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**Using Private Contracts
to Create Adoptions from Foster Care**

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Mary Eschelbach Hansen **

Abstract

Creating adoptions for children waiting in foster care is a good investment, but the number of adoptions created each year meets only a fraction of the need. This paper explores how the organization of the delivery of social services to waiting children and prospective adoptive families influences adoption creation. Cross-section time-series estimates are supplemented with a new augmented fixed effects procedure to demonstrate that the use of contracts with private agencies bolsters adoption creation. Contracts for recruitment and orientation of prospective adoptive parents are particularly effective.

Key words: adoption, child welfare, fixed effects vector decomposition, foster care, privatization

JEL classification: D61, J13, J18

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Using Private Contracts to Create Adoptions from Foster Care

More than a half million children are currently in foster care in the United States (US DHHS 2006a). While most of the children will return to their families of origin, over 100,000 will never be able to return home. About half of these “waiting” children will be adopted in any given year; the other 50,000 children will continue to wait for a safe and permanent family.

Federal law, particularly the Adoption and Safe Families Act (ASFA) P.L. 105-89, reauthorized by P.L. 108-145), holds adoption to be the preferred alternative for providing a permanent family for most children who cannot be reunited with their families of origin. Adoption improves physical, psychological, and behavioral health—as well as related educational and employment outcomes—relative to the alternative of long-term foster care (see recent reviews by Rushton 2004; Triseliotis 2002, van Ijzendoorn 2006, and Hansen 2006a).

Although local and state child welfare agencies are responsible for the placements of the children in their care, Congress has actively promoted adoption since the late 1970s. Between 1980 and 1996, federal adoption promotion focused on the provision of tax and subsidy incentives directed towards adoptive parents. ASFA created the Adoption Incentive Program, one of many outcome-oriented, federally-administered programs instituted under the Clinton administration. The Adoption Incentive Program consists of monetary bonuses to state child welfare agencies for increases in adoptions, and it imposes financial penalties on states that keep children in foster care for long periods of time. States responded to federal incentives to create adoptions by increasing the post-adoption financial supports offered, in turn, to families (Hansen 2006b). Prospective adoptive families appear to be sensitive to post-adoption supports (Hansen and Hansen 2006), so that the combination of incentives to states and incentives to families doubled adoptions from foster

care in the late 1990s; see figure 1. However, the number of adoptions created for children waiting in foster care has leveled off at about 50,000 for the last several fiscal years.

Adoption creation could be stymied by a shortage of available adoptive families, yet surveys indicate that interest in adoption is strong and that a sizeable number of adults who express interest in adoption consider adopting children who wait in foster care (Chandra et al 1999, Harris Interactive 2002). In the past few years states have tried to cut back on post-adoption financial support (Eckolm 2005; NACAC 2003). The decisions of prospective adoptive families is sensitive to the willingness of the state to secure post-adoption funds to protect the family against financial risk associated with agreeing to raise a child with significant special needs (Hansen and Hansen 2006); therefore, cutting adoption subsidies may cut adoption creation.

Define adoption creation as the number of adoptions created in a fiscal year relative to the number of waiting children at the end of the previous fiscal year. The rate of adoption creation was high in the late 1990s and early 2000s, as shown in table 1. This has been attributed to states' efforts to clear a backlog of cases (Hansen 2006c). A large increase in the percentage of adoptions completed by kin and foster parents indicates many long-term placements were converted into adoptions (US DHHS 2006a, Hansen 2006d).

In recent fiscal years, adoption creation has fallen along with adoptions in aggregate. That is, the slowdown in adoptions is not accounted for by a decline in waiting children. This paper explores how the organization of the delivery of social services to waiting children influences adoption creation. Specifically, I find that the use of contracts with private agencies increases adoption creation.

