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Child center closures: Does nonprofit status provide a comparative advantage?

Marcus Lam [a,*], Sacha Klein [b,1], Bridget Freisthler [c,2], Robert E. Weiss [d,3]

[a] Columbia University School of Social Work, 1255 Amsterdam Avenue, New York, NY 10027, USA
[b] School of Social Work, Michigan State University, Baker Hall, 655 Auditorium Road, Room 24, East Lansing, MI 48824, USA
[c] UCLA Meyer and Renee Luskin School of Public Affairs, 3250 Public Affairs Building, Los Angeles, CA 90095-1656, USA
[d] UCLA School of Public Health, Department of Biostatistics, Los Angeles, CA 90095-1772, USA

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ABSTRACT

Reliable access to dependable, high quality childcare services is a vital concern for large numbers of American families. The childcare industry consists of private nonprofit, private for-profit, and governmental providers that differ along many dimensions, including quality, clientele served, and organizational stability. Nonprofit providers are theorized to provide higher quality services given comparative tax advantages, higher levels of consumer trust, and management by mission driven entrepreneurs. This study examines the influence of ownership structure, defined as nonprofit, for-profit sole proprietors, for-profit companies, and governmental centers, on organizational instability, defined as childcare center closures. Using a cross sectional data set of 15724 childcare licenses in California for 2007, we model the predicted closures of childcare centers as a function of ownership structure as well as center age and capacity. Findings indicate that for small centers (capacity of 30 or less) nonprofits are more likely to close, but for larger centers (capacity 30+) nonprofits are less likely to close. This suggests that the comparative advantages available for nonprofit organizations may be better utilized by larger centers than by small centers. We consider the implications of our findings for parents, practitioners, and social policy.

1. Introduction

The most recent U.S. Census estimates indicate that almost 7 million (35%) of American children, between the ages of 0 through 4 years, spend some part of their week in a non-relative, formal childcare arrangement; additionally, nearly 4.7 million children (23.3%) are enrolled in an institutional, center-based childcare program such as Head Start programs, preschools, nursery schools, and daycare centers (Laughlin, 2010). This makes childcare centers, also known as day care centers, a vital resource for a large proportion of parents and young children in the United States. During the past several decades, the percentage of mothers of young children employed outside the home has risen dramatically, generating an increasing demand for reliable childcare services (Laughlin, 2010; Sosinsky, Lord, & Zigler, 2007).

An often overlooked measure of center quality is center instability, defined here as closures. Closures of childcare centers can be disruptive for young children as well as for parents (Kershaw, Forer, & Goelman, 2005). For children, center closures severs the “nexus” of relationships that includes the emotional ties to teachers and peer networks important for healthy development; for parents, center closures may create financial burdens if parents have to take time away from work in order to find new childcare providers that may cost more, may be further from their home, or may be of lower quality (Kershaw et al., 2005).

Ownership structure, defined as nonprofit, for-profit, and governmental providers, has emerged as an important predictor of childcare stability and quality (Cleveland & Krashinsky, 2009; Gelles, 2000; Kershaw et al., 2005; Rose-Ackerman, 1986). Nonprofits are legally defined in the IRS tax code as 501c organizations and can range from the traditional 501c(3) public charities created to serve certain segments of the population (i.e., children, elderly, disabled, etc.), 501c(4) organizations that provide a community benefit (i.e., civic associations and volunteer fire departments), or 501c(5) member serving organizations (i.e. labor unions) (Anheier, 2005; Salamon, 2012). Many nonprofits, especially 501c(3) organizations, are given certain tax privileges due to their charitable missions (Anheier, 2005; Weisbrod, 1998). For-profits are traditional businesses that exist for the monetary benefit of its owners or shareholders. They can take on a variety of legal structures such as sole proprietors, partnerships, corporations, or limited liability companies. Lastly, governmental organizations, while also nonprofit, are defined here as government entities funded directly by tax dollars (i.e. public schools, hospitals, etc.). Governmental providers serve a broader range of the population and are distinct from charitable nonprofits which provide services to a specific membership base, population, or community.

* Corresponding author. Tel.: +1 212 851 2378.
E-mail addresses: ml3260@columbia.edu (M. Lam), kleinsa@msu.edu (S. Klein), freisthler@publicaffairs.ucla.edu (B. Freisthler), robweiss@ucla.edu (R.E. Weiss).
[1] Tel.: +1 517 432 3736.
[2] Tel.: +1 310 206 1602.
[3] Tel.: +1 310 206 9626.

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Unlike for-profits and governmental organizations, nonprofits have distinctive qualities that may give them a comparative advantage. These include monetary benefits, such as exemption from income and property taxes, as well as access to a variety of revenue streams, such as donations from individuals, earned income in the form of fees for service, and/or grants from foundations and government agencies. Nonprofit childcare centers also provide more than just day care; they also serve as "resource brokers" that connect parents to one another and to other service providers (Small, 2006). Nonprofit childcare providers are also more likely to be located in low income neighborhoods and thus are a vital resource for these communities (Small & Stark, 2005). In the social and human services fields, government agencies also contract with nonprofits to a greater extent when compared to for-profits (Boris, de Leon, Roeger, & Nikolova, 2010). Nonprofits, therefore, may be privileged to "in-tangible" and non-monetary advantages, such as higher levels of trust, greater support from donors, patrons, or elected officials, and a better reputation within the community (Hansmann, 1996).

