Wage Incentive Provision of the Extended Employment Funding Rule

An evaluation of the impact of the money appropriated for wage incentives and how the wage incentive program works

January 2008

Introduction

Minnesota Session Law Chapter 135, Sec. 9., authorized the Minnesota Department of Employment and Economic Development (DEED) to convene a work group to evaluate the impact of the money appropriated for wage incentives and how the wage incentive program works. A work group of three community rehabilitation program managers was convened in August 2007. The following report provides a summary of the findings and preliminary recommendations.

Wage Incentive Provision of the Extended Employment Funding Rule

The wage incentive provision is authorized in MN Rules 3300.2045 as part of the Extended Employment (EE) basic funding system, which funds community rehabilitation programs (CRPs) certified by DEED. The rule is authorized in MN Statute 268A.15.

The EE basic funding system is based on the number of hours worked by an individual with a severe disability who needs ongoing supports to maintain or improve his or her employment. Ongoing supports are based on the worker's needs under an individual employment plan. In each of the past few years, between 5,900 and 6,200 workers received supports from 29 community rehabilitation programs across the state.

The Extended Employment program recognizes four types of employment for funding:

1. Supported employment (SE): fully integrated employment in jobs in the community paid at normal competitive wages.
2. Community employment (CE): employment in jobs in the community that pay noncompetitive wages or may not be in an integrated setting.
3. Affirmative-based enterprise (ABE): pays competitive wages in an enterprise owned by a community rehabilitation program. The ABE work place does not meet standards of integration typically found in the community.
4. Center-based employment (CBE): work on the premises of a community rehabilitation center which may pay above minimum wage but will not be integrated. Programs may pay individuals below minimum wage if they have a sub-minimum wage certificate issued by the Department of Labor. Programs with a sub-minimum wage must meet requirements from the Department of Labor on how worker productivity is measured and appropriate wage rates assigned to the individual for each job performed.

How the Wage Incentive Works

Payments to providers are determined by the number of work hours reported by individuals in each type of employment. For supported employment the hourly rate is $3.60; for community employment and ABE it is $3.19; and for center-based employment the rate is $1.76. The payments are not necessarily equal to the cost of providing the ongoing supports. Providers usually supplement EE funding with other sources of income, such as business contract and county funds. In some cases a CRP may make the EE payments cover the full cost of the program.

Payments are made from two funds. The community support fund (CSF) pays for supported employment, community employment and ABE. The center-based fund (CBF) pays only for center-based employment. Providers may have contracts through either or both of the funds. Dollars may be transferred from the center-based fund to the community support fund, but not the other way. And once such a shift is made by a provider it is permanent and no return of the dollars in the other direction is allowed.

Providers are paid only for reported work hours. At the end of each state fiscal year a program audit verifies the accuracy of the hours reported to the Extended Employment program. If reported hours do not meet the standards under the rule the provider must return the payments. If a provider's reported hours in a particular fund fall short of what's specified in the contract, the provider will not receive the full contract payment. Any unearned contract dollars – both those returned after audit and those not paid – make up the dollars paid out under the wage incentive provision in the rule. The dollars fund separate wage incentive payments for the CSF and CBF based on the source of the dollars. In this biennium the Legislature appropriated an additional $125,000 directly for wage incentives for the community support fund for each year.

Wage incentive funding is based on the proportionate share of a provider's reported hours of work at minimum wage or higher compared to all hours reported by all providers. The total amount of wage incentive is the sum of the unearned dollars and returned dollars for the fund. Here's a simple example of how the formula works:

Provider XYZ reports 10,000 hours of work in the CSF. All providers report a combined total of 100,000 hours. There is $200,000 available to be distributed in wage incentives for the CSF. The equation is (10,000/100,000)*$200,000 = $20,000.

If a provider reports no hours in the CBF fund the provider's share is zero. The amount of wage incentive dollars a provider receives is never fixed. The amount available to distribute fluctuates when providers do not meet their individual contract production. Underproduction varies from year to year. An individual CRP's share depends not only on its own reported work hours but on every other provider's experience as well. A provider may report the same number of minimum wage hours as in the previous year, but still lose share because the total number of hours at minimum wage increased. Or a provider might increase its share, but receive fewer dollars because the total pot of dollars to be distributed has decreased.

History of the Wage Incentive

The current wage incentive provision is a product of a major 1999 revision of the Extended Employment funding rule. The change was intended to maintain some incentive for higher wages, which is a department goal.

