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# New York State and Mid-Hudson Valley Nonprofits: The Impacts of Late Contract Payments

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NEW YORK STATE AND MID-HUDSON VALLEY  
NONPROFITS: THE IMPACTS OF LATE CONTRACT  
PAYMENTS

BY

JODI FERNANDES

SUBMITTED IN PARTIAL FULFILLMENT OF  
REQUIREMENTS FOR THE DEGREE OF MASTER OF  
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Thank you all.

## **Introduction**

Government and nonprofit partnerships have existed in the United States as far back as colonial times (Young, 2006, p. 56). In more recent U. S. history, government support of nonprofit organizations increased greatly in the 1960's due to expansion of federal programs for social services, such as Medicare and Medicaid, community action agencies, neighborhood health centers, child protection agencies and through the 1967 Amendments to the Social Security Act (Smith, 2006; Young, 2006). This trend continued in 1974 with the passage of Title XX of the Social Security Act, also known as the Social Services Block grant, which encouraged states to contract with nonprofit organizations (Ferris, 1993, p. 364). Government financial support of nonprofits grew in the 1980's and 1990's in part due to the following developments: 1) the use of Medicaid to support social services, 2) new federal programs for children and youth, such as the National Children, Youth, and Families at Risk (CYFAR) Program, 3) welfare reform legislation providing funds for job training, and 4) new innovations in the form of federal financing, such as tax credits and loans (Smith, 2002).

As these few points illustrate, the partnerships between government and nonprofit organizations have been and continue to be greatly affected by changes in policy. Economic factors also play an important role in the relationship between governments and nonprofits. The priorities of the government will inevitably change depending on the economic climate which will then determine availability of funds to be allocated for government-funded programs, as has been the case in the recent economic downturn. For example, in an effort to respond to the economic crisis, Congress passed the American Recovery and Reinvestment Act of 2009, which lists the following goals: creating new jobs and saving existing ones, spurring economic activity and investing in long-

term growth and fostering unprecedented levels of accountability and transparency in government spending (Public Law 111-5 2009). In some cases changes in priorities such as these will bring more short-term money for certain programs, such as the TANF (Temporary Assistance for Needy Families) program, created under the welfare reform legislation of 1996, which has received money through the American Recovery and Reinvestment Act in the form of the TANF Emergency Fund. This fund will distribute \$5 billion to states through September 30, 2010 for increased spending in specified program areas, which includes nonprofit organizations. This is just one example of how a shift in government spending can have an effect on the nonprofit sector (Smith 2006).

There are many reasons why government chooses to outsource to nonprofit organizations, especially in the area of human services and healthcare. In many cases these organizations already have an established, trusted relationship within a community and therefore are in a better position to respond effectively to that community's needs. A nonprofit organization is more flexible than a state government which can prove invaluable when it comes to providing for the essential needs of a community, especially during trying economic times. Governments may also turn to nonprofits due to their expertise and proven track record in a particular field. Cost savings to the government are also a consideration, especially in the area of personnel.

The State of New York had about 31,000 active contracts with nonprofit organizations as of June 2009, according to the Office of the State Comptroller (OSC, 2010). These contracts make up a significant portion of the budget for many of those organizations. As outlined in a recent report by the Congressional Research Service, grants and payments from the government (state and federal) are the second largest source of revenue for nonprofits (Sherlock and Gravelle, 2009). This same report further distinguishes among the sectors within the nonprofit world to show that the healthcare and

human services sectors receive the most funding through government contracts at 37% and 36% of budget respectively. The organizations in these sectors provide essential services to the communities in which they reside. Another recent survey of nonprofit organizations nationwide, conducted by the Nonprofit Finance Fund in 2009, found that 91% of the nonprofits defined as providing essential services serve vulnerable populations and 93% of those organizations saw increased demand for services during that year (NFF, 2009).

Nonprofits in New York State are also experiencing increases in demand for services in the current economic crisis, as outlined in a report on the sector released by the Office of the State Comptroller in January 2010. Additionally, this report states due to the economic crisis nonprofits are experiencing decreases in all types of fundraising and the state budget deficits are causing contract delays and late payments. According to a report by the Office of the State Comptroller in May 2009, 87% of state contracts with nonprofits were approved late (OSC, 2009).

A survey of nonprofit organizations in New York State, conducted by the New York Council of Nonprofits for the State Comptroller's Office early this year found that 66% of respondents had to borrow money because of delayed government contracts and/or payments during the last two years. The response rate of the nonprofits to that survey was swift, according to a NYCON press release, with about 200 responses received within 24 hours of the survey being sent out. The respondents also submitted over 100 comments to the Comptroller's Office on the issue of late contract payments explaining how the situation was affecting their organization. The resulting situations they described ranged from lay-offs to taking lines of credit with banks to having to close their doors. The response of these organizations to this survey, and their comments, help illustrate the seriousness of the issue of late contract payments.



States are facing serious budget deficits with a very slow recovery projected. As a result the issue of late contract payments will continue to be a serious national problem affecting nonprofits in every state. Meanwhile the needs of the children and families that depend on these nonprofits will still have to be met. Clara Miller, President and CEO of the Nonprofit Finance Fund, says of the current situation, "We expect 2010 to be another treacherous year for many nonprofits that routinely take heroic measures to meet demand for services. While the 'coping mechanisms' we're seeing are encouraging, we also need to make fundamental changes to the way the sector is financed" (Nonprofit Finance Fund, Press Release 3/22/10).

There are indications that the problems being faced by the nonprofit sector in relation to a growing dependence on government funding, such as contracts, are beginning to be heard. In New York State, for example, the State Comptroller has pledged his commitment to assisting the nonprofit sector and working together to improve the current situation. To that end he has been conducting forums and meetings with nonprofits across New York State to discuss possible solutions. In November 2009, The Urban Institute received a grant from the Bill and Melinda Gates Foundation to support a research and advocacy project around the impact of government contracting policies and practices in the nonprofit sector. Part of that research includes a national survey by The Center on Nonprofits and Philanthropy at the Urban Institute and the National Council that was sent in March of this year to explore how nonprofits are being impacted by late payments and other contracting issues. The project also aims to develop strategies for reform of current contracting processes. As the awarding of this grant indicates, this is an important issue which is on the mind of all nonprofits that have contracts with state and federal governments. Solutions need to be found to alleviate the situation in the near and long term to ensure continued support of the essential services they provide.

The purpose of this research will be to examine the impact of the late payment issue on nonprofits that have multiple contracts with different state agencies in the Mid-Hudson Valley of New York. This research will also provide some analysis and comparison into the reason for the late payments by looking at the experiences of these organizations with their contracting agencies. In looking at the impact of late payments on the nonprofits the research will focus on two main questions:

- How does the organization deal with the shortfall caused by the late payments?
  - What are the short term consequences of their decision?
  - What are the long-term consequences of their decision?
  
- What is the cost to the nonprofit?
  - What do they defer?
  - How are the populations they serve affected?

To examine the reason for the late payments this research will focus on the following question:

- What are the differences in contracting processes, if any, between the various funding agencies?
  - Are some more efficient than others?
  - What are the factors that influence these differences?
  - Have laws in New York State meant to alleviate late contract payments made a difference?

## **Review of the Literature**

As described above, late government contract payments are a current issue affecting nonprofits across the country; however, the issue is not new, as an article by David Grossman from 1992 illustrates. He describes how the State of New York relies on nonprofits to deliver a wide variety of public services. He goes on to say that state and local governments choose to contract with nonprofit organizations for their expertise, community knowledge and cost savings. Nonprofits also benefit from the contract arrangement, Grossman writes, as they receive the financial support they need to fulfill their missions. He goes on to describe New York State's contracting history with nonprofits and then explains two issues involving cash flow that caused problems with the contracting process: slow turnaround time on vouchers submitted for payment and delays in approving contracts. He describes how New York State dealt with these problems by outlining the history that led to two laws meant to improve the situation: the Prompt Payment Law, enacted in 1984, and the Prompt Contracting Law, adopted in 1991. He concluded that the Prompt Payment Law had resulted in state agencies improving internal procedures and improving staff levels to reduce voucher processing time. The Prompt Contracting Law had been in effect only a short time when Grossman's article was published so he was unable to conclude if the new law was having its intended effects. However he did feel that the legislative debates and work that led to the law clearly established that the state was committed to improving its administration of the contracts with the nonprofits and that in light of the law's imposing interest penalties on late contract payments that state agencies were respecting the time targets put in place for contract award. He ultimately concluded that it remained to be seen if the new laws would really make a difference in New York State's contracting practices with nonprofit organizations.

