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Background

My name is Catherine Trapani, and I am the Executive Director of Homeless Services United (HSU). I would like to express my gratitude to the New York City Council's Committees on General Welfare and Contracts, particularly Chairs Levin and Brannan for calling this hearing today and providing me with the opportunity to testify.

HSU is a coalition of approximately 50 non-profit agencies serving homeless and at-risk adults and families in New York City. HSU provides advocacy, information, and training to member agencies to expand their capacity to deliver high-quality services.

When the right to shelter was first upheld in the City of New York, the City worked to establish a system to provide shelter and care to every person who needed it. By the mid-1990s, the City grew to realize that government couldn't rise to this challenge on their own and began to privatize the shelter system, contracting with nonprofit providers who were mission driven and who has the requisite skills to design effective programs that could properly support the growing homeless population in our City. As the system grew, a competitive application process was created where nonprofits proposed programs that conformed to City and State regulations while explaining their unique approach to combat homelessness. These applications were vetted and subject to hearings and responsibility determinations prior to awards being made based on the approach outlined by the provider and nonprofits were allowed to execute programs. These multiyear contracts were entered into, but there was no plan in place to support programs in the long term. An optimistic reading of the history might suggest that many assumed the first Tier II shelters for families would be transitioned into permanent housing within a few years and there would not be a need to manage and maintain a large shelter system in the long term. Sadly, this was not the case. Contracts did need to be renewed, and extended and more and more capacity has been necessary. Failure to plan for this capacity in advance led to a haphazard system functioning in an emergency/crisis mode with little thought given to how to preserve shelter. Rates for the provision of shelter services have remained stagnant since the system was created over 30 years ago.

A less optimistic view of our history might also note that some of this failure to plan for the preservation of shelter by raising rates of creating a capacity plan was by design: by allowing existing shelters to deteriorate and failing to mindfully plan for new, quality shelter capacity when it was needed, the City actively discouraged families and individuals to enter shelters in a bid to reduce the number of people utilizing shelter without actually having to address their housing needs. Provider requests for additional funds (known as “new needs” requests) to address maintenance and other critical needs went unanswered, attempts to purchase City owned properties and raise capital funding to make necessary improvements were rebuffed and the system and the clients it served continued to suffer.

However one chooses to read the historical record, one thing is clear, the shelter system evolved from one that was designed to entrust nonprofit service providers to meet a critical service need of the most vulnerable New Yorkers to one that was starved for resources and haphazardly expanded to meet an ever growing need. Andrea Elliot’s *Invisible Child* series published in the *New York Times* at the end of the Bloomberg administration painstakingly documented the human costs of this disinvestment. During Mayor de Blasio’s first years in office, audits and other reports followed documenting poor shelter conditions and other deficiencies. The administration identified key reforms, first in the 90-Day Review of homeless services and later in the Turning the Tide plan to tackle these issues but, from the perspective of HSU member service providers, the biggest obstacle in delivering on those reforms and initiatives was clear: **you cannot deliver quality services if there isn’t sufficient funding flowing in the system to support those services.**

It has become routine for contracts to be so short funded that providers run out of many half or two thirds the way into the fiscal year. The stressful work environments and challenging working conditions resulted in staff turnover, ironically resulting in accruals providers have come to rely upon to plug funding gaps. Many providers require numerous modifications to use such accruals to plug such budget holes. Amendments have also become commonplace; the City will add funds on an emergency basis to cover costs that cannot be otherwise met. These practices have resulted in an unusually high number of contract actions and have contributed to chronic delays in contract registration and payments that have resulted in serious cash flow problems. Most providers run deficits, many rely on emergency loans and lines of credit, some have strained relationships with vendors, struggle to cover critical costs like payroll, employee health insurance payments and more. Many have maxed out lines of credit. The interest paid to banks by nonprofit providers to cover their bank loans is estimated to be at least $1.25 million and could be up to $3 million – enough to operate a service rich medium sized shelter for families with children for one year.

In addition to unreimbursed interest, delays in contract registration and payment lags result in significant financial hardship. A recent report by the New York City Comptroller noted that 100% of homeless services were registered retroactively meaning providers were unable to draw down funds on their contract until after work had started in every contracted program for fiscal 17. While the situation has modestly improved since then, delays remain routine. The total cost of these delays in the current fiscal year using the most optimistic estimates is roughly $325,000,000 for the provision of shelter services (services already rendered, but not paid). Because of delays in payments, many providers have had to rely on lines of credit to make ends meet. Some organizations are still awaiting payments from as far back as fiscal year 2015. The books are closed for those tax years and agencies have been forced to post substantial losses - this reflects poorly on the fiscal health of service providers and could impact their credit ratings and ability to secure financing for future projects and program expansions.