Using Contracts for Public Services

Private contracting, especially for municipal services, was widespread and growing as the twentieth century ended (Florestano and Gordon 1980, Pool and Fixler 1987). There is a large literature on the appropriate use of private contracts in the provision of public services (Lipsky and Smith 1989), and perhaps an even larger literature exists on measuring the outcomes of private contracting (Fernandez and Fabricant 2000). The quality of services provided through private contracts likely depends on the way bids are solicited and contracts are written (Hart et al 1997, Shetterly 2000), but most studies show that private contracting for municipal services such as garbage collection is cheaper than direct government provision of services (e.g. McDavid 1985), although private contracts are not preferred by all stakeholders (Dilger et al 1997).

The results of studies of the outcomes of private contracts in public health and mental health are mixed. While there may be a cost savings (e.g. Schlesinger et al 1986, Clark et al 1994), William Shonick and Ruth Roemer (1982) and George Avery (2000) note that positive outcomes of privatization of hospitals may depend on the size of the market. The decision to pursue private contracts may not be made solely on the basis of a cost/benefit analysis; it appears that administrators' ideology influences the decision (Keane et al 2001).

In the aftermath of litigation over lapses in the public provision of child welfare services, many state and local jurisdictions privatized all or part of their child protective and child welfare services (Nightingale and Pindus 1997, Kinnevy 2002). Cooperation between private and public agencies remain "complex, involving differences among public and private cultures, the blending of formal and informal services, and conflicting strategies with regard to client services" (Kinnevy 2002: 53; see also: Blank 2000, Van Slyke 2003, Zullo 2006).

In case studies, the use of private contracts seems to be related to efficient delivery of adoption services. Erwin Blackstone, Andrew Buck, and Simon Hakim (2004) argue that private

administration of adoption services improved efficiency and may have reduced cost in Kansas, Michigan, and Illinois. Thelma Smith-McKeever and Ruth McRoy (2005) show that 70 percent of African American families served by private agencies had previously, and unsuccessfully, attempted to adopt through a public agency. Many post-adoption services are also provided by private agencies (Mack 2006), although there is little evidence to date regarding the success of private versus public provision in this area.

Organizational Barriers to Adoption Creation

Whether private or public, the successful provider of adoption services must overcome three organizational problems: the problem of many tasks, the problem of hierarchical structure, and the problem of multiple principals.

The Problem of Many Tasks

State legislatures delegate a wide range of responsibilities to child welfare agencies. They must respond to reports of child abuse and neglect, they must place children on an emergency basis, they must find and train families who are willing to serve as foster parents, they must work with families of origin, they must create adoptions. When the responsibility for many tasks is delegated by a principal to an agent, the effectiveness of an incentive depends upon whether the tasks are complements or substitutes in the cost function of the agent. A simple example following Holstrom and Milgrom (1999) and using a quadric formulation of the costs incurred by the agency is useful for understanding the problem of many tasks in child welfare service. Assume there are two tasks: emergency placement (e) and adoptive placement (a). The agency's costs are

$$C(e, a) = e^2 + 2\lambda ea + a^2$$

where $-1 < \lambda < 1$. If $\lambda < 0$, then emergency and adoptive placements are complements in cost; it costs less to do both tasks than to do only one. If $\lambda > 0$, the tasks are substitutes; it costs more to do both tasks together than to do them separately.

The Adoption Incentive Program, which again is the federal incentive to states to create adoptions, should have its greatest effect when the agency groups together tasks that are complementary in costs to adoption tasks, and keeps tasks that are substitutes in cost separate from the provision of adoption services. Agencies can use a system of specialists to separate the tasks. Alternatively, contracting for specific services with private agencies solves the problem of multiple tasks by creating a one-to-one correspondence between agents and tasks, effectively rendering emergency and adoptive placements substitutes in cost.

The Problem of Hierarchical Structure

The Adoption Incentive Program creates a bonus system for states, but states must find ways to induce cooperation from local jurisdictions to claim federal bonuses. Individual local child welfare agencies and front-line social workers may consider free-riding on other jurisdictions and other social workers viable. A similar phenomenon is observed in the administration of asylum applications in Europe (Holzer, Schneider, and Widmer 2000). Contracting for private services creates a transparent monitoring mechanism that solves the problem of hierarchical structure.