Late payments on contracts are not unique to New York State, as evidenced by reports from other states, such as Illinois. A joint study by the Illinois Facilities Fund and Donors Forum of Chicago took an in-depth look at the financial health of that state's nonprofit sector issuing their final report in December of 1998. One result of that study was the creation of a publication resource for nonprofits called the Capacity-Building Digest series. The fifth issue in that series, published in 2000, is entitled *Costs of late government payments*. As in many other states, including New York, Illinois relies heavily on nonprofits to be service providers, especially in the human services sector. The publication describes how changes in government policies concerning outsourcing have caused serious cash flow problems, namely in moving from a contract model, where the nonprofit would receive some funds up-front and then would receive monthly installments, to a fee-for-service model where the nonprofit bills the government for services already rendered. This new business model has created serious cash flow problems for the nonprofits whose largest revenue source is the government.

The 1998 study mentioned earlier found that state grants and contracts constitute 50.3% of all revenue for Illinois nonprofits and that “there is a direct relationship between the level of government funding and the presence of cash flow problems” (IFF, 2000, p.1 ). Through interviews conducted with the management of fourteen nonprofit organizations in the human services sector, the report outlines the strategies they have employed to meet the challenges created by late government payments.

Three categories emerged from the strategies discussed: systems, cash and credit. Establishing good financial systems within the organization, creating cash reserves through other fundraising efforts and having a line of credit with a bank all proved helpful when dealing with the

effects of late government payments (IFF, 2000, p. 10). This publication identifies two other less obvious effects of the late payments. The first is opportunity costs, which are difficult to assign a dollar amount to, but cannot be left out of this discussion. Opportunity costs represent "...the earnings or other benefit that might have been obtained if the cash had been applied to an alternative use..." (IFF, 2000, p. 8), in this case, to cover the amount of cash lacking due to the late payments. The second is the cost to government in that their relationships with these nonprofits will be strained and the nonprofit sector which they rely on to deliver these services will become less able to meet the needs of the community in a timely manner (IFF, 2000, p. 9).

The State of Connecticut is also dealing with the issue of late contract payments to its nonprofit providers. A report prepared in May 2009 details the effects of this trend on the nonprofits in that state. The Connecticut Association of Nonprofits surveyed 500 of its members to determine the effects of the financial downturn, with the focus of the survey being government funding and timely contract payments (Andrews, 2009). This report identified which state agencies have contracts with the nonprofits that responded to the survey and further identified the number of nonprofits that have experienced late payments by each of those agencies.

The nonprofits in Connecticut, as in New York and Illinois, are left with a cash deficit and a challenge to continue to meet the needs of their community as a direct result of these late payments. The cash deficit coupled with the economic downturn, which has decreased other sources of funding, has led the nonprofits in Connecticut to resort to such measures as reducing staff, cutting employee benefits, eliminating some programs, reducing operating hours and increasing their fees. As in the case of Illinois nonprofits, some in Connecticut are relying more heavily on lines of credit with a

bank to make up the cash shortfall, usually to support operating and program costs and salary and benefits for their employees.

The report concluded that the organizations that are experiencing late payments are put at risk, with the community suffering the most from lack of timely services. It also makes the important point that these organizations provide services on behalf of the state at great savings to the state and “should not wait to be paid” (Andrews, 2009).

Michigan is another state with reports out about the state of its nonprofit organizations. Earlier this year, the Michigan Nonprofit Association and the Johnson Center at Grand Valley State University conducted a survey of over 200 nonprofits in that state to see how the economic crisis is impacting their operations. Among other results, the survey found that 45% of nonprofits who receive government funding were experiencing late contract payments (Miller, 2010a, p. 1). As in Connecticut, nonprofits in Michigan were dealing with the decrease in cash flow due to late contract payments by letting staff go, cutting back on program services, and reducing employee benefits (Miller, 2010a, p. 4).

To look more closely at the January survey’s finding that 45 % of nonprofits were experiencing late government payments a follow-up survey was conducted in April. This survey focused on all levels of government funding, with 26% of respondents reporting their state contracts were received late. Of the state agencies in contract with nonprofits the largest funder is the Department of Human Services which was also determined to be the agency that was having the most difficulty making timely payments to its nonprofit service providers. This report concluded that this is a particularly challenging time for nonprofits in Michigan with increased demand for services as

well as state budget problems making it difficult to meet the immediate needs of children and families (Miller, 2010b, p. 3).

The Alliance for Children and Families and United Neighborhood Centers of America conducted a survey of their members across the country in April of 2009 looking specifically at the delayed government contract payment issue. They received responses from 96 nonprofit organizations in the human services field in 30 states (Winder, 2009). Of those 30 states, 19 responded that nonprofits in their states were experiencing late contract payments and, as a result, reduced cash flow. As other studies also found, many of these organizations were forced to reduce staff, cut programming and apply for bank loans to cover the shortfall. The report went on to give a state-by-state summary of the comments they received describing the resulting effects of this issue.

The Urban Institute's Center on Nonprofits and Philanthropy and the National Council of Nonprofits have joined forces, with funding from the Bill & Melinda Gates Foundation, on a project which aims to take a broad look at the government-nonprofit contracting relationship across the nation and to propose ways to improve these important relationships (Boris, de Leon, Roeger, & Nikolova, 2010). The first phase of the project was a nationwide survey of human service nonprofit organizations which have contracts with federal, state and/or local governments. The results of the study were released on October 7, 2010.

The survey was completed by 2,153 organizations nationwide with government contracts and grants. It gathered data on the impact of the recession on these organizations, details about the organization's government funding and contracting, contracting problems, issues surrounding accountability and reporting, and some information on the finances of these organizations.

The findings of this extensive survey provide important insights into the government-nonprofit contracting relationship. The survey results revealed that of all the revenue sources for human service organizations the largest for three out five nonprofits is government contracts or grants and state funding in particular is the largest source for two in five organizations (Boris et al., 2010).

On the issue of contracting problems, the authors describe five problems areas that arose from their research into the literature and media reports: 1) Payments that do not cover the full cost of contracted services; 2) Complex and time-consuming reporting requirements; 3) Complex and time-consuming application requirements; 4) Changes made to contracts and grants; and 5) Late payments on contracts (Boris, et al., p.12, 2010).

Late payments from government contracts were a problem for 53% of the organizations responding to the survey, and of that percentage, one in four defined late payments as a “big problem” (Boris, et al., p. 15, 2010). Additional results show that of all the levels of government, states were the most late, often as much as at least 90 days late in making contract payments. Late payments, the authors found, place a large burden on the budgets of these organizations which in turn affects their ability to provide services.

The authors also report on the recent recession’s effect on revenues for these nonprofit organizations. Through the survey, Boris et al., discovered that revenue shortfalls in organization’s with existing contracting problems were made worse by the recession causing them to make programmatic and personnel cutbacks (p. 19, 2010).

The authors conclude that the effects on these nonprofit organizations caused by the ongoing problems with government contracts and grants combined with the recent recession may take years to



repair, if ever (Boris et al., p. 24, 2010). They argue that "...better government management of contracts and grants can at least avoid adding to nonprofits' financial stress" (Boris et al., p.1, 2010).

The National Council of Nonprofits issued a special report entitled, "Costs, Complexification and Crisis: Government's Human Services Contracting "System" Hurts Everyone," in conjunction with the release of the Urban Institute's study. The Council's special report adds perspective to the survey's findings and expands on the issue of government and nonprofit contracting problems.

Through its research, the Council reports that the contracting system as it currently exists is inadequate and poses great threats to its nonprofits partners and the communities they serve. They detail how the system in its current form hurts the people in need, taxpayers, employees of the nonprofits, nonprofits that do not contract with government, and other funding sources such as private foundations. In addition, they make the argument that there are many additional ways the current contracting system negatively affects the wider economy. One example of this is that outside private vendors are not working with these nonprofits as they used to because the nonprofits are experiencing cash flow problems due to the late contract payments with their government partners (National Council of Nonprofits, p. 8, 2010). Through this and other examples, the Council effectively describes the domino effect these contracting problems are having on communities around the country.

The Council goes on to describe the five problem areas of the nonprofit – government contracting relationship, including late contract payments, which were initially outlined by the Urban Institute study. In this report, on the issue of late payments, the Council reasons that by paying late on contracts, governments are essentially using that money as free financing (National Council of Nonprofits, p. 15, 2010).

