around the legal status of the **Service Agreement Information Kit**,

because of the department's ability to unilaterally change its content and policies. This can impact on organisations' ability to meet contract requirements.

- After a year of negotiations with the funding departments over the 2015-18 Service Agreement, new clauses were presented as proposed solutions the above problems by the non-government members of the Service Agreement Working Group (SAWG), with the assistance of Justice Connect Not-for profit law.

- These proposed clauses were not incorporated in the Draft 2015-2018 Service Agreement subsequently provided by the departments to the non-government members of the SAWG, which was greatly disappointing to the sector.

- VCOSS in collaboration with the non-government SAWG members have since made a joint submission, to the Department of Health and Human Services and Department of Education and Training in March 2015, outlining this disappointment, reiterating the problems raised by the sector and again presenting the proposed solutions.

EQUAL REMUNERATION ORDER

Fair Work Australia awarded the Equal Remuneration Order (ERO) in 2011, in recognition of the historical under-payment of community service workers. It described its decision as an important step toward achieving equal pay for workers in the sector, and one that could strengthen the workforce by helping organisations attract and retain skilled staff. The ERO means community organisations must pay wage increases of between 23 and 41 per cent to workers over eight years, through to December 2019.

The ERO was funded by the Victorian government over the first three years of its implementation, up to June 2015. However ERO funding for the wage increases has not been included in state budget forward estimates after June 2015.

As highlighted in the VCOSS Budget Submission 2015-16, a commitment to fund the ERO is needed from the Victorian government to ensure community organisations continue providing quality services to help people overcome disadvantage. The government has also previously stated that it has an obligation to fund the ERO.[1] It has previously been publicly stated that funding the ERO in 2015-16 would cost $160 million in 2015-16.

Without ongoing government funding to cover the prescribed ERO wage increases, community organisations will need to cut staff and services, putting at risk the wide range of programs and services they provide to those facing disadvantage.

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[1] Mr James Merlino, addressing the VCOSS Annual General Meeting, 17 November 2014.

FAIRER FUNDING INDEXATION

Like all organisations, community organisations face rising costs associated with wages, salaries and other non-salary items needed to operate. As highlighted in the VCOSS 2015-16 State Budget Submission, the state government can help community organisations meet the rising costs of providing services, by annually indexing its funding for the sector using an appropriate formula that accounts for rising wages and other rising costs of service delivery.

Wages and prices have both risen at a greater rate than the 2.0 per cent indexation rate applied to government funding of community services over the 2012-15 period. Wages rose on average 2.83 per cent per annum and non-wage components (prices) have risen on average 2.38 per cent per annum. VCOSS calculates that community services have sustained a 2.63 per cent cut in real funding during the 2012-15 funding period, due to inadequate indexation (including a failure to fully fund mandated superannuation increases). For more analysis regarding this, please see Appendix 1, Table 1.

If governments apply an indexation rate that falls below the rate at which costs are increasing, funding is cut in real terms. Community organisations must then cut their operational expenditure. An independent report has found the community sector has already made significant productivity gains, and that achieving further gains would be difficult because of the labour-intensive, people-oriented nature of its services[2]. Cutting expenditure simply means people needing support will receive a lower standard of care, or that fewer people will get the support they need.

When asked about indexation in the lead-up to the 2014 state election, Victorian Labor assured community organisations that it was "absolutely committed to working with you on a fair and reasonable outcome".[3]

This briefing paper proposes the following 'real cost' variable indexation model to ensure funding keeps pace with the real costs of providing services, but that neither government nor the community sector faces windfall losses or gains due to fluctuating price pressures. It also proposes an additional one-off superannuation and funding payment be made in recognition of inadequate indexation over the 2012-15 funding agreement period.

For more background and analysis regarding the need for appropriate indexation in the community sector, please see Appendix 1 – Fairer indexation for the community sector.

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[2] Allens Consulting, 'How many wheelchairs can you push at once?' — Productivity in the community service organisation sector in Victoria, 2008, Victorian Council of Social Service

[3] Mr James Merlino, addressing the VCOSS Annual General Meeting, 17 November 2014.

A ‘real cost’ variable indexation formula

Historically, community organisations have discussed and advocated for a specific indexation percentage for each year over a three-year funding period. However, this approach contains risks that funding increases will be granted at a higher rate than actual rises in costs incurred over the period and organisations will gain a windfall, or conversely, that the indexation will not cover the actual rising costs incurred over the period and organisations will face a shortfall.