The EE funding system was severely criticized in the early 1980s because the cost-based system in use at the time provided no measure of how effectively providers delivered services to individuals with severe disabilities. Critics also said the EE work standard was not up to the standard found in the community.

Indeed, most of the work (90 percent) was center-based employment – which at the time was called “sheltered” work – at a very low wage determined by piece-rate production under the sub-minimum wage certificate held by providers. Critics said that workers were ghettoized and kept from a normalized work experience by being left to work in the sheltered workshop. The legislation that emerged from the discussion mandated some form of outcome-based funding. It also implemented a strong policy change that made integrated employment in the community a primary goal of the program.

An advisory work group of community rehabilitation providers and representatives of disability advocacy groups worked with the department and developed a performance-based funding rule, which was implemented in 1987. The rule was based on hours of work and service. The first funding rule used a complicated formula to adjust the allocation received by each provider. One variable, the hourly wage by individual, was adjusted by a severity of disability factor for the individual. This factor was one of several that adjusted the individual CRP’s allocation. Other variables included a measure of economic and geographic conditions in the community, percentage of hours worked in the community and the severity of disability in persons supported by the CRP.

Wages increased during the operation of the first funding rule. Some of the increase in wages can be attributed to the shift of funding from center-based programs to community employment. Generally jobs in the community paid more than center-based employment even, when the community employment paid sub-minimum wage. The number of individuals working in the community grew by over 200 percent and the number of reported work hours increased just as dramatically.

Another factor was the transfer of individuals to development training and habilitation (DTH) funding from extended employment funding. Center-based programs for “lower productivity” workers were ended, and some workers entered DTH programs.

These changes came at a price. The rule was hard to administer. It was complex, requiring significant data to be collected and manipulated, and several of the factors were flawed. Two examples of the flawed variables were 1) the severity of disability index and 2) the economic and geographic factor. Staffing size and computer system issues compounded this problem.

But the most significant problem was the unpredictability of the funding. The funding rule was, in effect, a zero sum game. One CRP's loss was another CRP's gain. A CRP could improve wages, support more jobs in the community and work with individuals with severe disabilities – and still lose money over the previous year. This happened when the mean of all performance increased because the programs that had been weak in some performance factors improved their outcomes.

The first funding rule operated effectively in establishing work as an outcome. Wages improved and jobs in the community became more widely available. But the complexity and unpredictability of the funding rule lead to an administrative morass. By the mid-1990s the system was in trouble. Providers and the department were at loggerheads over the administration of the program. In 1995, a mediated work group of the department and CRP executives made several key decisions. The first was to freeze the CRP's funding at their individual current contracts. The second was to develop a new funding rule based on what was learned from the experience of the first rule.

A work group including representatives from CRPs, advocacy organizations and Extended Employment staff drafted a reformed and simplified funding rule, which was implemented on July 1, 1999.

The group made several recommendations that were adopted in the final rule. One recommendation was to maintain a performance-based (outcome-based) funding system with the outcome being based on the hours of work. But all of the performance factors were eliminated. Each provider would be paid the same flat rate per hour of work reported. The only difference in rates paid was the differing rates for supported employment, community employment, and center based employment.

Providers were guaranteed the amount of the subsequent year's contract if they reported enough hours during the current year to earn their contract amount. Each CRP could predict its funding simply by meeting the terms and conditions of its contract.

Another change froze the total funding for center-based employment at the level established for SFY 1999. The total state funding would never increase. Department policy since then has had the effect of freezing a CRP's center-based funding at 1999 levels with some small cost of living increases. Of course, providers can voluntarily reduce center-based funding. Some CRPs have stopped receiving center-based funding, having transferred it to community support funds.

These changes presented a problem. What to do with contract dollars that were not earned or repaid after a program audit? The previous rule dealt with the issue by re-running the performance formulas and requiring payment from "losers" to be redistributed to "winners". This was the most contentious provision of the first funding rule. A return to that method was not acceptable to any of the partners in the rule development process.