In conclusion of their report, the Council suggests a plan to reach a “win-win” solution for everyone (National Council of Nonprofits, p. 25, 2010). They include action items for each level of government, for the nonprofits, for other funders, and for citizens intended to improve the situation.

The reports in this literature review are telling much the same story. Nonprofits with government contracts in New York State and in many other states across the country are not getting the payments owed them in a timely manner. While this issue may not be new to the government–nonprofit relationship, the severity of the problem has been exacerbated by the current economic climate which is decreasing funds from private donations and leaving many states with serious budget crises. Beyond the obvious cash flow problem, the late contract payments are eroding the relationship between nonprofits and government. The nonprofits are also less able to meet the needs of their constituents at a time of increased need. Solutions to this growing problem are not clear. What is clear is that these much-relied on organizations are facing serious challenges. The survey report released by the Nonprofit Finance Fund summarizes the situation quite well: “America’s nonprofits, including the ‘lifeline’ organizations that many depend on for food, shelter, and other basic services, are strained to the breaking point,” (NFF, 2009).

The recent release of the Urban Institute study and the report issued by the National Council on Nonprofits brings to light on a national level the seriousness of the problems governments and nonprofits are experiencing in their partnerships. Late contract payments have been identified as just one of several issues that need to be addressed. While solutions to these problems are not clear, these reports and the ongoing work of the Urban Institute and the National Council on Nonprofits are a good first step in a new direction that will hopefully bring about positive change.

## **Methodology**

In order to examine the impact of late contract payments on nonprofits in the Mid-Hudson Valley, an empirical study of nonprofits in the Mid-Hudson Valley area in the human services field which have multiple contracts with more than one state agency was conducted. The Mid-Hudson Valley consists of Columbia, Dutchess, Greene, Orange, Putnam, Sullivan and Ulster counties.

The population was identified with the help of the New York Council on Nonprofits, utilizing their member database as well as their extensive knowledge of the nonprofit sector in New York State, in addition to the Urban Institute's National Center on Charitable Statistics database.

To gather the data necessary to properly assess the impact of late contract payments, this research utilized a survey and a follow-up email question with some of the survey respondents. The questionnaire was prepared and the survey conducted using the on-line software, Survey Monkey. The questionnaire was comprised of a combination of closed-ended and open-ended questions in attempts to get a clear sense of the impact of the late payment issue on the organizations. There were also multiple choice questions. The survey questions can be found in Appendix A. A pre-test of the survey was conducted in advance and taken by four people. No changes were made to the survey as a result of the pre-test. The link to the online survey was sent by email to the individuals at the identified nonprofit organizations, responses were tracked and one reminder email message was sent after two weeks of the survey being distributed. The survey remained open for four weeks. All respondents were assured of their anonymity. One follow-up question was sent to a randomly selected sample of the population which took the survey.

The chosen method for carrying out this research was best to obtain the data necessary to examine the impact of late contract payments on nonprofits. The research was seeking information about the direct experiences these organizations are having with the contracting agencies and this was best gathered through a survey questionnaire. Additional data was obtained through a follow-up email. Weaknesses of this chosen method included the possibility of a low response rate to the survey thus potentially leaving the research results with low external validity.

## **Findings**

Fifty-four nonprofit organizations in the Mid-Hudson Valley were contacted by email with a request to take the survey. Twenty-six organizations did not respond and ten responded that they did not currently have contracts with New York State and as such would not fit the parameters of the study. Eighteen organizations responded that they would be willing to complete the survey. Of the eighteen surveys sent thirteen were completed. One started the survey but did not complete it because they receive their money from the state through a county agency.

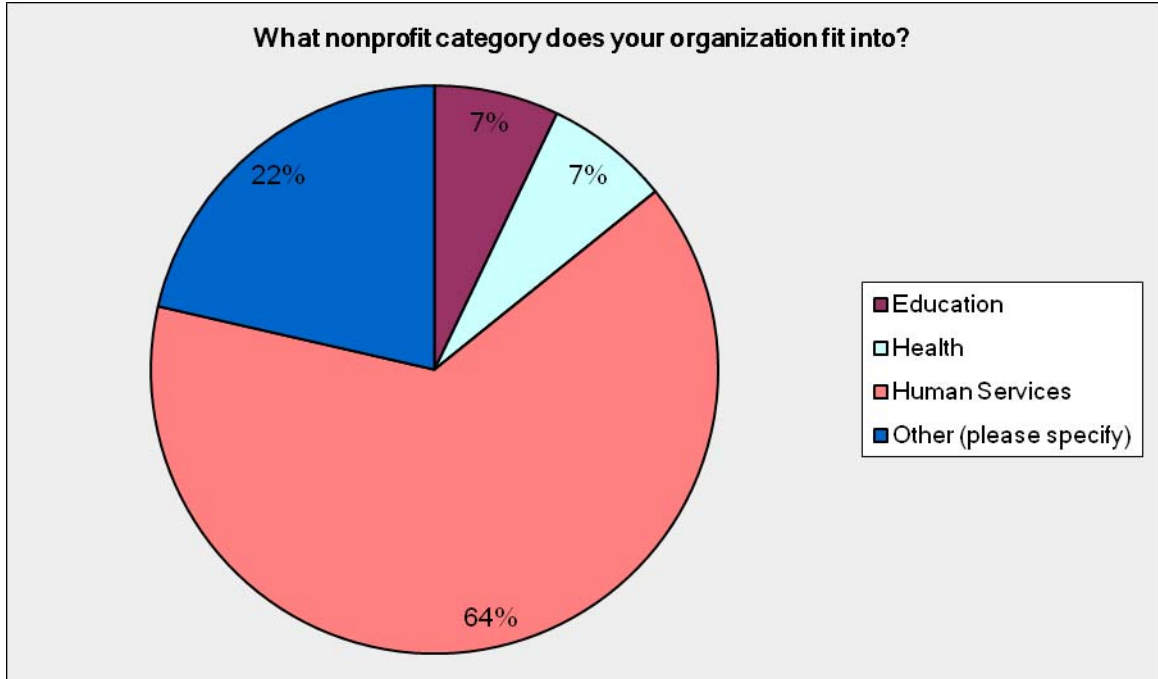
One follow-up question was sent to ten of the eighteen organizations which had agreed to complete the survey. Nine of the ten organizations replied to the follow-up question.

The survey had three sections:

- 1) Questions 1 through 8 focused on demographics and organizational information.
- 2) Questions 9 through 16 dealt with contracts and contracting agencies.
- 3) Questions 17 through 21 asked about planning and outlook for the future.

The organizations who responded to the survey fell into the following nonprofit categories:

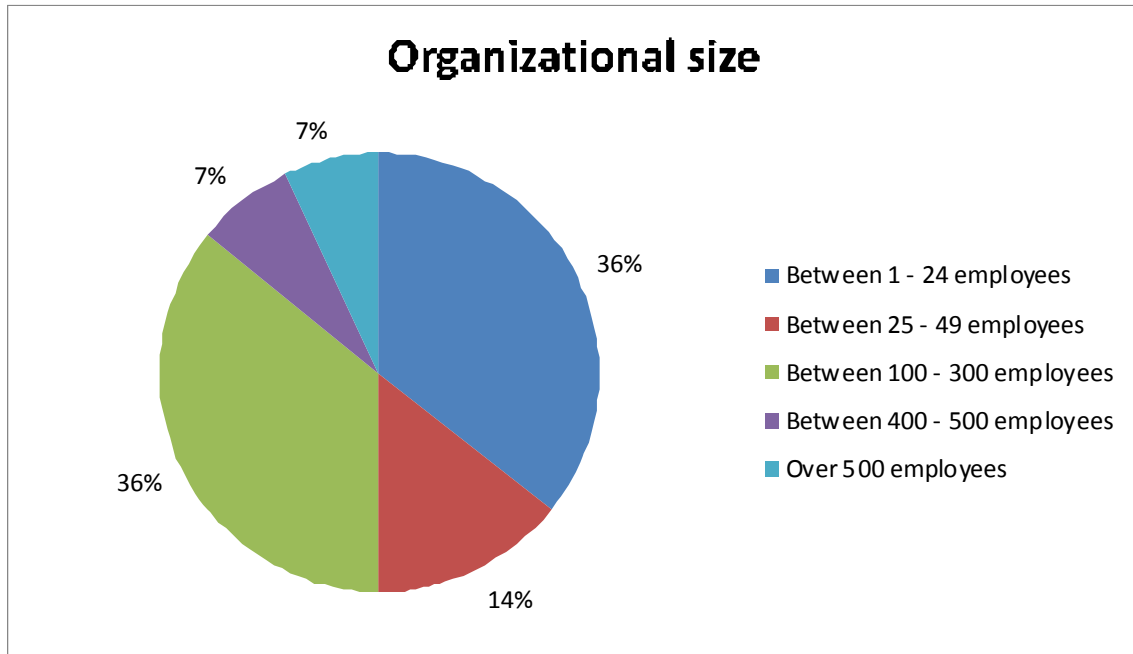
*FIGURE 1: Nonprofit categories*



Human services organizations were the largest category of survey respondents at 64%, followed by 'Other' with 22% of the respondents falling into that category. The three respondents which put themselves in the 'Other' category described their organizations as 1) housing, 2) healthcare workforce development, and 3) prevention education and counseling. Education and health organizations made up 7% each of the remaining organizations who responded to the survey.