To mitigate this risk, VCOSS advocates linking indexation to actual wage and consumer price increases. This could then be built into the state’s recurrent budget, and projected as an ordinary parameter variation by the Department of Treasury and Finance, rather than being the subject of community advocacy every three years.

VCOSS proposes the following formula for funding increases for the 2015-18 funding and service agreement period; and to be used beyond as a recurrent state budget item:

Annual indexation = 0.8 x NMWO + 0.2 x CPI

Where:

NMWO = the minimum wage percentage increase determined in the National Minimum Wage Order by the Fair Work Commission for the funding year

CPI = the year-to-March Melbourne consumer price index immediately preceding the funding year

This formula uses the most current and relevant wage and price changes, as made available before the commencement of the funding year. This means it can be calculated and disseminated to community organisations before the funding year starts, as soon as the NMWO increase is known, along with the current CPI for that period, and can be immediately factored into organisational budgets.

This approach is taken in other jurisdictions, including West Australia and the Australian Capital Territory, where indexation is linked to changes in wages and prices with an 80:20 split.

A one-off superannuation and funding shortfall payment

As proposed in our State Budget Submission 2015-16, VCOSS further proposes a one-off payment of 2.6 per cent, on top of the above ‘real cost’ variable indexation formula, to cover superannuation costs (0.4 per cent), underfunding of NMWO wage increases (0.8 per cent), and the lack of indexation for the non-wage costs (1.4 per cent) during the 2012-15 funding period.

We further propose the Victorian government commit to using the ‘exceptional circumstances’ clause of the standard service agreement, to cover genuinely unexpected increases in costs, such as the 2012 federal legislative changes to the superannuation guarantee.

CREATING A FAIR AND BALANCED SERVICE AGREEMENT

Community sector organisations hold significant concerns over the 2012-15 Service Agreement, and have stated that its implementation has caused them significant problems.

VCOSS has been working for more than a year to negotiate a fairer Funding and Service Agreement for 2015 -2018. VCOSS has negotiated on behalf of the community sector as part of the Service Agreement Working Group (SAWG), convened by the Department of Health and Human Services and Department of Education and Training. In this period VCOSS and the non-government SAWG members provided draft clauses and proposals to improve the Service Agreement, based on feedback from their organisations and members.

In February 2015, VCOSS conducted a new round of consultations with more than 50 member organisations across Victoria, including Warrnambool, Bendigo, Ballarat, Morwell, Shepparton and Melbourne. These consultations confirmed the significant problems community organisations experience in relation to the 2012-15 Service Agreement.

The following is a summary of these problems and the proposed solutions that have been put to, but as yet not adopted by, the Department of Health and Human Services and the Department of Education and Training in the draft 2015-18 Funding and Service Agreement.

2015-18 Funding and Service Agreement: Priority areas for improvement

Records

The 2012-15 Service Agreement gives ownership of an organisation's records to the funding department.

This is an unnecessary and inappropriate burden on independent community sector organisations, which are independently regulated and governed and should not be required to divest records to another agency. It is inappropriate for the government to own independent community service organisations' service and client records (apart from those kept for statutory clients, such as children in out-of-home care).

Divesting ownership of client records also interrupts organisations' engagement and relationships with vulnerable service users, as clients should be informed their records are owned by the government. Many people have multiple barriers to accessing a service and need intensive engagement. Informing them their records are owned by the government disrupts this engagement process and can jeopardise trust. For this reason, many organisations have not been informing their clients about the ownership of records.

Community organisations are also concerned about their clients' privacy once records are handed over to other agencies. Client records may include information regarding a number of funded programs from multiple departments (state and federal) as well as non-government funded programs. A community organisation providing a client's records to the funding department may breach that client's right to privacy. However, avoiding this by maintaining several files for a single client may impede an organisation's ability to provide comprehensive services from multiple funding sources.

Community organisations may have legal or professional responsibilities to their clients that contradict the department's claim on record ownership. Organisations providing services under the Social Housing Advocacy and Support Program have highlighted that the department is the "landlord, the supplier of the client, and the owner of client records", which may impede a client's ability to achieve fair representation in eviction proceedings.