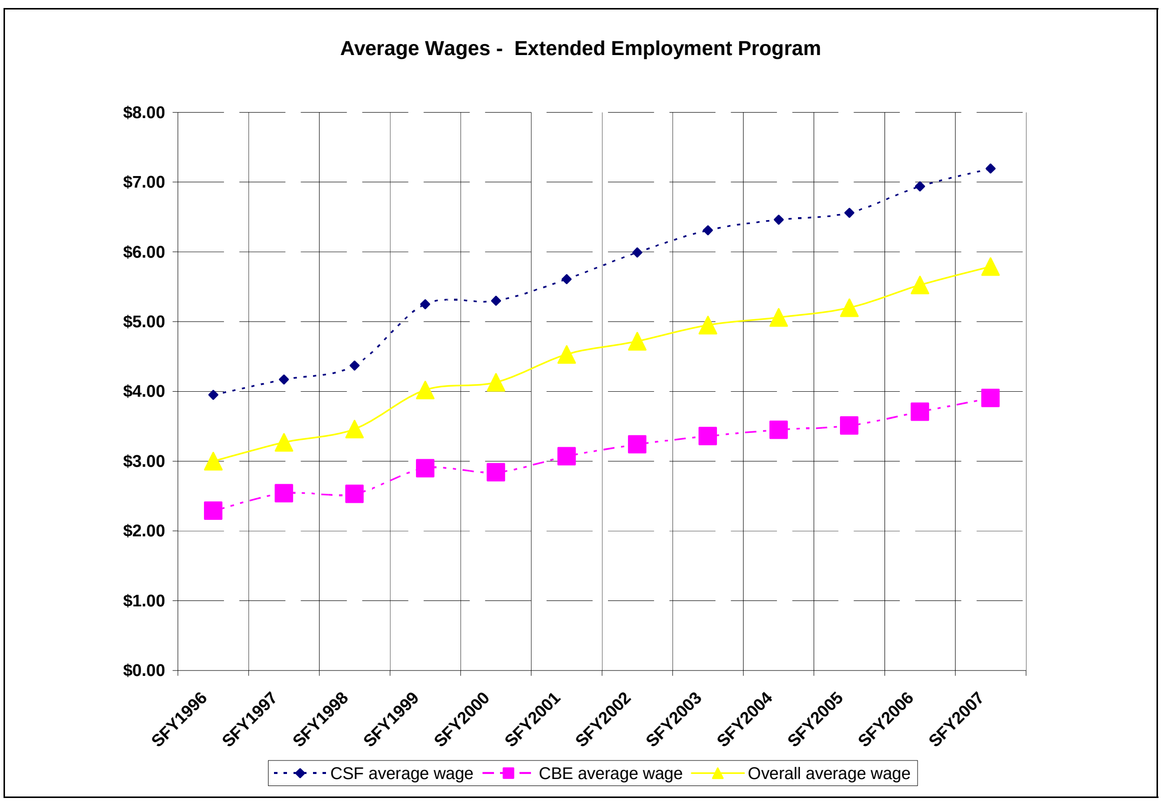
As part of the rule development the department conducted focus groups with extended employees. The primary request from the workers taking part in the groups was for more money. The work group recognized increased wages as a goal for the new funding system, and recommended that unearned and repaid dollars be used to provide a pool to fund an annual "wage incentive."

But what formula should be used to distribute the dollars? Two basic approaches were considered. The first was to use some variant of average wage by facility. This was discarded for two reasons. Rural CRPs felt that wage differentials between the metro and rural regions would put them at a disadvantage. Advocates did not want to distribute the dollars based on a funding system that rewarded sub-minimum wage.