The size of the organizations responding to the survey in terms of the number of employees is as follows:

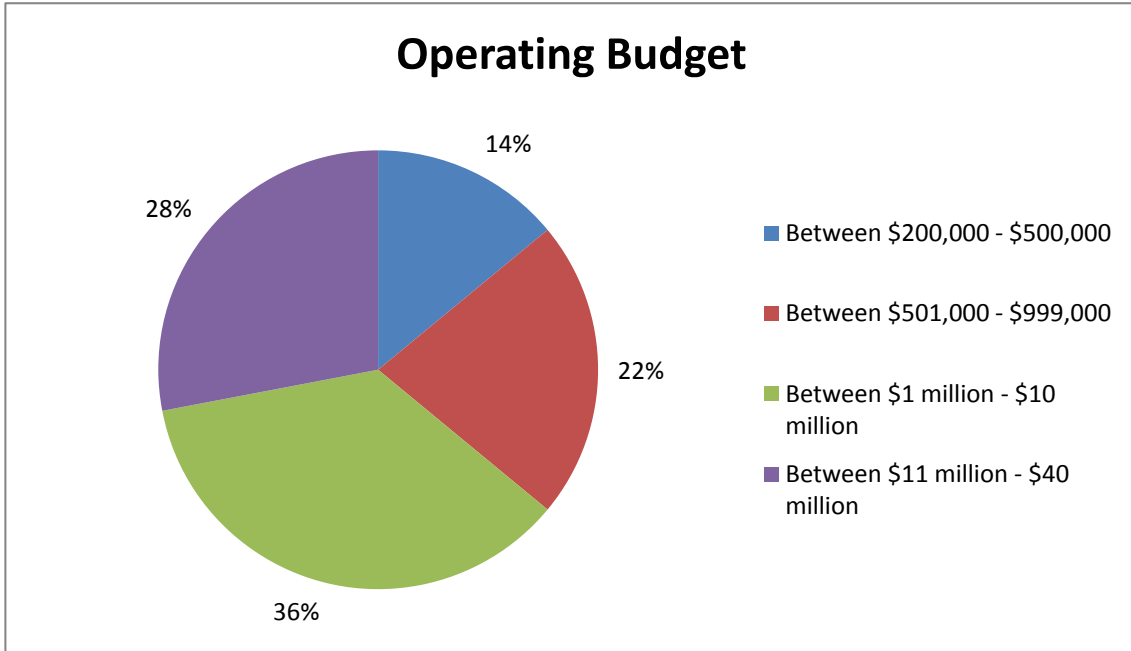
*FIGURE 2: Organizational size*



Organizations employing between 1-24 employees and 100 – 300 employees made up most of the survey respondents at 36% each. Organizations with between 25 – 49 employees made up 14% of respondents, while larger organizations, between 400 – 500 employees and over 500 employees, were the smallest percentage of respondents at 7% of the total each.

The organizations fell in to the following ranges of size of operating budget:

*FIGURE 3: Size of operating budget*

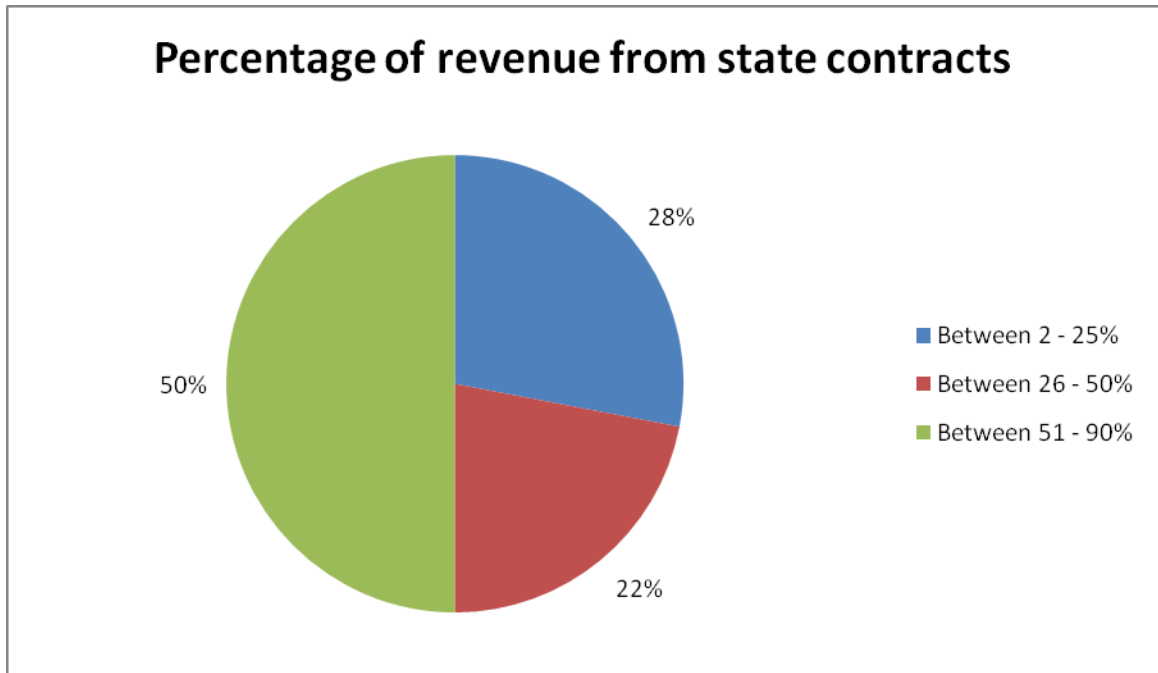


Most of the organizations who participated in the survey have operating budgets between \$1 million - \$10 million at 36% of survey respondents. Organizations with an operating budget between \$11 million - \$40 million made up 28% of respondents, with 22% of the organizations falling into the range of \$501,000 - \$999,000 and 14% with operating budgets in the range of \$200,000 - \$500,000.



When asked what percentage of their revenue comes from contracts with New York State, the organizations' responses fell into the following ranges:

*FIGURE 4: Revenue from state contracts*



Of the organizations who responded to this survey, half receive between 51 – 90% of their revenue from state contracts. Organizations with between 26-50% of their revenue coming from state contracts made up 22% of the respondents and 28% of respondents receive between 2 – 25% of their revenue from state contracts.

