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A Performance Audit of the Use of COLA Funds by HHS Local Providers

Cost-of-living adjustments (COLAs) for state-contracted local service providers for the Departments of Health (DOH), Human Services (DHS), and Environmental Quality (DEQ), appear to be used properly for employee compensation and operating costs. We do not believe it necessary to have greater state control over the funds' distribution or use. In fact, given the amount of the funding increases, their appropriate uses, and the large number of providers to which funds are dispersed, it may be beneficial to call these funds a provider funding increase and eliminate the designation as a COLA.

There are some misconceptions as to the amount and use of local provider "COLAs" entrusted to three Utah departments. These misconceptions include the following:

- that state agencies are holding and not releasing the funds to the service providers
- that the Budgetary Procedures Act (***Utah Code*** 63-38) requires the funding to be used specifically for provider staff compensation
- that the funding calculation method should reflect varying percentages for personnel costs, differing by provider group

Fiscal year 2002 provider funding increases were appropriated without direction on use.

In fact, state agencies sent the fiscal year 2002 funding increase to service providers and local authorities as intended. Second, while recommended by the Governor as a cost-of-living adjustment, the funding, when approved by the Legislature, is provided without specific direction and without intent language. In spite of the lack of direction, the funding appears to be used for provider expenses (frequently compensation) that are within the scope of the contract.

Finally, the issue of how to calculate the funding increase has been raised. Specifically, there is a concern that too much money may be appropriated if the increase is calculated on over-estimated provider personnel expenditures. Rather than complicate the calculations by using percentages varying between 65 and 80 percent for different providers, the Legislature should consider amending the Budgetary Procedures Act to eliminate the compensation-related terminology and revamping the COLA as a funding increase. Then the funding calculation would no longer be affected by the percent of personnel costs in providers' budgets. Giving a simple funding increase makes sense in that the funding given to providers is a small portion of their total funding; asking them to track the funds to ensure their use as compensation might place a disproportionate burden on their reporting systems.

In practice, the increase is combined with other General Fund appropriations to provider entities and spent as needed for contracted service provision. We found that surveyed service providers gave staff raises for fiscal year 2002 and many indicated the increase in funds was used as part of those raises. Thus, it appears these funds may not need increased controls and, in fact, the funding increase constitutes too small a proportion of providers' total funding to justify adding controls. Many providers reported the state cost-of-living adjustment to be about 0.6 percent of their total revenue stream; even the increase to providers that are primarily state-funded came to just 2.27 percent of their total revenues.

Limited Provider Funds Are Widely Distributed

The Utah Departments of Human Services, Health, and Environmental Quality provide some services by contracting with 400 direct service providers, local authorities, and/or local health departments.

In fiscal year 2002, over \$119,000,000 in state General Funds were contracted to these providers, with an additional \$2.9 million (2.4 percent) being appropriated to increase funding to the providers. Significant amounts of provider funds also come from other sources not used in the cost-of-living calculations, including federal grants and local matching funds.

Figure 1. State-contracted General Funds to Local Providers Were Eligible for an Increase for Fiscal Year 2002. The increase in state General Funding is relatively small compared to the total local provider contracting from General Funds by three of Utah's departments.

Department	Total General Fund (GF) Base	FY2002 Increase**	Percent of GF
Human Services*	\$116,420,600	\$2,794,100	2.40%
Health	2,085,700	48,100	2.31
Environmental Quality	815,100	18,600	2.28
Total	\$119,321,400	\$2,860,800	2.40%

* Data on Human Services taken from Fiscal Analyst's report on COLAs.

** The amount of increase was calculated on fiscal year 2001 General Funds.

As the figure shows, the majority of the fiscal year 2002 increase went to DHS local providers. Percentages are lower than the appropriated three percent because the increases were based on the personal services, not total, budgets. Thus, if personnel costs are 80 percent of a provider's budget, the 3 percent increase would be applied to 80 percent of the total General Fund base, resulting in a 2.4 percent increase in the total.

DHS Local Providers Receive Majority of Funding

The Department of Human Services (DHS) contracts with 389 providers for about 97 percent (\$116 million) of the state funding that is subject to the so-called COLA adjustments. Three divisions contract directly with service providers and three contract with local authorities, which may in turn contract with local service providers.

DHS contracts with direct service providers through the following divisions:

Almost 400 providers for six Human Services divisions receive 97% of funding that is eligible for an increase.

- Child and Family Services (DCFS)
- Youth Corrections (DYC)
- Services for People with Disabilities (DSPD)

Contract payments occur under a unit-of-service arrangement; contracts are both rate-based, open-ended and lump sum. Provider payments are determined by the amount of specific service provided.