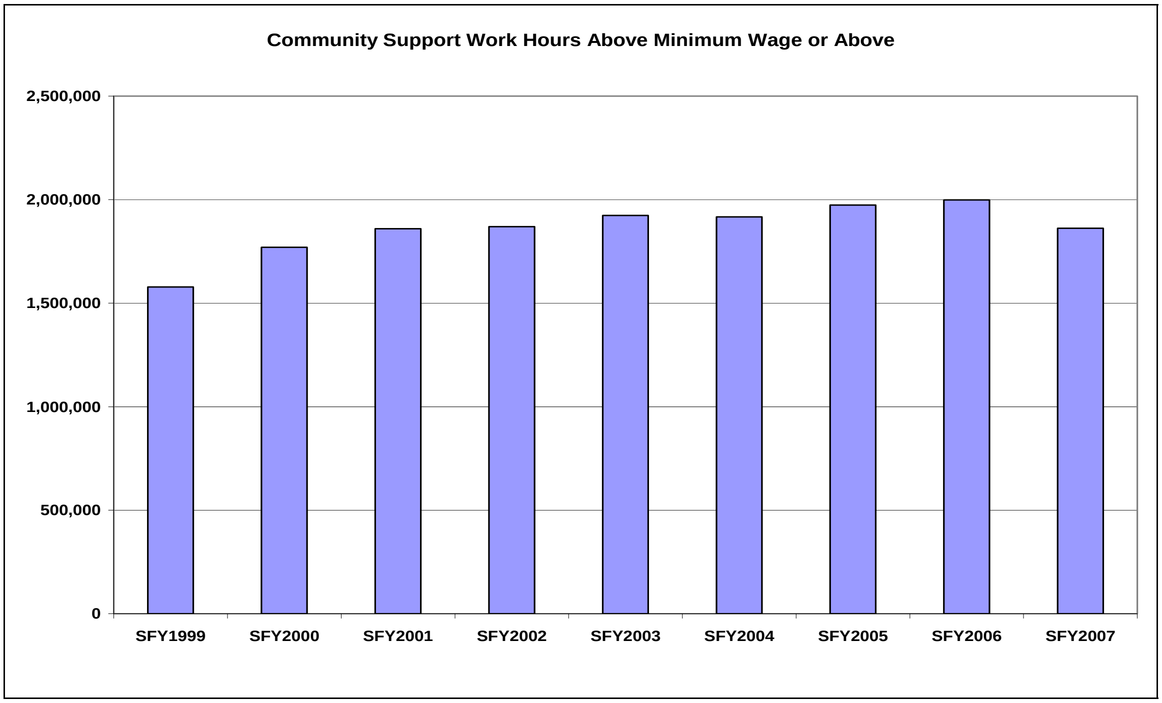
The combination of eliminating sub-minimum wages and no average wage lead to use of hours at or above minimum wage. This minimized the rural-urban differential and provided a proxy for competitive wages. This formed the basis of the current wage incentive system.

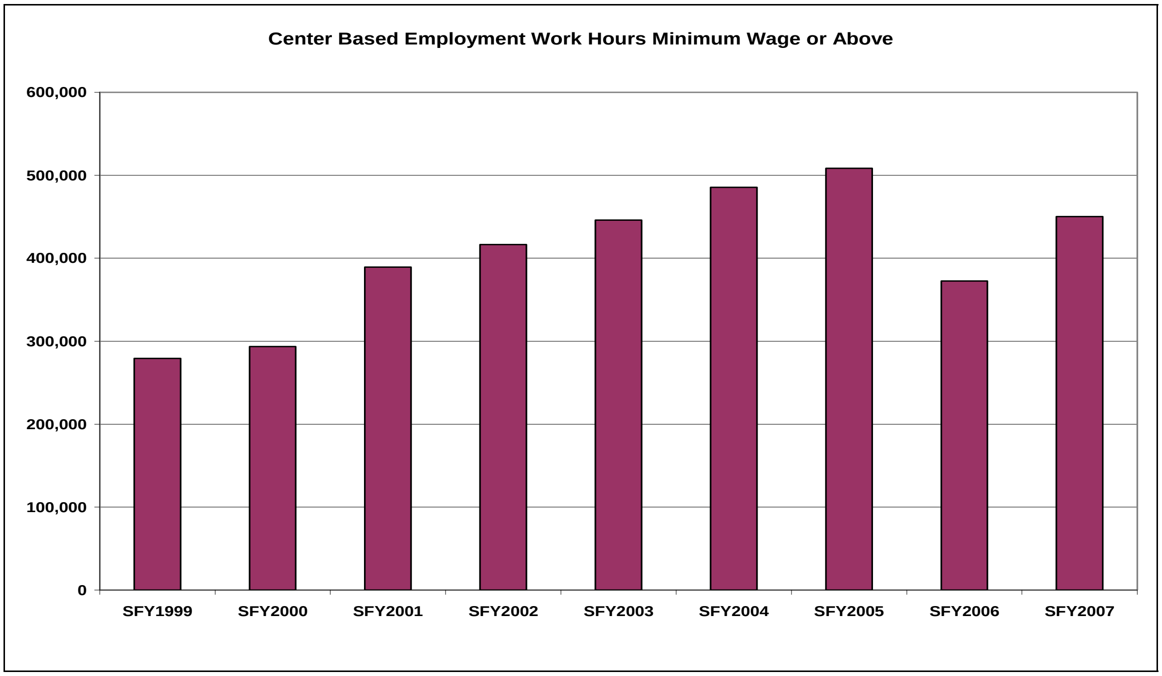
Assessment and Findings of the Wage Incentive

Average wages for extended employees have increased under both versions of the funding rule. Their overall average hourly wage has almost doubled since SFY 1996, moving from $3.00 per hour in SFY 1996 to $5.71 in SFY 2007. As the following chart shows there has been consistent increase in wages paid for both community and center-based programs.