The Problem of Multiple Principals

The front-line social worker may see adoption as a problem of multiple principals, each trying to influence the aspects tasks he values most. For example: Congress and the Department of Health and Human Services (DHHS) want more finalized adoptions; the local supervisor wants to avoid any negative publicity; the association of social workers to which she belongs emphasizes race-sensitive placement; families want speedy placements. Each principal rewards the tasks that he values and, at best, offers no reward for completion of tasks that he does not value. If, again, the

tasks are complements in the cost function of the agent, then the effects of incentives offered by different principals are unproblematic. If the tasks are substitutes in the cost function, however, there is substantial weakening of the effect of incentives. Returning to the quadratic formulation of cost above, the optimal incentive is now inversely related both to λ and to the number of principals, n (Bernheim and Whinston 1986, Dixit 1997, Holstrom and Milgrom 1999). This implies that a given level of incentive will be more effective in organizations in which social workers have contact with a smaller number of principals. Again, private contracting for delivery of specific services can solve the problem.

As discussed above, existing evidence about the outcomes of private contracts for child welfare services is based upon case study. This is because consistent, national data on adoptions did not exist before 1995. Further, only recently have surveys of state child welfare administrators provided information on the types of private contracts that states use.

Data and Methods

Adoption Incentive program created by ASEFA provided an incentive for data collection. To qualify for incentive payments, states had to document increases in adoptions. Effectively states were required to come into compliance with a federal rule issued in December 1993 requiring the submission of data on adoptions with state agency involvement. The data collection system is known as the Adoption and Foster Care Analysis and Reporting System (AFCARS). Prior to implementation of AFCARS, only voluntary systems existed for collection of child welfare data. States are now required to submit information about all children in foster care and information about children whose adoptions were finalized after any state agency involvement. The public agency may have placed the child for adoption, or it may have contracted with a private agency to achieve adoptive placement. In a few cases, public agency involvement may be limited to processing

claims for Title IV-E funds only. States are encouraged, but not required, to submit data for all other adoptions including adoptions through tribal agencies, private agencies, and independent adoptions. Here attention is limited to the cases with state agency involvement that are reported in AFCARS. The Children's Bureau publishes tabulations on the Web (US DHHS 2006a, for example) and in an annual outcomes report.

Table 1, again, shows the decline in adoption creation evident in the AFCARS data from 2000 to 2004. The number of waiting children in the average state fell from 2,632 in fiscal year 1999 to 2,282 in 2004. In 2000, states created adoptions for 61 percent of children who were waiting at the end of fiscal year 1999. In 2001, states created adoptions for 72 percent of children waiting at the end of 2000. But in fiscal years 2002 through 2004, states created adoptions for less than half of waiting children.

Data on Adoption Service Contracting

A 2002 survey of state adoption administrators sponsored by the Packard Foundation provides detail about the adoption services contracted out by the states (Wilson et al 2005). The survey asked states to identify the extent of private contracts in eight service areas: recruitment of foster and adoptive parents, orientation of foster and adoptive parents, processing of applications to foster or adopt, completion of the homestudy for prospective adoptive parents, training of foster and adoptive parents, matching prospective adoptive parents with waiting children, facilitating placement of children into families, and provision of post-placement services such as counseling. Forty states responded to the survey, but not all states were able to provide information about all of the types of contracts.

The data from the survey were merged with AFCARS administrative data. The variation in the state average of adoption creation by the extent of contracting is shown in table 2. The average number of adoptions created was higher when contracting was used in the provision of recruitment,

orientation, application, homestudy, and training and post-placement services. The greatest difference is between states with no private contracts and states with at least some contracts; a dummy variable indicting the use of contracts will be used in the next section to measure contracting.

Only modest correlations ($\rho < .3$) exist between the use of contracts for one type of services and most other types of services. The greatest correlation was between contracts for recruiting and orientation and matching and placement services. Contracts for these services were combined in the creation of the dummy variables.

Other influences on adoption creation include total resources available for adoption assistance subsidies to families and the total budget for administration of adoption. The Urban Institute’s survey of child welfare administrators for 2000 and 2002 provide information about state spending on adoption assistance subsidies (Scarcella et al 2004). Forty nine states and the District of Columbia responded to the 2002 survey.