3 divisions contract directly with service providers, 3 with local authorities.

The following DHS divisions contract with local authorities, which are public or private agencies authorized to provide specific services in a given area of the state:

- Aging and Adult Services (DAAS)
- Mental Health (DMH)
- Substance Abuse (DSA)

Funds are passed through these state divisions via contract on a cost reimbursement basis. Funds are allocated among the local authorities through formulas developed by each of the three divisions; formulas typically include such factors as population, square mileage of the area, and percent of the service population (such as the elderly) living in the area. Some of the local authorities provide services themselves, while others subcontract with local providers for needed services.

DOH and DEQ Contract with Local Health Departments

DOH and DEQ contract over \$2.8 million to 12 local health departments.

The Departments of Health (DOH) and Environmental Quality (DEQ) contract with Utah's 12 local health departments (LHD) to provide a variety of health-related services. In fiscal year 2002, DOH contracted out \$2 million for local services and DEQ contracted out \$815,000 to the LHDs. These 12 LHDs are eligible for funding increases under the Budgetary Procedures Act; they received an additional \$48,100 in DOH funds and \$18,600 in DEQ funds.

Funds are allocated to each LHD based on the population and square miles of each service area; in addition, the DOH allocation formula includes the area's poverty level as a factor. DOH sets minimum performance standards for the LHDs and lets them decide which health services are needed in their service area. DEQ contracts for services specified in an annual work plan set up with each LHD.

Finally, although the State Office of Rehabilitation received a cost-of-living adjustment for its independent living center providers, the office was not included in this review. The increase was not provided because of Budgetary Procedures Act requirements, but was approved through intent language in the Appropriations Act for fiscal year 2002. The increase may or may not be an ongoing appropriation. As noted in the Legislative Fiscal Analyst's report, "Review of Calculation Method for Local Provider COLA," on computing COLAs, the Legislature may want to consider whether to provide such increases to entities not listed in the law.

Provider Cola Is Not Required; Use of Funds Is Not Specified

The Budgetary Procedures Act does not require local provider COLAs.

The Budgetary Procedures Act (*Utah Code* 63-38) does not require the appropriation of cost-of-living adjustments (COLAs) to local service providers, but just requires the Governor to consider recommending such adjustments. Additionally, the Appropriations Act for fiscal year 2002 contains no relevant intent language directing that any of the increase in funds for local providers must be used for COLAs. Further, contracts with providers lack specific directions for the use of the increase. Though some providers and state contract coordinators perceive the funds to be meant for compensation increases, there is no legal obligation for this specific use.

Funds Lack Obligating Intent Language

According to the Budgetary Procedures Act, the Governor must *consider recommending* the same increase for wages and benefits for certain local providers that he recommends for state employees. In his 2002 budget proposal, the Governor recommended a three percent cost-of-living adjustment for the providers listed in the Budgetary Procedures Act. However, nothing in the language of the Budgetary Procedures Act requires the Legislature to approve the recommended adjustments.

Specifically, *Utah Code* 63-38-2(10)(b) states the following:

In his budget recommendations under Subsections (10)(a)(i), (ii), and (iii), the governor shall consider an amount sufficient to grant local health departments, local mental health authorities, local

Law directs the Governor to *consider recommending* a provider increase for wages and benefits.

substance abuse authorities, and area agencies the same percentage increase for wages and benefits that he includes in his budget for persons employed by the state.

Another similar provision, **Utah Code** 63-38-2(11)(a) includes more service providers as follows:

In submitting the budget for the Division of Services for People with Disabilities, the Division of Child and Family Services, and the Division of Youth Corrections within the Department of Human Services, the governor shall consider an amount sufficient to grant employees of corporations that provide direct services under contract with those divisions, the same percentage increase for cost-of-living that he includes in his budget for persons employed by the state.

Like all other recommendations from the Governor, these recommendations were submitted to the Legislature for approval, modification, or rejection in the appropriations process. A specific use of appropriated funding can be required if intent language is attached to the appropriation. However, a review of the fiscal year 2002 Appropriations Act (S.B.01) did not find any intent language regarding specific use of the approved three percent increase for Health and Human Services local providers. The Legislative Fiscal Analyst's Office confirmed that no relevant intent language has been written for these funds.

A review of contracts between the three departments and their local providers found no provisions directing the providers to use a portion of their funding for compensation increases. If present, contract provisions could legally bind the contractor to a specific use of the funds. State contract coordinators agree that the contracts do not refer specifically to the increased funds.