Given this history, it should be no surprise that HSU and our member programs were thrilled when we learned that the administration was planning to embark on a process to reform the way rates for shelter were set. The City announced it would undergo a "rate rationalization" process where programs would be reimbursed according to formulas based on the real cost of operating shelter programs and would no longer be subject to wild variations depending on who was able to negotiate an emergency deal with the most favorable terms at some point in history.

The City created what we have come to know as the "model budget" to guide this process and, providers were optimistic that it would align current costs with actual rates, rightsizing decades old contracts to ensure funding levels were sufficient to cover maintenance and operations of an aging shelter portfolio. We were hopeful that the new rates would ensure sufficient funding to fulfill State and Local mandates for staffing and service requirements which hadn't kept pace with wage growth resulting in high turnover and instability in the sector.

The sector enthusiastically supported this effort, hoping that after decades of neglect, the City would support mission driven providers and partner with us to transform the shelter system and restore quality services for homeless New Yorkers Citywide.

To our dismay, instead of undertaking a collaborative "rate rationalization" process that would address the historic lack of escalations in funding and chronic underinvestment, the City approached it as an exercise in micromanaging budgets line by line forcing changes in approach that belie the expertise of providers, continued to underfund documented costs and mandates while only partially addressing the desperate need for increased resources.

"Model Budget" Approach and Parameters

The City held community meetings at the beginning of the "model budget" process to share their vision with the community outlining goals and what would and would not be included in the model. Following this meeting, providers were under the impression that the City would roll out a template for a model budget - that there would be assumptions made with regard to unit costs and/or standard salaries for like positions. Instead, providers have been given little to no direction regarding how to build these "model budgets". The City did not share with providers what bottom line number they were trying to get to overall, or, in any cost category forcing an iterative, labor intensive process where providers were blind as to the City's goals. In most cases, providers first proposed real costs then, when that budget was rejected, they began arbitrarily paring down costs in an effort to conform with City expectations sometimes being told to increase or decrease lines in different ways by different DHS staffers to get to some unknown goal. Had the City created and released term sheets, providers would have been better able to understand the City's parameters and come up with a budget that conformed to those standards on the first round. As a result, each provider is negotiating differing rates and percent increases. Our observations of these disparities seem to be contrary to the notion of a true "model" and while we expect some degree of variation based on a given providers' approach, it remains unclear how rate disparity across providers for similar services will be addressed.

Our understanding of the methodology used as a basis for the negotiations is that the City is determining cost targets for line item expenses based on average rates of pay in the DHS portfolio. Given the historic underfunding of the entire sector, averages are a poor metric of where we should be given that a "model budget" exercise would not be necessary if the average rate of pay was sufficient. A more suitable metric might be to look more broadly beyond the DHS system to determine rates for salaries, fringe, and other metrics that may have more appropriate comparables.

For example, average costs are an imperfect metric for lines like maintenance. There is great variation in the true cost of maintaining a shelter facility depending on the age of the structure, what building materials have been used, the type and age of building systems in place and more. Using only an average per unit/bed cost misses these nuances such that using the DHS formula a building constructed in 2015 with modern materials and green construction is funded at the same rate as a building constructed in 1905 with an oil burning boiler, porous brick facade and aging roof. There is also doesn't appear to be a distinction between properties owned by the City, which historically suffered the most disinvestment, or properties owned and managed by mission driven nonprofits or other entities which have less deferred maintenance.

While most providers anticipate substantial increases in their maintenance lines, and we are grateful for those increases, using a true cost approach to set those rates would be more appropriate and, may allow some providers with more efficient and durable properties to redirect some monies to other areas in the budget that require more resources.

In addition, only looking at average cost line by line misses the opportunity to look at the totality of the program and tailor the "model" to a providers' approach. Providers who are able to save money in one cost category are not necessarily being allowed to shift resources to lines where they feel they need more support if it's out of alignment with the model even if the bottom line amount is the same and even if the provider is able to adhere to state and city regulations and other programmatic requirements. For instance, security is the other area (in addition to maintenance) where shelters are seeing substantial investments under the model given NYPD recommendations have driven up average costs and recommendations on this line. However, if a provider's approach to shelter security relies on low staff to client ratios and a competitively paid workforce with lower than average turnover to engender trust with clients and reduce conflict, they may not need to spend up to the average in this category. Such a provider may wish to spend less on security guards and more on case managers but, it is unclear if the model isn't flexible enough to support this approach.