Estimation Strategy

Consider first the pooled cross-section time series model of the form

$$A_{it} = \alpha + C_i\beta + X_{it}\Phi + \omega_t + \varepsilon_{it},$$

where A_{it} is adoption creation in state i in year t . The parameters to be estimated are α, β and Φ . The final two terms are the year-specific, and “usual” residuals. Elements of X_{it} are control variables. Controls include adoption subsidy expenditures, adoption administration expenditures, and the federal medical assistant percentage, which controls for relative economic position of the state. Elements of C_i describe organizational structure in state child welfare agencies, here described by the use of private contracts.

Such a parsimonious model is likely to suffer from omitted variable bias; it is desirable to use a fixed effects framework to obtain unbiased estimates. However, the existence of private

contracting is measured at only one point in time, and must be assumed not to have changed over the relatively brief time period studied here. Because the measure of contracting does not vary over time its effect cannot be disentangled from the state effect in the usual fixed effect framework.

An augmented panel regression procedure called *fixed-effect vector decomposition* solves this problem (Pluempfer and Troeger 2007).¹ The model is

$$A_{it} = \alpha + X_{it}\varphi + C_i\gamma + v_i + \omega_t + u_{it},$$

which is the same as a usual fixed effects model, with the addition of a term including the vector of the dummies indicating the existence of contracting, C_i . The state-specific fixed effect v_i is assumed to be correlated with at least one element of X and one of C .

Fixed effect vector decomposition is a three-stage estimation procedure. The first stage estimates the usual fixed effects model. The within-estimator identifies the state effect as the part of the mean of the state adoption creation rate that cannot be explained by the time-varying variables:

$$\hat{v}_i = \bar{a}_i - \bar{x}_i\varphi.$$

The second stage of the procedure estimates (by OLS) the effect of the time-invariant c -variables on the fixed effects,

$$\hat{v}_i = \phi + c_i\gamma + v_i,$$

where ϕ is a constant term and v_i is an error term. This stage brings to mind an Oaxaca decomposition of differences in wage rates into the part that can be explained by differences in independent variables and the part that cannot be explained. In the third stage, the results from the second stage estimation are included in a pooled OLS re-estimation of the model, so that

$$a_{it} = \alpha + x_{it}\varphi + c_i\gamma + v_i + u_{it}.$$

The inclusion of v_i in the final stage accounts for the part of the original state effect that is due to

¹ Random effects with the Hausman-Taylor (1981) procedure yields same-signed results, but the magnitudes of the coefficients are sensitive to specification. Further, the state effect is unlikely to be the outcome of a random process.

still-omitted variables. The coefficient on ν_i is expected to equal one after correction for heteroscedasticity or serial correlation. Note that the choice to use private contracts is assumed to be orthogonal to the unexplained unit effects. If this assumption does not hold, then some omitted variable bias remains. It is thus nearly always the case that “researchers face a choice between using as much information as possible and using an unbiased estimator” (Pluemper and Troeger 2007: 129). Thomas Pluemper and Vera Troeger use Monte Carlo simulations to show that fixed effect vector decomposition has nicer finite sample properties than alternatives already discussed for estimating the effect of time-invariant variables using panel data.

Explaining Adoption Creation

Table 3 shows the pooled cross-section time series results (columns 1 and 2) alongside the results of the fixed effect vector decomposition (column 3). A log-log specification allows coefficients to be interpreted as elasticities. The existence of private contracting alone explains 19 percent of the variation in adoption creation in the states from 2000 to 2004. Using private contracts to provide orientation and recruiting appear to be especially effective ways to bolster adoption creation. Private contracts in these two areas nearly double adoption creation even in the simple cross-section time-series regression in the first column of table 3. Training contracts increase adoption creation by nearly as much, but without controls for the federal matching rate, the size of subsidy payments, and the size of administrative costs, the effect of training contracts is not statistically significant.