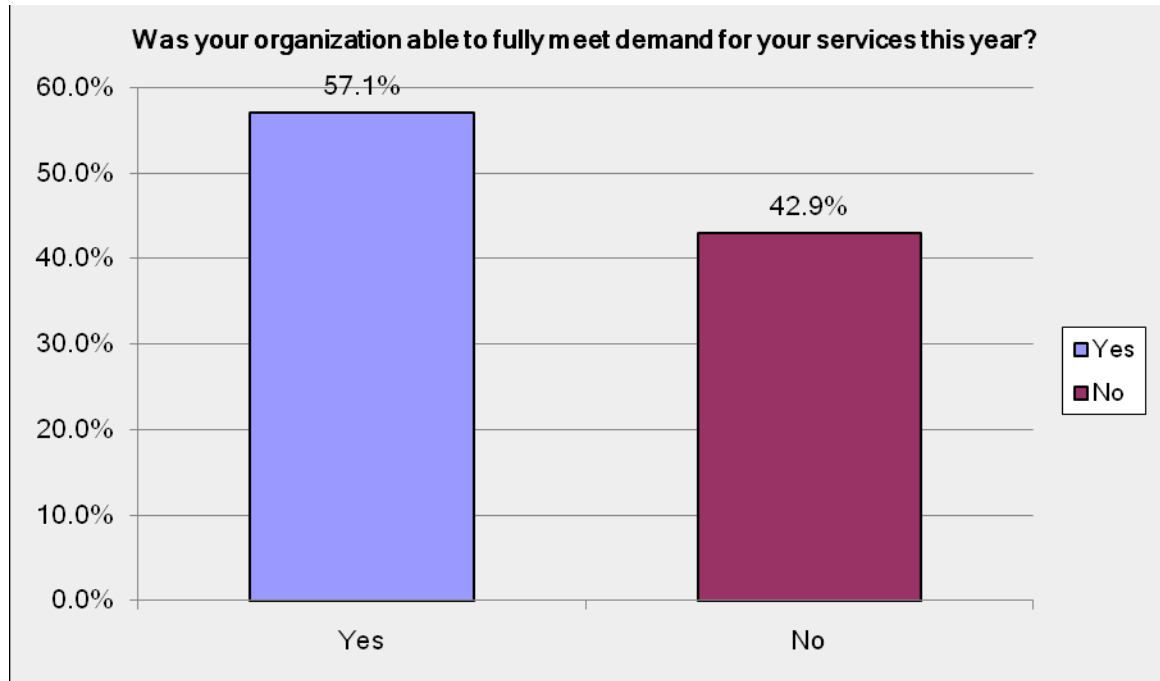
All of the organizations responded that the services they provide are considered critical to people in need. The organizations responses to two questions regarding the need for their services and their ability to meet that demand are presented in the following two charts:

FIGURE 5: Demand for services



More than half of the organizations in this survey report a significant increase in the demand for their services this year, while just over 40% report a slight increase in demand. No organizations reported a decrease or no change in demand for services.

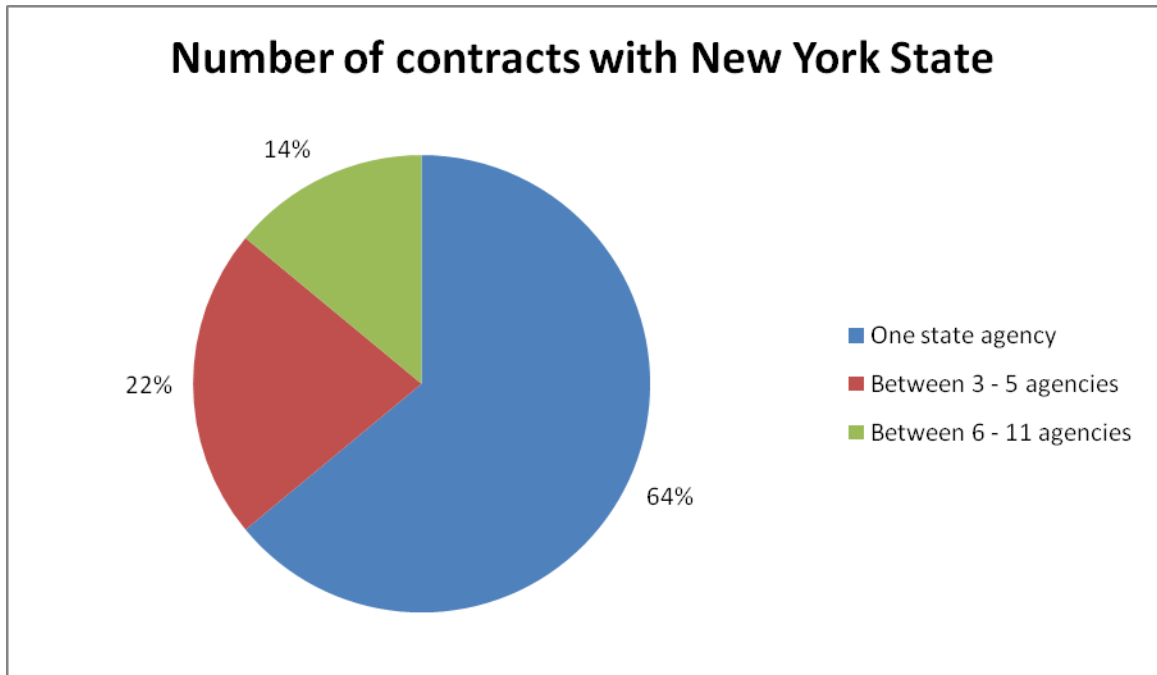
*FIGURE 6: Ability to meet demand for services*



More than half of responding organizations reported that they were able to fully meet demand for their services this year, while just over 40% reported they were not able to fully meet demand for their services.

Next the organizations were asked with how many state agencies they have contracts with:

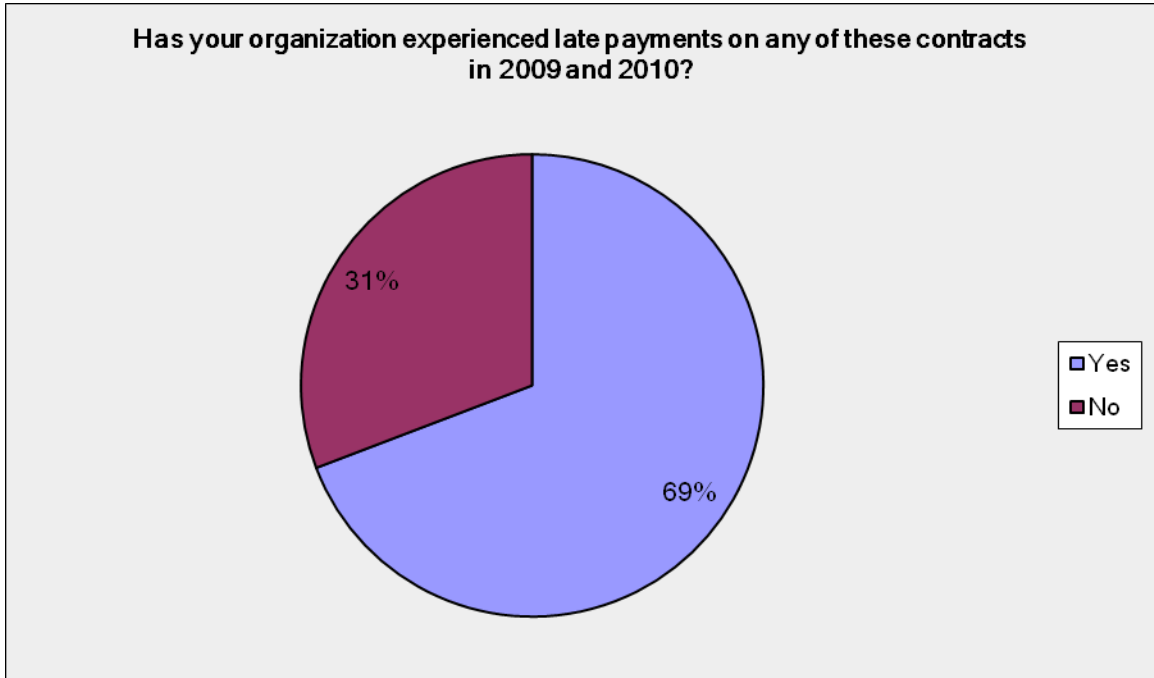
*FIGURE 7: Number of state contracts*



Sixty-four percent of organizations in this study have contracts with one state agency, twenty-two percent report having contracts with between 3 – 5 agencies, and 14% of organizations have contracts with between 6 – 11 state agencies.