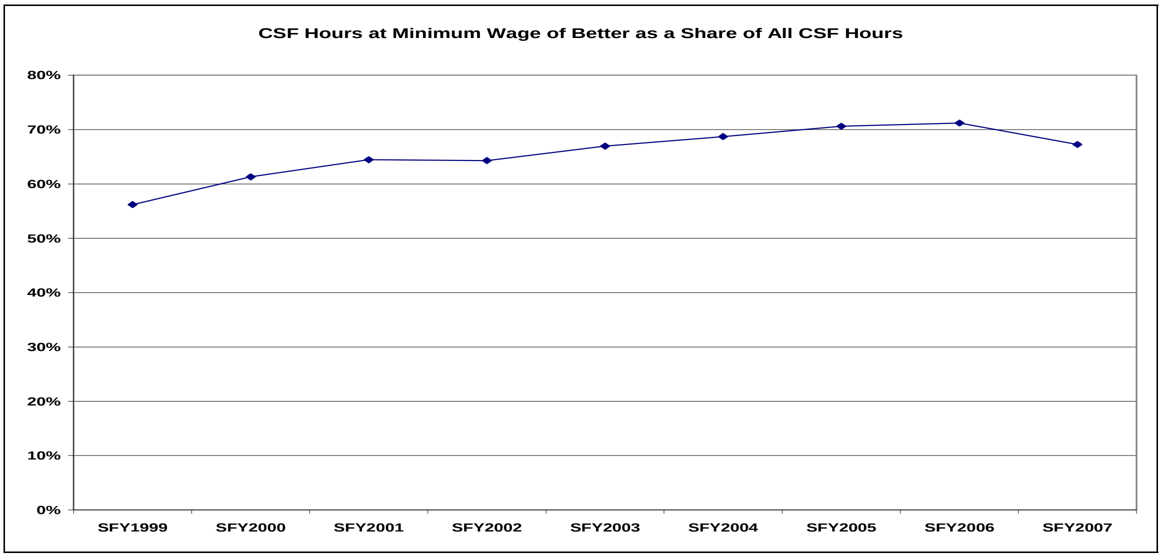


The general question is: How significant is the contribution of the wage incentive provision to the funding rule to this growth? After the implementation of the rule there was an increase in the number of hours worked with wages above minimum wage. CRPs initially reported increased hours for employment both in facilities and in the community. The following two graphs display the history for both types of employment.