Controlling for expenditures on adoption assistance subsidies and adoption administration, as well as for economic conditions in the state as captured by the federal medical assistance percentage, boosts the explanatory power of the model even as it reduces the number of

observations by limiting the study to the years 2000 and 2002.² Orientation, recruiting, and training have large and statistically significant positive effects on adoption creation. In the specification in column 2 of table 3, using orientation and recruiting contracts increases adoption creation by nearly 180 percent; using training contracts increases adoption creation by 145 percent.

The signs on the controls are as expected and are generally consistent with previously published studies (Hansen and Hansen 2006): poorer states have higher federal medical assistance percentages and lower rates adoption creation. States that support adoptive families more generously with adoption assistance payments create more adoptions (Avery & Mont 1992). Overall spending on the administration of adoption does not predict adoption creation.

After correcting for omitted variable bias through the fixed effect vector decomposition procedure, all of the types of contracts have statistically significant effects on adoption creation. Orientation and recruiting contracts remain the most effective method of boosting adoption creation: using these contracts increases adoption creation 245%. Using training contracts increases adoption creation 86 percent. Using contracts to complete application and homestudy tasks both increase adoption creation by about 40 percent. Returning to table 1, these results indicate that the average state could have achieved a greater rate of adoption creation in 2003 than it did in 2000 by using private contracts in these areas.

In all three specifications, matching or placement contracts are negatively associated with adoption creation. More detailed investigation is beyond the scope of this paper, but likely represents negative selection. For example, states that use private contracting for matching and placement may have larger populations of harder-to-place children.

² States dropped do not differ in a statistically significant way from states retained in the estimation

Conclusion

Creating adoptions for waiting children has a significant payoff for states. An adoption from foster care costs state and federal government about \$115,000, but saves the government about \$258,000 in child welfare and human service costs, netting a savings of \$143,000 (Barth et al 2006, adjusted for inflation to 2000 dollars). Mary Hansen (2006a) estimates that each adoption of a waiting child nets between \$88,000 and \$150,000 in private benefits and \$190,000 to \$235,000 in total public benefits (in constant 2000 dollars). That is, each dollar spent on the adoption of a child from foster care yields between 2 and 3 dollars in benefits to society.

Of course, the benefits of adoption are realized later, while the expenditures are made today. Federal adoption expenditures grew from less than \$400,000 in fiscal year 1981 to \$1.3 billion in fiscal year 2002 (Dalberth et al 2005). State expenditures have grown nearly as much. Since 2000, fiscal stress has led several states to attempt to cut post-adoption spending (North American Council on Adoptable Children [NACAC], 2003; Eckholm, 2005). Some of the cuts have been blocked by the courts, which have made it clear that adoptive parents have legal standing to protect their children's entitlements (*E.C. v. Blunt* (05-0726-CV-W-SOW) and *A.S.W. v. Oregon* (also known as *A.S.W. v. Mink*, 424 F. 3d 970 (9th Cir. 2005)). These decisions effectively require states and the federal government to consider other ways to cut the cost of providing permanent families for waiting children. This paper shows that states that may reduce the administrative cost of creating adoptions through the judicious use of private contracts.

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Table 1. Adoption Creation in the Average State

	Waiting Children	Adoptions _t / Waiting _{t,t} (%)
1999	2,632	
2000	2,576	61
2001	2,552	72
2002	2,406	49
2003	2,301	44
2004	2,282	47

Source: Author's calculations from US DHHS (2006a).

Table 2. Adoptions Created by Contract Amount

	No	Some	Most	All
	Contracts	Contracts	Contracted	Contracted
Recruitment	23	50	41	52
Standard Dev.	23	54	26	41
No. of States	5	20	3	6
Orientation	10	47	59	54
Standard Dev.	22	54	44	41
No. of States	6	16	5	6
Application	30	48	67	46
Standard Dev.	26	57	47	28
No. of States	10	15	8	2
Homestudy	39	47	48	29
Standard Dev.	26	40	55	16
No. of States	2	11	19	1
Training	35	49	44	52
Standard Dev.	38	55	31	40
No. of States	4	19	5	6
Matching	48	49	38	27
Standard Dev.	43	55	30	4
No. of States	13	17	4	1
Placement	50	47	35	27
Standard Dev.	42	52	28	4

No. of States	13	17	2	1
Post-Placement Services	37	44	53	53
Standard Dev.	32	46	51	48
No. of States	5	15	7	7

Sources: US DHHS (2006), Wilson et al (2005).