Community organisations seek client consent before transferring records to the department or a third party. Community organisations have been retaining copies of client records even when files are transferred because they are aware that they may called to testify in future legal proceedings or inquiries (e.g. Royal Commission into Institutional Child Abuse) which is in breach of the current agreement.

Proposed solutions for the 2015-18 Funding and Service Agreement:

- Define 'client', 'service' and 'other' records
- The department to own the client records of 'statutory clients' (i.e. children in out-of-home care). All other records to be owned by the organisation.
- In order to maintain service continuity when departments want to transition clients from one organisation to another, consent from current clients is obtained at that time, rather than the department needing to own the records.

Notice periods

There is a lack of procedural fairness around the notice that funding departments are required to give organisations with regard to various policy and operational aspects, within the 2012-15 Service Agreement.

Community organisations are required to adopt changes in departmental policy or clauses of the services agreement, but departments are not required to inform them of these changes in a fair and timely manner. Community organisations are instead expected to adopt changes as soon as notified. Notification is usually by email with a link to a website. This has resulted in organisations not adopting the new requirements and potentially being in breach of the 2012-15 Service Agreement.

Other clauses within the agreement allow the department to request records or other information to be provided 'immediately'. The department is also able to demand an organisation suspend or cease activities 'immediately'. In practice, it is often impractical or impossible to meet these requests 'immediately'. Again notification is often is often via email, which may not be read for some time. Organisations have commitments to staff that other laws and regulations cover and without adequate notice periods, they are unable to meet these obligations, for example inadequate notice of funding ceasing.

Proposed solutions for the 2015-18 Funding and Service Agreement:

- Removal of the word 'immediately' in numerous clauses in 2015-18 draft agreement.
- Addition of adequate notice requirements in numerous clauses.

- Alternatively provide a schedule to the agreement that covers notice period obligations of organisations and funding departments in relation to the agreement, rather than having notice periods, or lack thereof, included in each clause.

Dispute resolution

There is a lack of procedural fairness in the dispute resolution clause in the 2012-15 Service Agreement. While relations between organisations and departments are usually positive and professional, differences do arise from time to time. These are usually settled without using the formal dispute resolution procedure in the agreement. However, it is more difficult to resolve disputes as the department has reduced its staffing levels in the regional offices. In addition, where differences are not settled to the satisfaction of the community organisation, the dispute resolution procedures have not often been used because there is concern there will not be a fair process, as the final decision rests with the department they are in dispute with.

Proposed solution for the 2015-18 Funding and Service Agreement:

- Inclusion of a fairer dispute resolution procedure including an independent final arbiter

Variations

Currently the funding department can to vary the conditions in the Service Agreement without the written consent of the organisation. This can include things like operational targets, reporting requirements, changes in policy that impact on the organisation. Again, email notification of a variation with a link to the Funded Agency Channel website is used, but this may not be read in a timely manner or may go astray and not be received or read by the appropriate person at the organisation. It can also be difficult to find the variation on the Funded Agency Channel.

Proposed solution for the 2015-18 Funding and Service Agreement

- Require written consent from the organisation to any variation
- Remove the deeming process, where organisations are deemed to have accepted the variation even if they have not approved the variation.
- Improve the communication processes (e.g. through the Funded Agency Channel) that explicitly notify organisations (with the appropriate notice period) when there are changes in policies or procedures that may impact on the organisation.

Cessation, suspension and termination

The 2012-15 Service Agreement gives the funding department the right to unilaterally suspend, cease or terminate the agreement across a number of clauses. These clauses are extremely complex and inconsistently drafted. For example, a change in government policy can lead to termination of an agreement without compensation or even adequate notice.

The current agreement enables funding departments to exercise significant discretion, through the inclusion of terms such as ‘in the Department’s reasonable opinion’, ‘to the Department’s reasonable satisfaction’, ‘expected community standards’ or ‘ethical standards’. Organisations report that the open-ended nature of these clauses has been used to intimidate them into accepting variations in targets and the like.

Proposed solution for the 2015-18 Funding and Service Agreement:

- Introduce fairer and clearer clauses on cessation, suspension and termination.

Intellectual property

The 2012-15 Service Agreement gives funding departments unrestricted license to use an organisation's background and current intellectual property. Intellectual property is increasingly seen as an asset for community organisations in a competitive environment. While many community organisations are willing to share this asset, they wish to do so on their own terms.