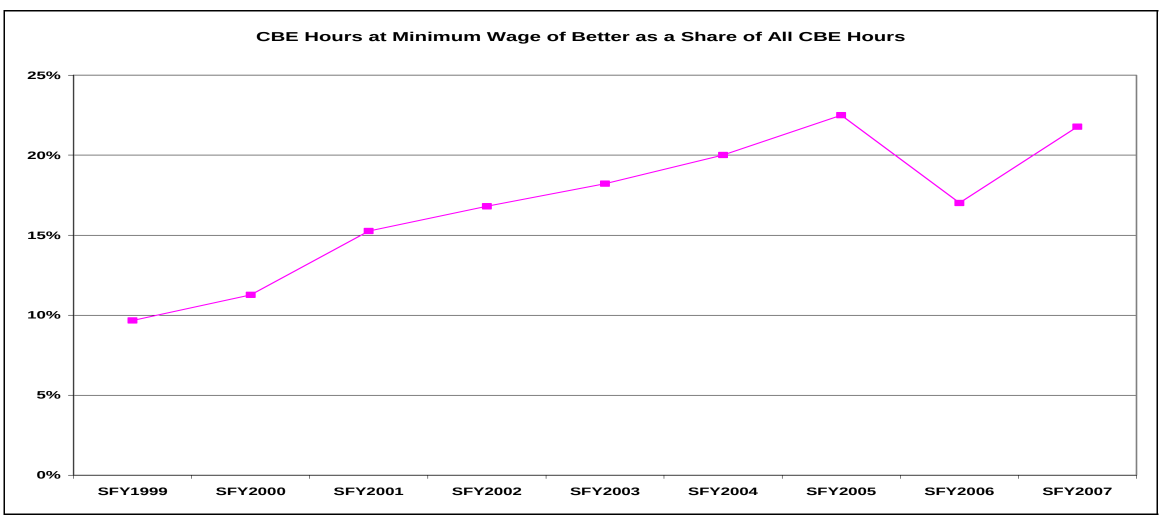




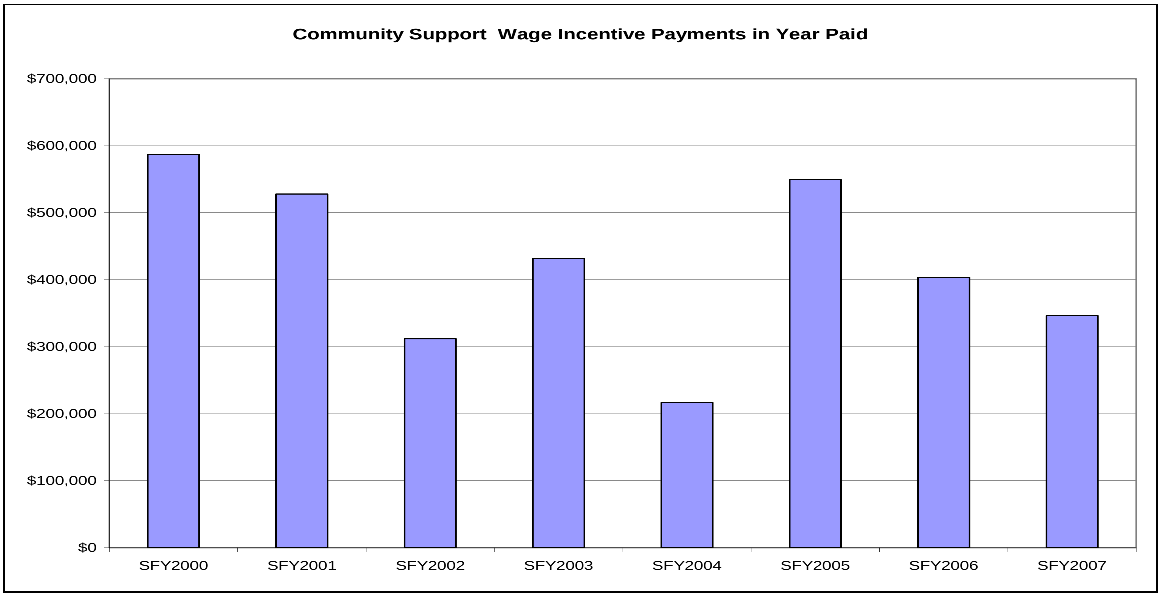
A significantly greater number of hours were reported from employment in the community as compared to center-based employment. Currently CSF reports approximately four times more hours than center-based. The community support fund hours essentially have been static since 2001. However the share of all reported community hours of work that minimum wage or better has gradually but steadily increased during that period. In the past few years around 70 percent of the hours in the community have been at minimum wage. The total number of community hours of work reported to the Extended Employment program has been decreasing slightly during those years. Much of the growth in share of all hours is the effect of the gradual shrinking of the overall hours reported in the Community Support Fund.