Given these general comparative advantages of nonprofits this study addresses the following question: *Are nonprofit childcare centers less likely to close compared to for-profit and governmental childcare centers?* To fully realize these comparative advantages, however, nonprofits require resources that newer and younger organizations may not have. Thus, in addition to ownership structure, this study will also consider the influence of organizational age and capacity on center closures in the childcare industry.

1.1. Childcare industry

The immediate and long-term benefits of childcare extend not just to the child and family but to the larger society (Sosinsky et al., 2007). Thus, public policy promotes the availability of childcare services through both direct provision of childcare by local government agencies and public schools (often with the support of federal funds) as well as private sector provision of childcare services by nonprofit and increasingly, for-profit providers (Riccucci & Meyers, 2008). The 2007 Economic Census estimates that there are 75112 child day care establishments in the United States (NAICS 62441). Of these, 71% (53592) are incorporated as for-profit businesses (of these, 39% are corporations; 25% are individual proprietorships; 7% are partnerships; and 1% are other legal forms of organization), and 29% (21520) are nonprofit and governmental establishments. However, 63.7% of total revenue for nonprofit and governmental day care providers comes from government payers (i.e. Medicaid) while only 36.3% come from private payers. In contrast, for-profit child day care providers receive only 28.6% of their total revenue from government payers and 71.4% of their total revenue from private payers (Bureau of Labor Statistics, U.S. Department of Labor, Quarterly Census of Employment and Wages Website, 2007). This is evidence of market segmentation where nonprofit and governmental centers serve populations receiving government subsidies, like low income families, while the majority of for-profit centers serve higher income families who can afford to pay for services out of pocket. However, the impact of this provider mix, and subsequent market segmentation on service availability, service stability, and social welfare outcomes (such as service quality, equality of access to vulnerable populations, or fidelity to public goals and mandates) remains unclear.

1.2. Nonprofit theory, behavior, and population ecology

Nonprofit theory suggests that differences in organizational behavior, including who organizations serve, stem from two sources: the motivations of entrepreneurs who create the organization and the legal constraints imposed on the organization. Commonly known as the stakeholder theory and trust theory, nonprofits are posited to behave in a more socially responsible and trustworthy manner relative to for-profit providers (Hansmann, 1980, 1996; Rose-Ackerman, 1986). Stakeholder theory (Rose-Ackerman, 1986) suggests that nonprofit entrepreneurs are often guided by ideological values, such as strong religious or political beliefs and/or adherence to a particular treatment or learning modality, and therefore focus organizational activities to further these values. In contrast, for-profit providers are expected to focus more on activities that enhance profit maximization (Steinberg, 2006), while governmental providers are expected to focus on activities that promote equality and service access (Kapur & Weisbrod, 2000).

Rose-Ackerman's (1986) cross sectional study of the child day care industry in the United States finds that nonprofits tend to be managed by altruists or mission driven entrepreneurs and provide high quality services at low prices. However, given that there are only a limited number of altruists relative to demand, there is room for alternative providers such as for-profit centers to enter the market to profit from excess demand at the margins (Rose-Ackerman, 1986). Hence, Rose-Ackerman (1986) concludes that nonprofit entrepreneurs are not pure profit maximizers, but instead strive for "the concrete realization of an ideal" and thus may also have "a clear vision of desirable service provision" (p. 292). Thus, parents may feel assured that nonprofit providers will emphasize certain aspects of care and service quality that they especially value, for example, a church affiliated day care center may promote Christian values. Consequently, those who share the organization's mission and values are more likely to patronize it and may provide additional support with donations of time and money.

Trust Theory (Hansmann, 1980, 1996) also predicts that nonprofit childcare centers are likely to enjoy a competitive advantage over their governmental and for-profit counterparts. According to this theory, nonprofits are less likely to exploit consumers and donors because they are legally constrained from distributing profits to managers or directors for personal gain; thus, they are deemed more "trustworthy" (Hansmann, 1996). This "trust" relationship is especially salient in the childcare field because the purchasers of childcare are not its direct consumers (Gelles, 2000). As Hansmann (1980) notes, "Children typically are not very discriminating consumers, nor even, in many cases, good sources of information about the nature of the services they receive" (p856). Consequently, the purchasers of services (parents) must make their purchasing decision based on "trust" rather than firsthand knowledge that the organization will provide high quality care. A nonprofit ownership structure, therefore, can serve as a signal to parents that the organization is more trustworthy, won't shirk on service quality to save on costs, and will reinvest revenues to serve its social mission rather than to enrich its manger and directors (Hansmann, 1980, 1996).

Despite this scholarship comparing nonprofit and for-profit organizations, the differences between nonprofit and governmental providers have been less studied. This is largely due to the assumption that nonprofit organizations, as recipients of government funding, will also have similar priorities and behaviors as governmental providers. Public mandates, however, are often broad, unclear, and contradictory, which gives nonprofit providers a great deal of discretion in how policy is implemented and how services are provided (Salamon, 1995; Sosin, 2010). In addition, governmental providers are also regarded as "suppliers of last resort" and generally serve a broader clientele, many of whom cannot afford to purchase services at market rates (Kapur & Weisbrod, 2000). The childcare industry provides support for the idea that governmental providers are more likely to serve publicly subsidized clients (Kapur & Weisbrod, 2000; Small & Stark, 2005).

These theories suggest that nonprofit providers have a number of comparative advantages over other providers, in particular in "trust" industries such as childcare. In addition to the passion of mission-driven entrepreneurs and higher levels of trust, nonprofits also enjoy specific legal and tax advantages, such as the ability to solicit tax deductible donations and the exemption from property and corporate income taxes. While the relationship of these advantages to service quality is not unknown/new, this study contributes to the