State staff report they do not give other specific instructions on how to use the funding increase. Rather, the funds are included with other contract funding as a lump sum increase to the local authorities, or as a rate increase for the direct service providers on rate-based contracts.

Funds Can Be Spent as Needed

Either specific intent language in the Appropriations Act or a provision in providers' contracts would be required to obligate providers to use the

No binding intent language exists to limit the use of provider increases.

We found no contract provisions directing specific use of the provider increase.

At present, the funds can be used for anything within the scope of the contract.

increase in contract funds for compensation. Lacking such legally binding directives, the funds can be used for compensation increases or other needs.

An Office of Legislative Research and General Counsel attorney indicated that the lack of intent language allows the providers to use the funds any way they wish within the scope of the contract. Further, legal counsel indicated that nothing in the Budgetary Procedures Act requires the Legislature either to appropriate the recommended funds or to restrict their use. If the Legislature wants to limit the use of funds appropriated for increases in the future, legislative intent language should be included in the Appropriations Act.

Providers Use Funds Appropriately

The Departments of Human Services, Health, and Environmental Quality passed the appropriated funding increase along to the local providers, local authorities, and local health departments as intended. Local authorities and other providers indicate they used the fiscal year 2002 increase to give compensation adjustments or to provide services.

Funding Increases Are Passed to Providers

Once appropriated to state departments, the funding increases are intended to be passed through to the local providers and authorities. We found that all DHS divisions as well as DOH and DEQ have dispersed these funds to their contracted providers as intended.

In DHS, two methods are used to distribute these funds. The three divisions allocating funds to local authorities (Substance Abuse, Aging and Adult Services, and Mental Health) put the funds through their allocation formulas with the rest of the General Funds to be allocated, then amend the contracts with the local authorities to reflect the increase. We spoke with local authorities' staff and received assurances that the funds had been added to their contracts for fiscal year 2002. A review of contract documents and correspondence between the divisions and their contractors confirms that the increases were distributed to the local authorities.

DHS, DOH, DEQ all pass the funding increases to their local providers as intended.

Three divisions disperse the increase by increasing payment rates to providers.

The three divisions contracting with direct service providers (Child and Family Services, Youth Corrections, and Services to People with Disabilities) adjust many of their service rates to reflect the increase in funding. For example, contract management staff stated that the majority of payments by both DCFS and DYC are for residential care and residential treatment services; we noted an appropriate increase in the rate of payment per unit of service for these and other commonly used service codes. Other provider documentation confirmed the increases.

Data from DSPD show that, at 7.5 months (62.5 percent) into the fiscal year, about 77 percent of the COLA funds have been spent through increased rates paid to providers. At the present rate of expenditure, DSPD will disperse all of the increase to providers before the end of the fiscal year. Data from DCFS and DYC were not easily available, but because of a shift in demand to a lower cost treatment service, these divisions may have some funds left at the end of the year. The department's Director of Fiscal Operations indicated that, in the event funds remained in any accounts used to pay providers, those funds would lapse to the General Fund or be used for provider services in the next fiscal year.

DEQ and DOH pass the increase to LHDs in their General Fund allocations.

DOH and DEQ staff handling contracts with the local health departments provided documentation showing that the increased funding was being allocated to the LHDs in the same proportion as the rest of the contracted General Funds. LHD directors confirmed that the increase was received and was used where most needed to provide contracted services.

Uses of Funds Include Compensation, Service Provision

In general, providers said they used the increase for pay adjustments or for operating costs.

We contacted a sample of providers to determine how they used the fiscal year 2002 increase. In general, providers said they used the funds either for compensation increases or for operating costs. While some providers believe that these funds are given specifically for compensation adjustments, others view the funds simply as an increase in funding and use the money where needed. Because these providers are service-based entities, the majority of their operating costs are for personnel. Thus, even those who said the increase went to operating costs would have used much of the funds for personnel.

Many providers used the increase in funds for salaries and benefit increases.

Some providers say they didn't know the increase was meant for compensation and used it for other costs.

It appears unnecessary to add controls over the use of the funding increase.

A Number of Providers Indicated That the Funding Increase Was Used for Staff Wage or Benefit Increases. Several Mental Health local authorities indicated that although they were not specifically told to use the increase for compensation adjustments, they did use the funds for wages or benefits.

For example, one provider stated that he was aware of how the increase is calculated; he felt that since the increase was calculated based on provider personnel expenditures, he needed to use the increase in that area. This provider (and others) adjusted the staff pay plan to distribute the three percent increase among employees. In general, providers noted that whether or not a state funding increase occurs, they give compensation increases in order to compete in the market and keep their employees. Those local authorities that are county agencies are often able to provide county-approved compensation adjustments as well.