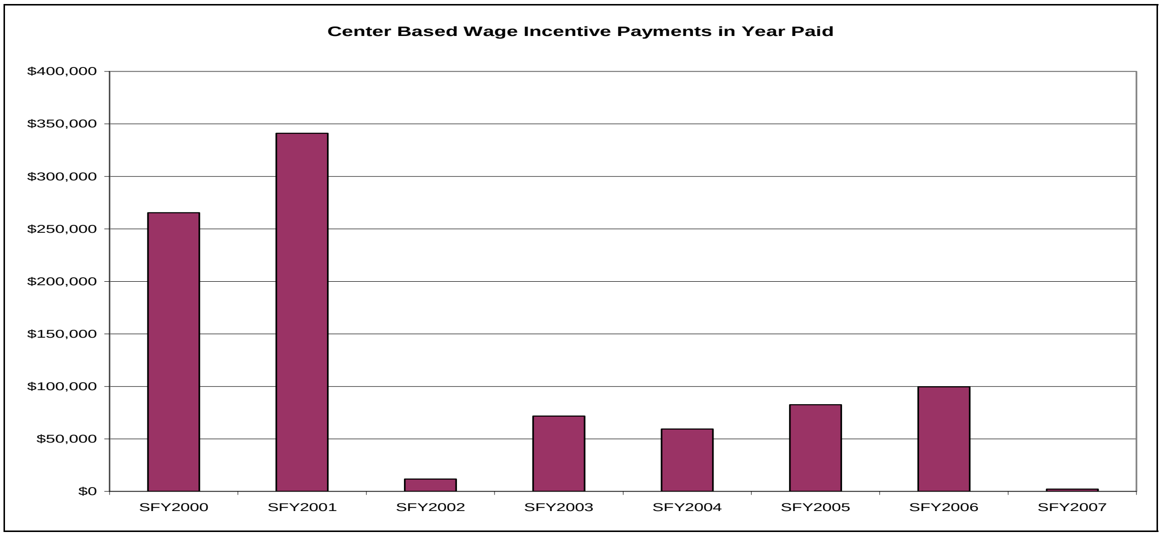


The growth in minimum wage hours paid in facility work has been much more dramatic; the share doubled during that time. The dramatic increase is mostly because the starting base was so low. Even now only one hour in five worked in center-based program is at minimum wage or higher.



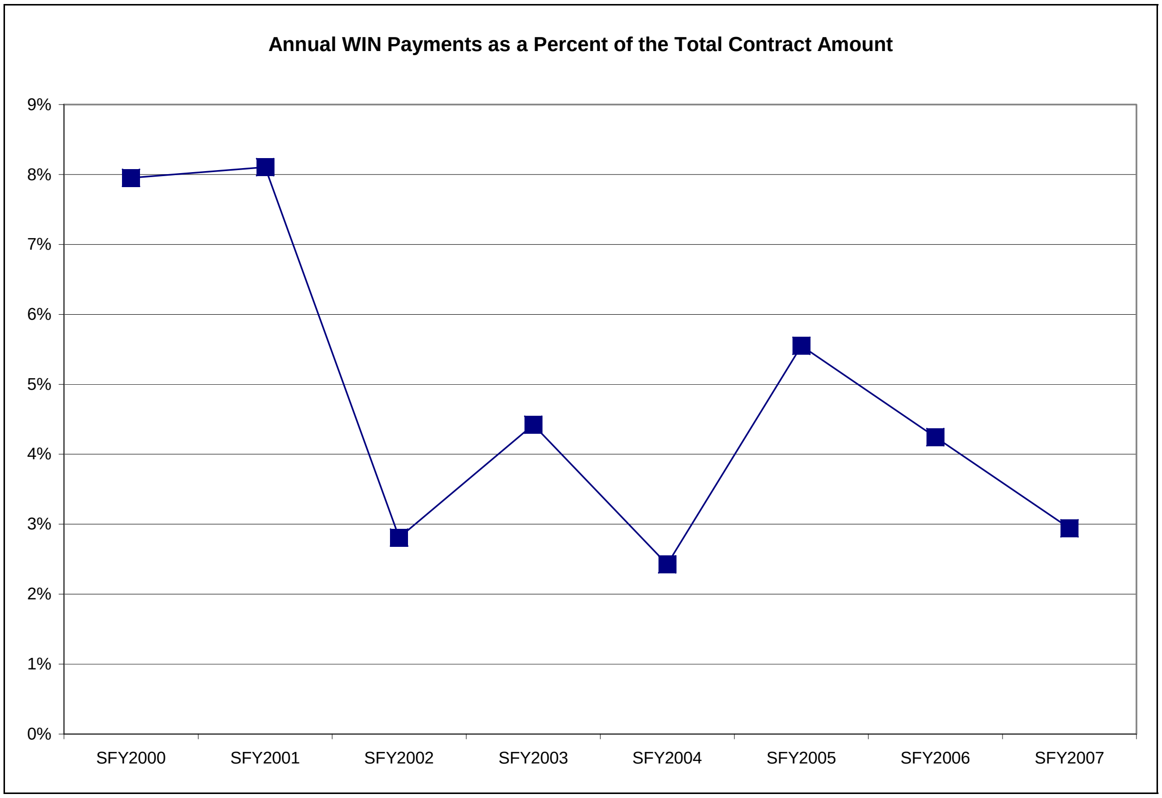
The first incentive payments were made in SFY 2000 based on the unearned and reconciled dollars. The dollars paid by year are shown in the following charts.