There are numerous examples of departments using background intellectual property in its tendering processes and the creator of that intellectual property has not won the tender.

During the transition to the National Disability Insurance Scheme, the Department of Health and Human Services is both a competitor and funder of community organisations. Special intellectual property clauses may be required for community organisations funded to provide disability services.

Proposed solution for the 2015-18 Funding and Service Agreement:

- Adopt the proposal as submitted by VCOSS and SAWG members that maintains community organisations' ownership of their intellectual property and grants the funding department a license to the full benefit of the services provided.
- In the transition to the NDIS, where the funding department is a competitor with, as well as a funder of, disability organisations, special clauses regarding intellectual property may be needed.

Changing the Service Agreement Information Kit and policies

The funding departments can unilaterally change the Service Agreement Information Kit and departmental policies. The kit is designed to provide funded organisations with information about interpreting the service agreement. However, it can be changed at any time, such as information on applicable departmental policies organisations need to comply with. There is uncertainty of the legal status of the Service Agreement Information Kit.

Organisations struggle to remain up-to-date with changes to government policies they must implement. Funding departments are inconsistent in informing organisations about changes to policies and it is often very difficult to find prescribed changes on relevant websites. Significant changes in policy impacting on organisations should require a period of consultation.

Proposed solution for the 2015-18 Funding and Service Agreement

- Clarify the status of the Service Agreement Information Kit and require adequate notice periods for changes in relevant policies.

APPENDIX 1 - FAIRER INDEXATION FOR THE COMMUNITY SECTOR: BACKGROUND ANALYSIS

What does fair indexation achieve?

A fair system of indexation for the community sector reflects real service delivery cost increases and allows community organisations to invest for the future, sustain their workforces at the legal minimum wage, and maintain their capabilities to innovate, collaborate and maintain the high standards required for delivering government-funded services. Without fair indexation, organisations can adopt a 'siege mentality', scrimping on staff development and asset investment that could yield real productivity gains, and avoiding innovation that produces better services with greater impact.

An indexation model that keeps pace with real costs means community organisations can plan for the future with certainty, rather than arbitrarily engaging in last minute cost-cutting in the face of unexpected price and wage rises, which wastes time and distracts managers from focusing on the needs of the people they help.

Community sector organisations wish to establish and maintain a relationship with government that is professional, efficient and sustainable. A solid financial footing is the foundation of this relationship, because organisations can then focus on working with funding agencies to achieve real results, rather than being diverted to managing declining revenues.

In summary, establishing a fair indexation formula means the Victorian government will help deliver:

- Community organisations that are focused on delivering the best ways of helping people who receive funded services, rather than scrambling to find staff and service cuts
- Services for the people who need them that are effectively and efficiently managed through a sustainable, long-term investment approach, rather than with a short-term cost-cutting focus
- Community organisations capable of collaborating with government and each other to maintain and implement quality standards and build a more cohesive sector, rather than focusing inward on revenue problems
- Services with the financial stability required to innovate, and be in a position to explore opportunities to innovate, experiment and evaluate their services.

Indexation: Facts and myths

Fact: Community services have been cut over the last three years
VCOSS calculates that community services have sustained a 2.63 per cent cut in real funding during the 2012-15 funding period, due to inadequate indexation (including a failure to fully fund superannuation increases – see Table 1).

Fact: Equal Remuneration Order funding does not cover all statutory wage rises
The Equal Remuneration Order (ERO) applies on top of increases determined by the National Minimum Wage Order (NMWO), meaning community organisations must pay the NMWO in July, and then the ERO in December. Occasionally, people believe that funding to fulfil the ERO covers all wage rises that community organisations are legally required to pay. This is not the case.

Fact: Rising wage costs are legal obligations for community organisations
Most community organisations pay at or near the award rate for their staff. Organisations rarely have the option of reducing staff wage rises in response to inadequate indexation, as award wage increases are set by Fair Work Australia through the NMWO and the ERO. As the ERO wage increases escalate, there will be very few community organisations able to offer above award wages.

Myth: Below cost indexation forces efficiency savings through productivity increases
The opportunity for productivity increases to offset the real decline in funding is severely limited by the labour intensive nature of the work being done in the community sector. There is no way of substituting or reducing staff costs without reducing services. VCOSS consultations have revealed that with regards to sustainable management practices, organisations are now focused only on minimising costs, and can no longer afford the upfront investment required for real productivity improvements through program innovation, system improvements and asset replacement. Real funding cuts make productivity worse, not better.