The next question asked if any of those contracts payments were paid late:

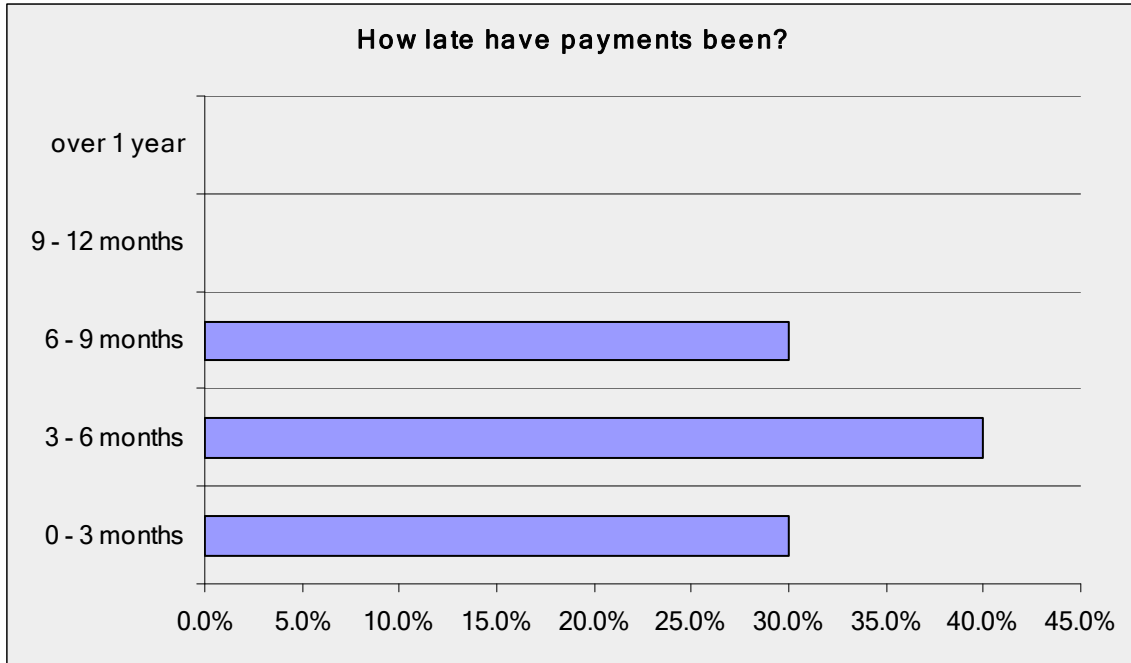
*FIGURE 8: Late payments in 2009 and 2010*



Late payments on contracts in 2009 and 2010 were reported by 69% of the responding organizations with 31% reporting no late payments.

When asked how late the payments have been, the responses were as follows:

*FIGURE 9: How late payments have been*



Most of the organizations that experienced late payments reported the payments were between 3 – 6 months late. Payments that were between 0 to 3 months were reported by 30% of the organizations and another 30% reported contract payments as late as 6 to 9 months. No organization reported receiving payments later than 9 months.

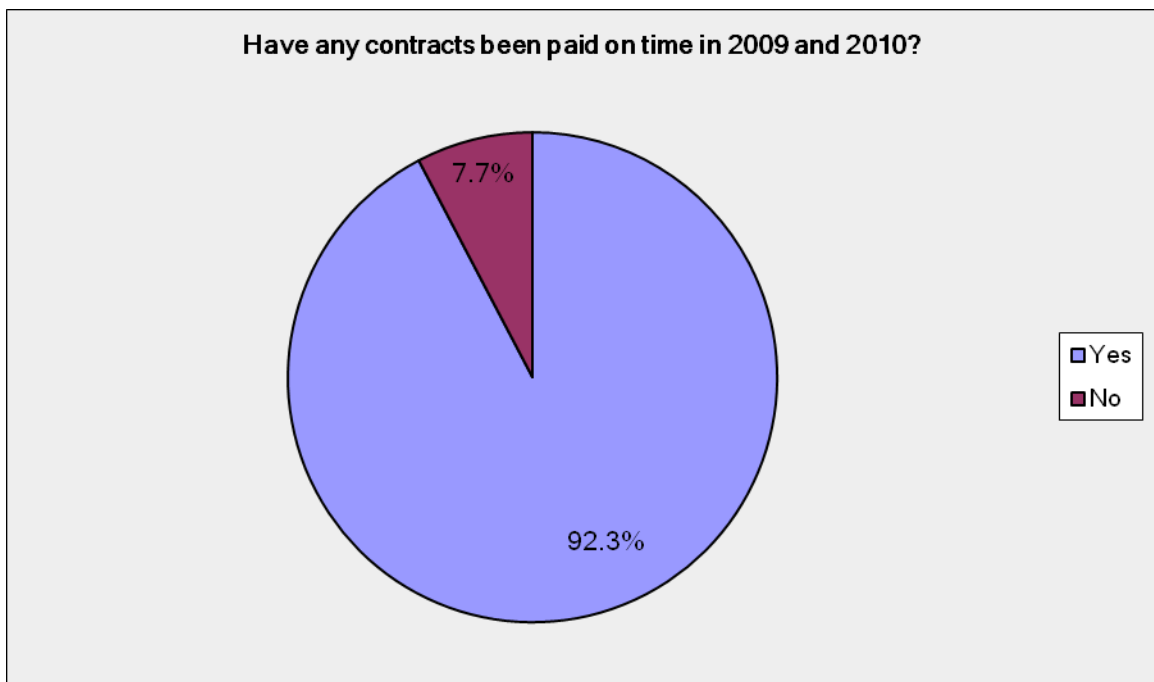
The organizations were next asked to describe the impacts the late contract payments have had on their organizations. The most common response was that they were experiencing cash flow difficulties, with two respondents reporting they had to access a line of credit and another having to use reserve funds to cover operating costs. One also reported being unable to pay vendors and having to prepare for layoffs and another was experiencing difficulty in meeting their payroll. Another reported being able to manage so far but noted with continued late payments they expected they

would begin to experience cash flow difficulties. Four of the respondents reported minimal to no difficulties as a result of late contract payments.

The next question asked the organizations to briefly describe any resulting impacts on the populations they serve because of the late contract payments. Four reported no impacts, while others reported such impacts as late rental subsidies placing low-income households at risk, having to delay cancer screenings and decreased transportation available for clients, and only billable services have been provided with non-mandated services being either eliminated or curtailed. It should be noted that seven of the 14 respondents did not respond to this question.

The next question asked if any contracts had been paid on time in 2009 and 2010. The responses were as follows:

*FIGURE 10: On time payments in 2009 and 2010*



Most of the organizations in this study also experienced some on time contract payments in 2009 and 2010.

All of the organizations responded that there are some state agencies that are more efficient than others in their contracting processes.

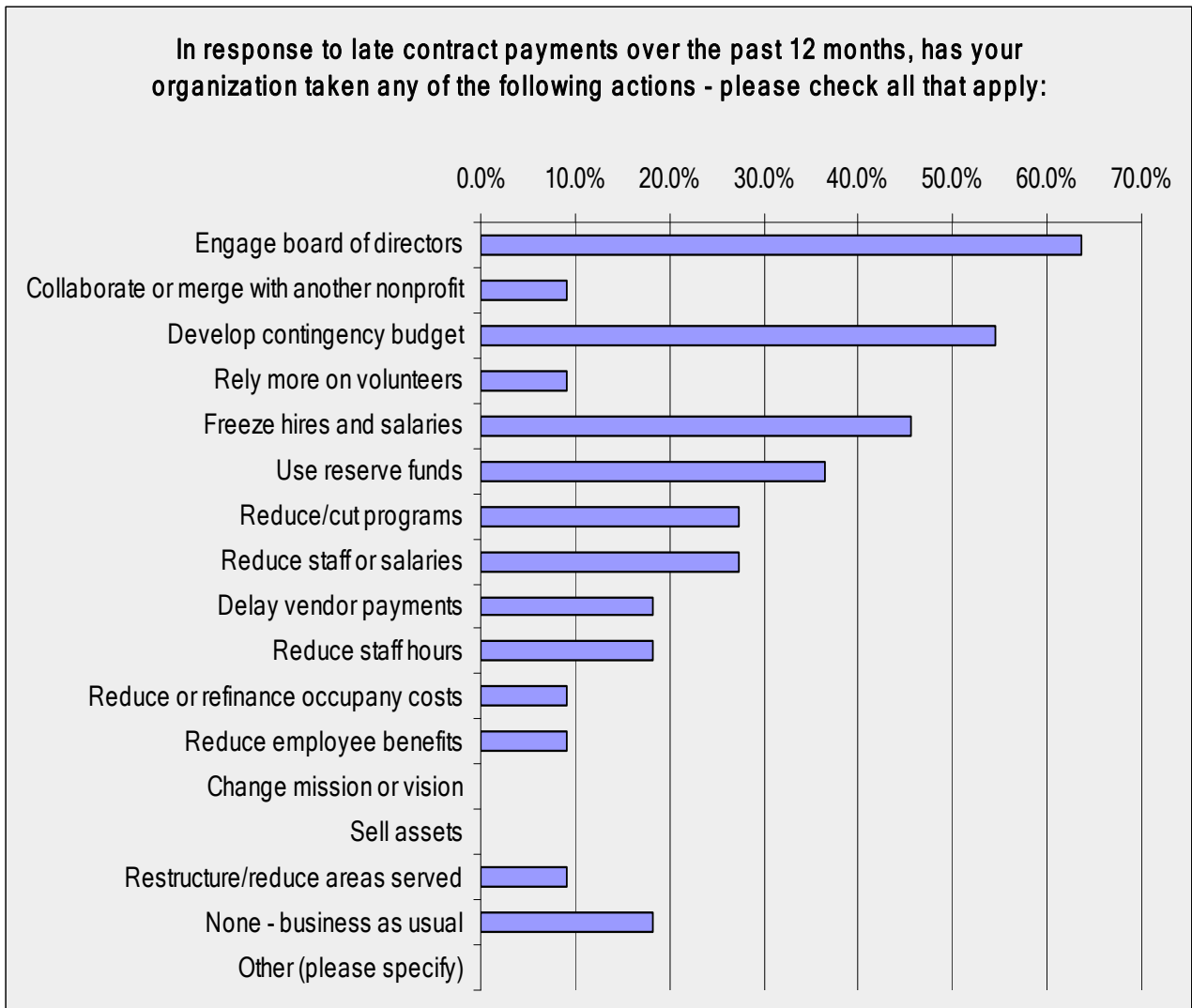
The next question asked the organizations to describe, based on their experience, what factors contribute to better efficiency in the contract process by an agency. Responses included the following factors:

- Knowledgeable staff
- Sufficient personnel
- Personal contacts with agency staff versus automated processes
- Well-organized staff
- Agency administration
- Clear and concise upfront processes
- Preplanning
- Timeliness
- Communication

Data gathered from the first two questions in the section on planning and outlook for the future are presented in the following charts.



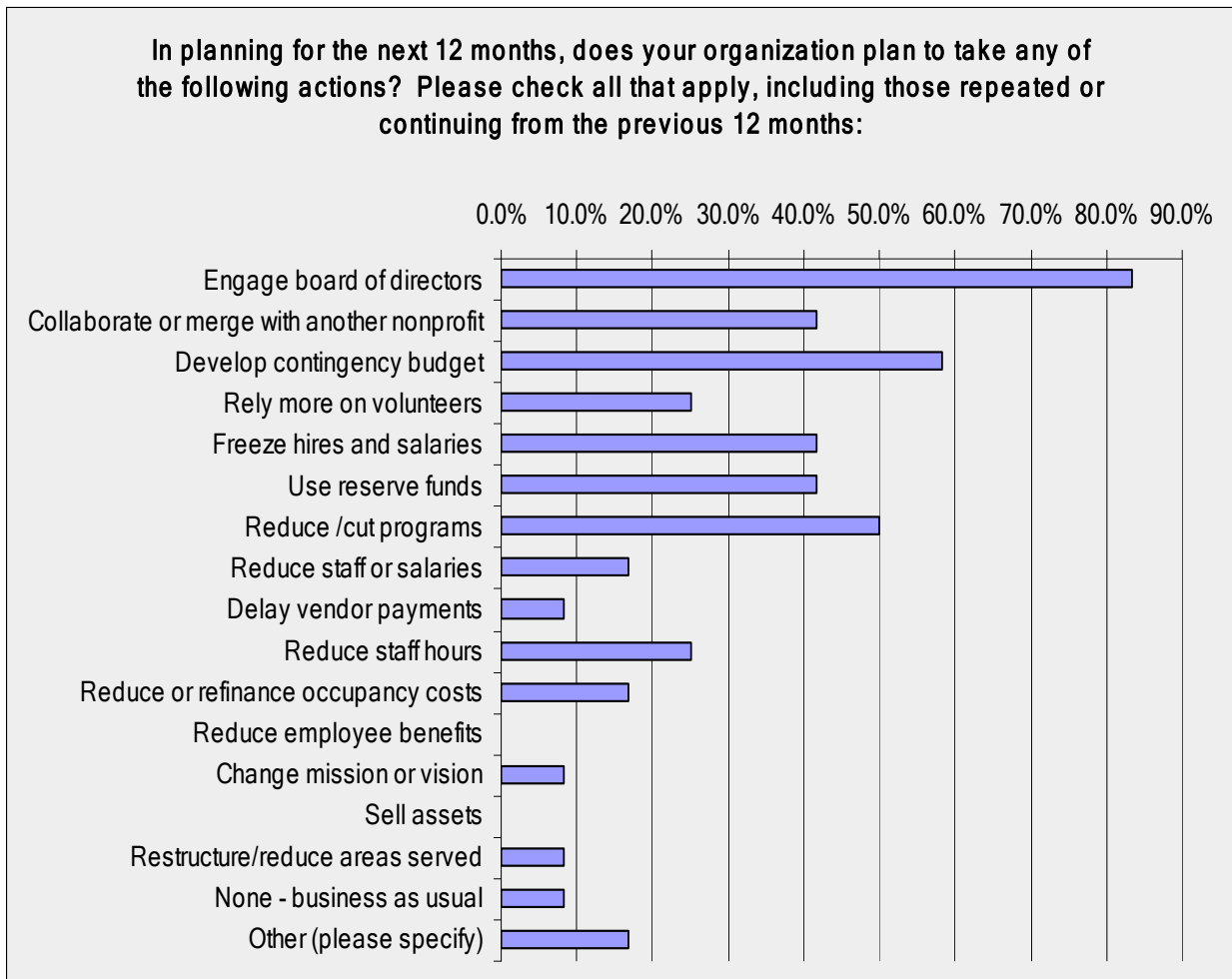
FIGURE 11: Actions taken in past 12 months



The data shows that most of the organizations engaged their board of directors as they faced problems caused by late contract payments in the past 12 months. Over half of the organizations developed a contingency budget while almost half had to freeze hires and salaries. The next most common action among respondents was to dip into their reserve funds. Almost 30% of respondents also reduced or cut programs and had to reduce staff or salaries. Nearly 20% of the responding

organizations had to delay vendor payments and reduce staff hours. That same amount reported no actions had to be taken in response to late contract payments in the past year.

*FIGURE 12: Actions planned for next 12 months*

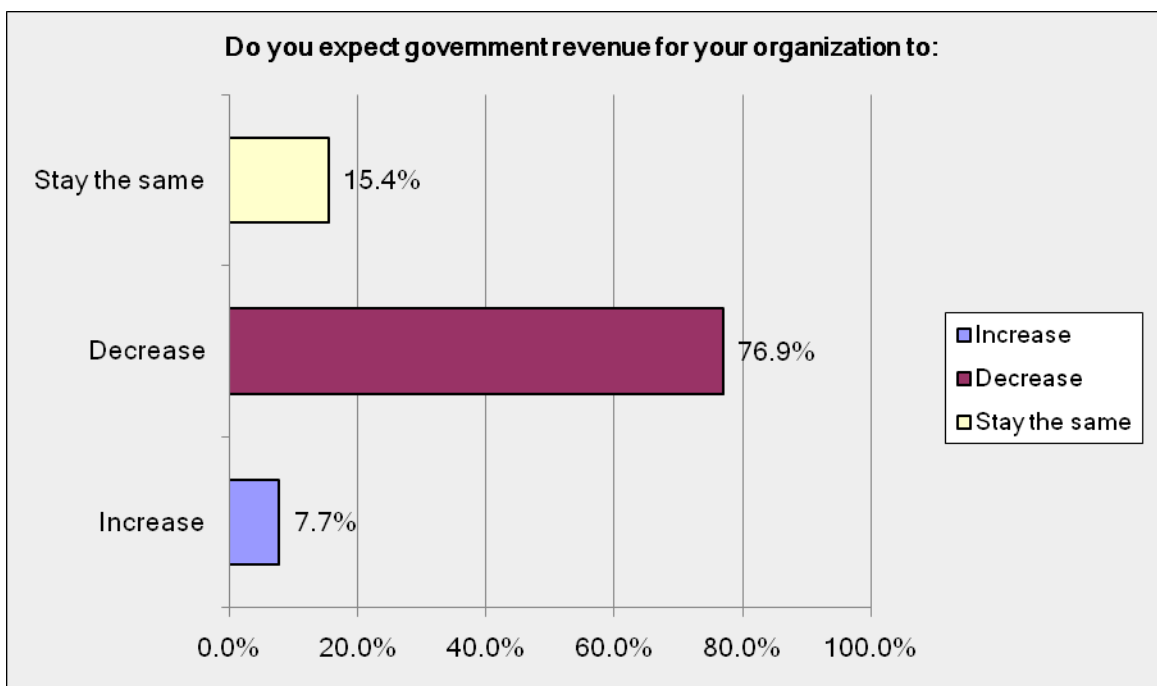


The data shows that more of the responding organizations are planning to engage their board of directors in the next 12 months in response to the issue of late contract payments and well over half will be developing a contingency budget. Half of the organizations are also anticipating having to reduce or cut programs in the next 12 months. Over 40% are expecting to collaborate or merge with

another nonprofit, freeze hires and salaries and use reserve funds. The responses regarding planning for the next 12 months in the 'Other' category included reviewing programmatic expenses and reducing future occupancy costs by having relocated earlier this year.