Because the funds available for the wage incentive payments depend on CRPs meeting their contract, the number of dollars subsequently paid out varies. The year-to-year variance can be substantial. The greater number of dollars distributed in the SFY 2000 and SFY 2001 was partially the result of the audit and reconciliation dollars collected before the implementation of the rule. The diminished dollars in succeeding years represents close to full production by most CRPs

The next chart shows the share that the WIN funds represent as a percent of the annual appropriation distributed to CRPs.



The share size varies from year to year. When the revised rules were drafted the expectation was that the value of the fund would eventually approach zero. The performance rule reduces program funding if an individual CRP does not meet its contract. The new funding level for the CRP is based on how the CRP actually performed. The new lower funding amount should be achievable. It was assumed that the capacity would go to a program which would be more effective at finding and providing hours of work. Theoretically equilibrium should be achieved among all CRPs meaning no funds would be available. This seems to be the case for center-based employment. The Community Support Fund also seems to be trending downward but it is not clear if a point of equilibrium will be reached.

It is fair to expect that the unearned and returned contract dollars to be used will stay within a range of 0-5 percent in the near future. The current biennial appropriation provides $125,000 annually to fund the community support wage incentive. For SFY 2008 the $125,000 is 1.4 percent of the Community Support Fund value.

Effectiveness of the Wage Incentive

How effective has the wage incentive been in increasing wages? The answer is clouded. Wages have increased, but the number of hours at minimum wage or higher stayed flat, or diminished, after an increase at the beginning of the new funding rule.

Employment at minimum wage is linked to the type of employment. Supported employment requires competitive wages which means the minimum wage is a floor. In

SFY 2006 85 percent of the reported hours in CSF were supported employment; in SFY 2007 the proportion is 82 percent. The drop in hours in CSF from SFY 2006 to SFY 2007 was attributed to fewer hours worked in supported employment. This suggests that a strong driver for minimum wage hours and overall wage increase is the strength of the supported employment program.

The policy of the Extended Employment program has been to encourage supported employment for over two decades. Currently the only new capacity for supported employment is developed through converting capacity from providers who did not earn contracts through an RFP process to new providers. By policy this new capacity is for supported employment only. This moves funding from sub-minimum wage capacity to employment that provides competitive wages. This engine of new supported employment capacity is a significant driver of minimum wage hours.

The Extended Employment rule provides the greatest hourly rate for supported employment. When the COLA rate changes, the greatest increase is for supported employment. The combination of these two policies provides financial incentive. The wage incentive funding supplements regular funding which emphasizes employment in the community. The wage incentive plan is useful to maintaining programs with higher wages, but it is not the primary mover of wage increases; supported employment is.

Center-based employment delivers far fewer hours at minimum wage. And the picture is somewhat distorted in Minnesota by one center-based employer. Since SFY 1999 Minnesota Diversified Industries (MDI), based in Saint Paul, Grand Rapids and Hibbing has reported more than half of the all the minimum wage hours worked in center-based programs. For SFY 2007 MDI reported 59 percent of all minimum wage hours. MDI is able to pay these wages because it bases its employment on dedicated federal contracts under the NISH program. These contracts provide sufficient income to maintain competitive wages.

When MDI hours are subtracted the remaining center-based hours represent about 5 percent of the reported hours. And some of those hours are generated by CRPs with smaller NISH contracts. There seems to be little incentive for minimum wages for most non-NISH employment.

Recommendations

Currently the wage incentive is in rule. Changing it will require rulemaking or legislative change. The rulemaking process would likely take 12 to 18 months from the time the process starts. Rule change likely would not be implemented until July 1, 2009 at the earliest. Rulemaking would encounter the same conditions that drove the first drafting of this provision: how to use unearned dollars effectively and the fairness of proportional distribution of the dollars. It would also have to examine the usefulness of funding non-NISH center-based contracts. Significant changes to the wage incentive process through the rule-making process would be most effective if done in conjunction with a full revision of the funding system which examines and determines the continuing role of sub-minimum wage employment in general.

The recent appropriation dedicates funding to wage incentives for the community support program. The legislative intent is to encourage higher wages using the existing rule. But its funding is of limited effectiveness since, in effect, it is linked to supported employment for most of its success.

If the intent is to increase wages, then a more effective method would be to add capacity for supported employment by increasing appropriations explicitly for that purpose. The current funding model is a zero sum game. Funding for new supported employment comes from sub-minimum wage employment. Since the payment rate for supported employment is greater than community employment or center-based employment, transferring current dollars from these programs to supported employment buys fewer hours of work but offers higher pay.