Employee Compensation not included in the "Model"

The "model" seems to include salary averages but, providers have been repeatedly told that "'model budget' is not an exercise in parity" and, that fringe is not a part of the "model". The omission of compensation from the model leaves providers with many unfunded mandates and makes it more challenging to attract and retain a high quality workforce that we need to ensure quality services.

Specifically, the following considerations are not a part of the model:

- **Fringe**: DHS continues to cap fringe at a max if 26%regardless of documented expenses being considerably higher, including in cases where agencies have unionized staff with labor agreements requiring larger investments; the industry average is 37%.
- **Salary parity:** while DHS did research to determine average salary across several lines, agencies were not permitted to raise salaries to the average to establish parity across programs or to assist with recruiting and retention. We understand that this was beyond the scope of the "model" but, in order to truly right-size budgets and attract and retain talented workers, parity will need to be addressed in the near future.
  - The impact of low wages and resulting high turnover cannot be overstated. Providers' ability to deliver quality services is hindered by turnover. This concern was raised with DHS during discussions related to performance metrics and targets with program staff and we were told then that it would be addressed with model budgets but, that has not been the case.
- **Wage compression solutions:** with the increase to minimum wage, some supervisors now earn the same as, or nearly the same as, their supervisees. In addition, THRIVE social workers were brought on at a standard salary of $55,000 per year, a level higher than some social service and program directors. While DHS made some exceptions for agencies to make wage adjustments in the most egregious cases, there was no guidance on how to address this across the board. Some agencies were told they could not adjust wages beyond implementing COLAs at all, while others successfully argued for exceptions to policy. The process was haphazard and seems contrary to the notion of a "model" given the lack of consistent guidance. We request that DHS make clear under what circumstances wage adjustments might be permitted and release guidance to all providers.
- **Overtime:** The model budget does not allow nonprofits to budget for overtime, even when it is common for certain titles. This leaves providers with an unfunded mandate to pay overtime wages to employees who work to cover holidays, stay late when emergencies arise to ensure coverage and to pass critical information on to first responders and more. Because new overtime regulations increase the wage at which employees are eligible for overtime pay to $58,500, nearly every employee working in shelters will no longer hold exempt status. Employees who routinely work more than 40 hours a week, such as superintendents of buildings and residence managers who must be able to respond to emergencies and work unforeseen extra hours will now be entitled to overtime pay yet, the model does not allow providers to budget for such expenses.
  - One provider had a solution - they calculated that it was actually less expensive to raise the wage of some titles to be higher than the new threshold to avoid having to pay overtime wages. Even though this was the less expensive option, DHS refused to allow the provider to do this and simply passed on the additional expense to the nonprofit without reimbursement

Indirect

The true cost of overhead or indirect expenses is still not funded in the "model". We are gratified that in accordance with new City policy DHS raised their indirect rate from 8.5% to 10% but the true cost is much higher.

Escalations

The model budget does not include any provisions for cost escalations over the course of multi-year contracts effectively negating the value of this entire exercise in the sense that we are doomed to have to repeat it. This may also deter providers from proposing new sites because the contract revenue isn't sufficient, particularly in the out years, to support responsible operations and building maintenance in the long term.

Implementation Challenges

The City has used several different forms and templates that have evolved over the course of negotiations which force providers to attempt to translate and unpack cost categories that are defined differently across various platforms (HHS Accelerator, internal DHS templates and spreadsheets). This is causing confusion and errors delaying the process.

Once providers submit templates it often takes months before they receive any feedback and several months more before a meeting takes place. Some providers in the first cohort to be called in for negotiations have been waiting since October-December 2017 for a response to their budget templates.

Providers who negotiated agreements in some areas with DHS leadership or DHS finance are later told by program analysts that agreed upon costs are not allowable and told to revise budgets and disallowing expenses. Providers are left with a lack of clarity over who has authority to negotiate, how to interpret agency commitments and how they may proceed with the process.

DHS has given conflicting information to providers on how the agency is handling "new needs" requests for additional funding mid-year to cover necessary costs not included in currently approved budgets. Initially, the agency had refused to entertain these because they would all be "folded into the model" but, because of the extensive time lags, some providers are being given emergency relief while others are not. There is no clear guidance into how this should be handled-- it is all done "case by case" leaving the community unclear on policy and unable to plan.

The result has been a process that has been crippled with delays – fewer than 10 providers have completed the process and the fiscal relief has yet to reach our membership. Despite much talk of the investments in areas like maintenance, security and social workers in family shelters, much little of this money is flowing to providers due to the slow implementation process and continued delays in registering contract amendments.