Table 3. Determinants of Adoption Creation

	Fixed Effect Vector		
	Cross-Section, Time Series		Decomposition
	(1)	(2)	(3)
FMAP		-0.028	-0.162**
		(0.018)	(0.018)
Ln (Adoption Subsidy Payments)		0.396*	1.050**
		(0.233)	(0.147)
Ln (Adoption Administration Costs)		-0.197	-0.111
		(0.177)	(0.066)
Orientation or Recruiting Contracts	0.977**	1.767**	2.445**
	(0.323)	(0.438)	(0.162)
Application Contracts	0.161	0.094	0.396**
	(0.218)	(0.339)	(0.113)
Homestudy Contracts	0.117	0.097	0.391**
	(0.200)	(0.285)	(0.120)
Training Contracts	0.950	1.454*	0.860**
	(0.449)	(0.811)	(0.309)
Matching or Placement Contracts	-0.244	-0.440	-0.799**
	(0.237)	(0.352)	(0.158)
R2	0.189	0.512	0.902
N	153	53	53

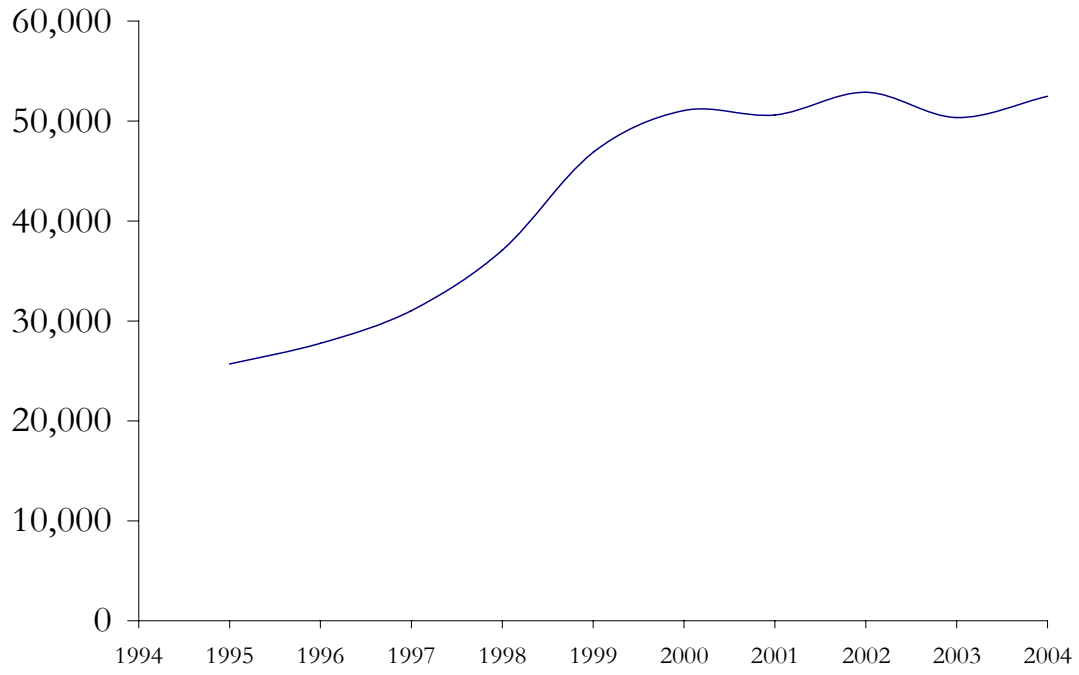
Robust standard errors in (.). ** indicates $p < .05$; * indicates $p < .10$ Constant term and year

effects estimated but not reported.

Sources: Authors calculations from US DHHS (2006a), Scarcella et al (2004)

and Wilson et al (2005).

Figure 1. Adoptions from Foster Care



Source: US DHHS (2006a).