Myth: Community organisations have excessive overheads
Community organisations often under-invest in administrative areas in the face of inadequate funding, running out-of-date software and IT, renting low-quality service delivery sites, and hiring too few administrative staff to effectively manage their organisation.

Myth: Community services can absorb funding cuts while maintaining services
VCOSS consultations with our members show that organisations have had to cut programs, reduce their organisational capacity, shrink overall staffing levels and 'top-up' funded programs with self-generated resources due to inadequate indexation, affecting their ability to help people. Inadequate indexation forces community service organisations to reduce quality monitoring and compliance functions, staff training and development, and management oversight and accountability. This increases the risk of service quality being compromised, and of people not receiving the support they need.

Counting the cost of unfair indexation

Inadequate indexation over the 2012-15 funding and service agreement period means community organisations have suffered a real funding cut of more than 2.6 per cent over three years. The cost impact of this has grown each year.

Table 1: The cost impact of inadequate indexation for 2012-15

	2012-13	2013-14	2014-15	Total: 2012-15
Wage component[1]	2.90%	2.60%	3.00%	8.50%
Superannuation[2]	0.00%	0.25%	0.25%	0.50%
Non-wage component[3]	2.20%	3.20%	1.75%	7.15%
Weighted total (80:20)[4]	2.76%	2.92%	2.95%	8.63%
Indexation provided	2.00%	2.00%	2.00%	6.00%
Cost Impact	0.76%	0.92%	0.95%	**-2.63%**

[1] Increase determined in the National Minimum Wage Order.
[2] Legislated increases in the superannuation guarantee.
[3] Melbourne All Groups Consumer Price Index for 2012-2014, 2014 Victorian Budget Update for 2014-15 estimate.
[4] Wages and superannuation components are weighted at 80%, non-wage component 20%.

While the Victorian government has funded the Equal Remuneration Order (ERO) wage increases component until June 2015, these have not included the cost of increases determined by the National Minimum Wage Order (NMWO). Community organisations are obliged to pay both.

Before the 2012-15 funding period, circumstances that forced community organisations to incur one-off cost increases, such as the 2012 increase in the superannuation guarantee, would have triggered the 'exceptional circumstances' clause of the relevant funding and service agreement, and additional funds been provided to cover the shortfall. While the community sector attempted to trigger the 'exceptional circumstances' clause of the 2012-15 Funding and Services Agreement to cover the cost increases resulting from the 2012 increase in the superannuation guarantee (which increased superannuation payment obligations for organisations in 2013 and 2014), the Victorian government refused to fund these.

The 2 per cent annual indexation formula for the 2012-15 funding and service agreement period did not cover the increases in non-wage costs.

Why inadequate indexation does not improve productivity

Inadequate indexation reduces the productivity and effectiveness of the services delivered by community organisations. It does not create productivity savings; it pushes organisations into 'survival mode', where they focus on short-term cost cutting rather than long-term investment, quality improvement and innovation. It distracts management from their core business and is inimical to long-term service planning. Organisations are forced to withdraw self-funded services and to top-up under-funded government programs. As a result, people in need of support from community services may receive more fragmented and poorer quality support.

Community organisations' greatest expenditure is on their workforces, and any reduction in real funding levels inevitably means job losses. Staff cuts mean the workforce concentrates almost solely on meeting the immediate numerical output targets set for it, and has less time for service innovation and planning, quality assurance, collaboration, and training and development. This erodes the level of professionalism and service delivery within community organisations, and means staff are less aware of, or able to respond to opportunities to work with other organisations and provide a seamless service offering. Services become increasingly disjointed and duplicated as organisations become more disconnected from the activities of others around them.

Ultimately, this means organisations are less able to effectively help people overcome the disadvantage they experience, which results in more people experiencing poverty and social issues for longer, with greater negative effect.

Paradoxically, rather than improve productivity, below par increases in indexation lead to productivity falls. VCOSS has previously commissioned research demonstrating the difficulties of productivity improvement in community services.[4] This research found the community sector has already made significant productivity gains, and that achieving further gains would be difficult because of the labour-intensive, people-oriented nature of its services.