Impact of Delays – Fiscal 2019 Implications

Because of delayed implementation, nonprofits haven't completed negotiations for their new FY2018 funding levels and those contract amendments haven't been registered. This is now impacting FY2019 budgets because, in order to ensure timely registration for those contracts and ensure cash flow, providers had to submit numbers to DHS in advance. This means that we are going into FY19 based on approved FY18 rates, the vast majority of which are actually rates that date back to the early-mid 1990s. This will make it necessary to once again go through an amendment process to catch up in fiscal 19, just as we've had to endure in prior years guaranteeing a third straight year of underfunded contracts and payment delays. In real terms, this translates to:

- **The promised indirect rate increase is not being implemented in FY19 budgets currently submitted to DHS.** Providers have not been allowed to adjust the old rate of 8.5% in their FY19 contracts because this new rate was bundled with other changes to the budget pending the outcome of model budget negotiations. We have been assured that this will be covered in a special addendum, but given the recent history, we are not overly confident.

- **COLA adjustments will be unfunded for a third straight year.** DHS paid the 2% COLA for FY16, but then failed to fund the FY17 and FY18 COLAS. By forcing providers to submit FY19 budgets based on FY 17/18 rates, this will be the third year the COLA has gone unfunded. By agreeing to COLA adjustments and then not funding the additional cost, DHS has prevented providers from giving adequate raises to staff, resulting in high rates of turnover in key service positions. One member agency has calculated that a typical case manager at one of our sites is owed about $2,200 in un-funded COLA adjustments. Because implementation of COLAs has been so delayed, there are now tax implications for employees and agencies alike with respect to retro-pay once/if those payments are eventually made

- **Unfunded mandatory minimum wage increases.** By not funding mandatory minimum wage increases until after model budgets are done negotiating, providers have had to float the new costs for an entire fiscal year. To date we estimate providers have been forced to cover more than $5 million in additional personnel costs to remain compliant with the law. Funds for this increase are not included in the FY19 budgets.

- **Requests for additional funding to address emergencies known as "new needs" requests, have gone unanswered**. This has forced providers to defer hiring on critical positions such as THRIVE Social Workers. Maintenance has also been delayed in some sites due to lack of funds which has only made it more difficult to register contracts and amendments down the road due to outstanding violations holding up the process.

- **Problems with Close-outs.** Because the abovementioned "new needs" requests are still pending final negotiations, these amendments are not yet active in Accelerator with only days left in the fiscal year. If the money does come through before June 30th programs cannot spend money fast enough in order to close out on time. CFOs and accounting staff don't know if they can book money as a receivable for the current fiscal year since it isn't clear it will be paid out given negotiations are still ongoing - this has implications for audits.

Conclusion

The homeless services sector has struggled with underfunded contracts and delayed payments for years. The impact of the lack of investment has truly pushed many providers to the brink. The "model budget", once fully implemented will substantially improve providers' ability to fully fund maintenance on most sites as well as security but, it leaves many critical cost categories underfunded and, does not provide a solution for the long term given the lack of escalation clauses in contracts. We are eager to find solutions to improve upon these processes that were meant to alleviate these challenges and to rebuild a shelter system that delivers the quality services homeless New Yorkers deserve.

To summarize our recommendations are as follows:

- Clear the backlog of unregistered contracts *and amendments* including those related to COLA implementation to ensure timely registration and ease cash flow
- Allow providers to include approved costs such as the 10% indirect rate in their FY19 budgets even if their "model budget" negotiations are not yet complete
- Work with providers to address challenges with close-outs in cases where pending amendments for the current fiscal year present challenges
- Share term sheets that include cost parameters with providers to make budget negotiations more transparent and efficient
- Use a true cost framework to set rates instead of relying on industry averages that are artificially low given the history of chronic underfunding in the homeless services sector
- Use consistent templates across platforms to implement the model (Accelerator, OTDA budget templates, DHS budget templates) to ensure consistency and lower administrative burdens
- Allow for flexibility across lines when providers can demonstrate an ability to comply with programmatic goals and regulations
- Make decision making protocols across both the finance and program divisions of DHS transparent so providers are clear on who is empowered to sign off on budget negotiations and to avoid different departments giving different guidance as is currently the case
- Address underfunded costs not included in the "model" including fringe, salary parity, salary compression, overtime and indirect
- Implement budgetary changes in any given fiscal year with ample time for registration of amendments prior to budgets being due for the following fiscal year to avoid a prolonged multi-year amendment process prior before providers experience budgetary relief
- Create a clear mechanism to address cost escalations in multi-year contracts

We thank the Council for your attention to these critical issues and look forward to continued partnership to restore the fiscal health of our sector. Thank you for the opportunity to testify.