Other Providers Told Us They Were Unaware of a Link to Employee Compensation. When asked how the funds were used, some providers stated that any increase in funding would be used where it was most needed. For example, directors of eight of the ten local health departments indicated the funds were used for program costs or service delivery. One director of an area agency on aging (AAA) stated that she did not differentiate the increase from other contract funds and that “all money is green.” State funding was used to provide program services as needed.

Contract management staff at the state level generally view the increase as a general funding increase for the local authorities and direct service providers. Some commented that they would prefer that the increase be called by something other than a COLA, such as a “contract increase” or “inflationary cost increase.”

Increase Too Small to Justify Adding Controls

More controls over the use of the local provider funding increase appear unnecessary. As discussed, current uses are appropriate and reasonable. Further, the increase in funding appropriated for fiscal year

2002 is a relatively small part of the total funding for the various Health and Human Services providers we reviewed. For many providers, the increase in funding comprises less than one percent of the total funding received from federal, state, and other sources. Therefore, we believe the addition of controls to monitor the use of these funds would unduly burden the local authorities and providers.

Increase a Small Portion of Providers' Funding

Though not an insignificant amount of General Funds, the \$2.9 million funding increase for local service providers nonetheless comprises a small portion of providers' funding when compared to total funding for those providers (state, federal, local, etc.). While the fiscal year 2002 increase was authorized as three percent of state General Funding, the net increase to many providers was much less. For example,

- The \$165,000 increase for all 12 Area Agencies of Aging is 0.57 percent of the state and federal funds passed through the DAAS. Since the AAAs also receive local and donated funding, the increase is an even smaller percentage of their total funds.
- The \$224,800 appropriated to the 13 Substance Abuse local authorities equals 1 percent of their combined federal, state, and county funding.
- Several individual local substance abuse authorities reported the increase to be from 0.40 to 0.64 percent of their total funds.
- Youth Corrections apportioned an \$891,900 increase to 76 providers through rate increases. The increase is 2.27 percent of the total state and federal funding contracted to those providers.
- The 12 local health departments received a \$66,700 increase from DOH and DEQ, with total reported funding of \$69,483,218 (calendar year 2002); the increase is just 0.1 percent of their total funds.

Added Controls Likely to Be Burdensome

Under current circumstances, the addition of controls to monitor the use of the provider increase may unduly burden the local authorities and

Some providers already deal with requirements to track many funding sources.

providers. The increase in funds is a small, yet important, portion of the funding used by these local providers. Given the small amount of funding and the fact that the funds appear to be used appropriately, it would be inefficient to require more administrative resources (for accounting or tracking controls) to be spent on these funds.

Present requirements on these providers, most of which have multiple funding sources, should also be considered. One provider located in the Wasatch Front indicated her agency has 64 sources of funding with varying tracking and reporting requirements. In our discussion on their use of the increase in state funds, this director pleaded with us, “please don’t make it any more complicated than it already is” in relation to her reporting process.

Any General Fund increases going to local service providers will be spent primarily on compensation adjustments. According to the Legislative Fiscal Analyst’s “Review of Calculation Method for Local Provider COLA,” personnel costs as a percentage of total operating budgets for the Health and Human Services providers range from 65 to 80 percent of total expenses. Thus, additional funding would likely be spent on personnel costs, regardless of the level of controls placed on spending.

Summary and Recommendations

In summary, the increase in provider funding is a small portion of total provider funding, with relatively small amounts of funds being spread among a large number of providers. Rather than identifying the precise amount of personnel expenditures for each group of providers in order to compute cost-of-living adjustments, it may be more efficient to eliminate the funding’s attachment to personnel and give providers general increases to be used as needed in their operations, especially considering the fact that providers typically spend the majority of their funds on personnel costs.

Alternately, the Legislature may want to clarify its intent to ensure that the appropriated increase is used for provider compensation costs. If so, the inclusion of intent language within the Appropriations Act when the provider increases are appropriated would be needed.

Recommendations:

1. We recommend that the Legislature consider amending the Budgetary Procedures Act to eliminate compensation-related language and use terminology such as “provider funding increase” instead.
2. We recommend that, if the Legislature prefers to leave the compensation language in the Budgetary Procedures Act, it may wish to consider either:
 - including intent language in the Appropriations Act directing the providers to use the funding increase for compensation,
or
 - directing the departments to amend their contracts with local providers to include language requiring the providers to use the funding increase for compensation.