VCOSS has also consulted our member organisations on how they respond to inadequate indexation. Most commonly, organisations report that they focus on covering immediate and short-term costs, at the expense of long-term innovation, quality assurance and infrastructure investment, or redirect revenue from self-funded community programs to 'top-up' underfunded government agreements. None reported that they were able to find more cost-effective ways to deliver services, as this requires time, resources and upfront investment.

Community organisations often generate revenue from fundraising and social enterprise sources that allow them to fill gaps in their suite of services, undertake community development activities in the communities they serve, and invest in their capability and capacity. Organisations report that they have had to curtail these activities in the face of budgetary pressures, which undermines the trust they build with communities, creates gaps in their ability to offer wrap-around person-centred services for individuals, and means they have less ability to pursue innovative service delivery models with the potential to provide better help for people more cost effectively.

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[4] Allen Consulting Group, *How many wheelchairs can you push at once?— Productivity in the community service organisation sector in Victoria*, Report to the Victorian Council of Social Service, December 2008.

Organisations also look to trim their greatest expenditure item: staff. Because organisations strive to meet their obligations in agreements with governments, the focus of staff cuts is often in organisational capacity – cutting staff who monitor and improve service quality, undertake service development, innovation and evaluation, or develop workforce capabilities and make sure training and collaboration take place. By reducing these staff, and focusing frontline workers solely on meeting funding obligations, organisations lose the capacity to innovate, collaborate and adapt to a changing regulatory environment and their ability to respond to the changing needs of government, people and communities. At the same time, governments and communities have rising expectations that services will increase their ability to undertake these same tasks. Real funding reductions mean organisations enter 'survival mode', where simply maintaining operations becomes the overriding focus, and strategic development and investment disappears from view.

Inadequate indexation means organisations take to 'sweating assets': only spending the minimum on building and maintenance, delaying replacement of ageing plant and equipment, or maintaining outdated IT and administrative systems, when investing in improved technology would deliver greater efficiency from a long-term perspective. Over time, this makes many community organisations less productive, as they make do with outdated equipment and technology, as well as being less able to produce useful data and information on their work and be accountable to funding bodies. Community organisations have difficulty in attracting capital and only occasionally hold debt, so long-term investment must generally be financed from cash reserves. Significant numbers of organisations have been running deficit budgets for several years, which has reduced the funds available for investment, and made them more financially fragile.

Inadequate indexation adds to other financial pressures

Inadequate levels of indexation are not the only financial pressure that community organisations have experienced in recent years. There has been a significant level of change in the sector, a range of escalating costs and fewer funding or revenue opportunities across the board. Real funding cuts through inadequate indexation add to an already difficult operating environment.

Some of the factors organisations face in their operating environment include:

- Significant re-tendering processes at both state and federal levels, causing large-scale disruptions to service delivery, and often imposing unfunded costs on organisations for tendering, service re-design, and winding down of de-funded services, including client transition processes and staff redundancies
- Increasing levels of red-tape, especially for newly imposed quality assurance processes such as record-keeping, complaints management, service audits and inspections, and additional reporting requirements
- Increasing 'hand-back' calls for underspent funds by agencies; while overspends are increasingly questioned and refused funding, especially in flexible funding models
- High growth in worker's compensation premiums in some service delivery areas
- Additional energy required to pursue unpaid invoices by government and other creditors, especially for small-scale and flexible funding models, meaning increased administrative intensity for little revenue
- Additional public holidays resulting in additional costs, especially for 24-hour services
- While the direct impact of the ERO has been provided for government-funded services up until end-June 2015, organisations have needed to find revenue for wage increases in self-

funded or philanthropic funded programs, as well as the indirect effects of the ERO, such as changing wage relativities for management and administrative staff, such that without wage increases, managers could be paid less than the staff they supervise.

Alternative revenue sources are also becoming increasingly difficult to secure for reasons including the following:

- At both the state and federal levels, there have been far fewer grants programs, which in the past often provided small amounts of funding for short-term projects or equipment
- Organisations receiving local government funding are planning for possible cuts due to the introduction of rates-capping
- Low interest rates have reduced returns on organisations' investment returns, as well as the returns of philanthropic institutions that provide funding to organisations
- A sluggish economic environment with rising unemployment has affected donations and the ability of organisations to secure revenue targets through fundraising activities
- Organisations receiving federal funding have similarly experienced funding clawbacks through inadequate indexation allocations.