In considering the outlook for future funding from the state, the respondents replied as follows:

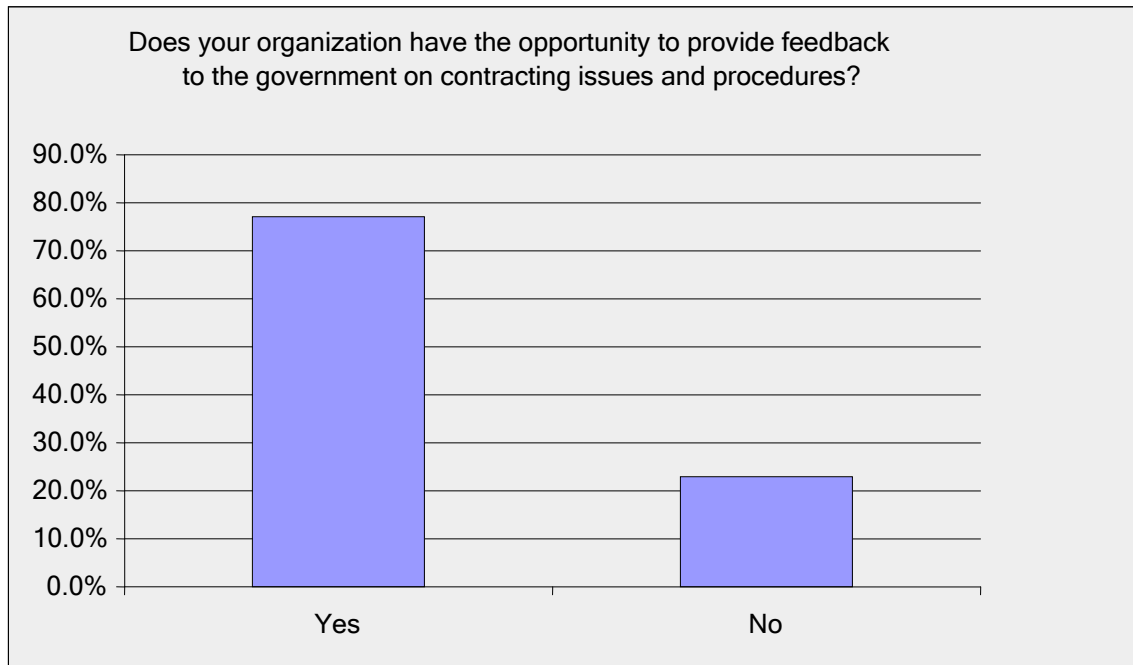
*FIGURE 13: Expectation for amount of government revenue*



Nearly 80% of organizations are expecting government revenue to decrease with 15.4% expecting it to remain the same and only 7.7% are anticipating an increase in government revenue.

To get a sense of communication between the nonprofit organization and the contracting agency, the following question was asked:

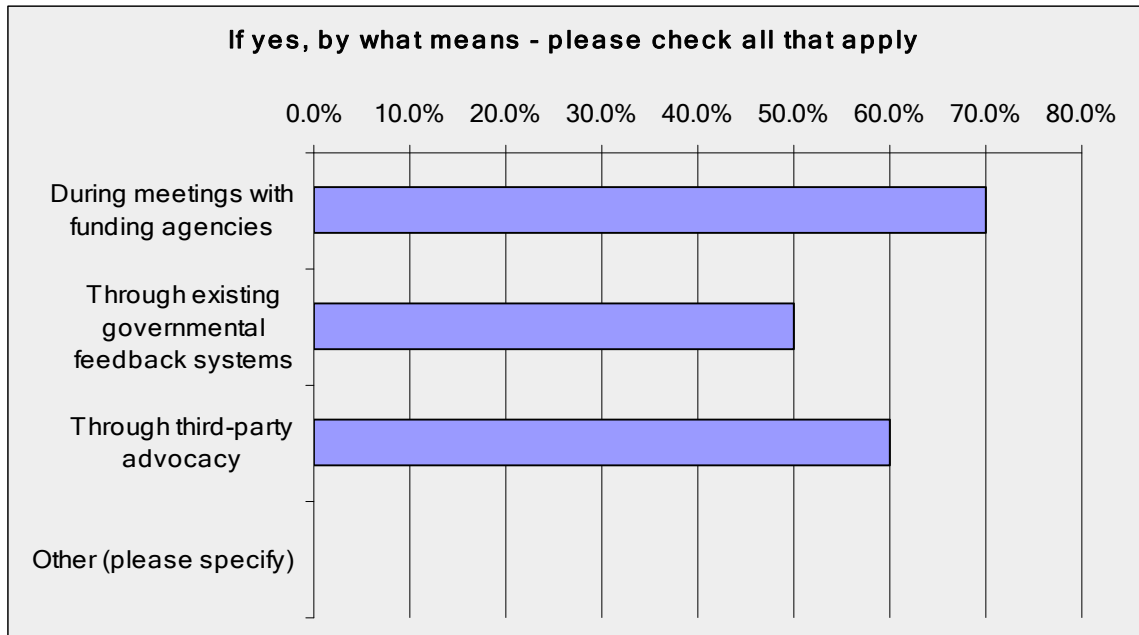
*FIGURE 14: Feedback opportunities on contracting*



Almost 80% of respondents report that they do have opportunities to provide feedback to the government on contracting issues and procedures with just over 20% reporting they do not have such opportunities.

Respondents were then asked to identify by which means the organizations are able to provide feedback to the government on contracting issues and procedures:

*FIGURE 15: Means of communicating with contracting agencies*



Most of the organizations in this study report being able to provide feedback to the government on contracting issues and procedures during meetings with funding agencies. Sixty percent of respondents report communicating on these issues through third-party advocacy and 50% use existing governmental feedback systems.

The respondents were offered the opportunity to make additional comments about their organization's experience with government contracting and the following six responses were received:

- They are now telling us to spend 100% of contracted amount but only expect them to reimburse at 98.9%, with the possibility they can make it up with federal money if they get it.
- Because the funding agencies are experiencing their own staff reductions the contract process has become more onerous; the go-to individuals are no longer there.
- Although [we] did not experience late payments on contracts, we did experience a 10% cut in our state contract which results in \$26,000 and laying off of staff.
- Due to the size of our agency, we are currently able to use surplus cash to cover any late payments. Due to the loss of \$1,000,000 dollars of Medicaid funding in the fourth quarter of 2010, I expect that we will begin to be challenged to continue this practice. The cuts to our Medicaid funding are a large concern.
- We receive a per diem rate for the services we provide that is determined by the state, but paid by different counties. We are vulnerable to the counties ability to execute payment, not the state.
- Local government does not seem to understand the impact our programs have on people. Our services provide long term lasting solutions. While not "urgent" in the immediate sense, this is an investment in the future of adults and their children (education oriented). We are not sure that local government recognizes this.

The following question was asked via email to ten of the eighteen organizations which had agreed to take the survey:

*Are you familiar with a law in New York State entitled "Prompt Contracting and Interest Payments for Not-For-Profit Organizations"?*

Nine of the ten responded, with six responding they are familiar with the law and three responding they are not familiar with the law.

## **Analysis of Findings**

The stated purpose of this research was to examine the impact of the late payment issue on nonprofits in the Mid-Hudson Valley that have contracts with New York State agencies. This research also aimed to provide some analysis and comparison into the reason for the late payments by looking at the experiences of these organizations with their contracting agencies.

The majority of the organizations in this study are mid-sized human services nonprofit organizations. All reported that their services are considered critical to people in need. More than half of these organizations receive 50 to 90% of their revenue from contracts with New York State.

The nonprofits who responded to this survey reported experiencing either a significant or slight increase in demand for their services over the past year. This trend was also experienced by nonprofits across the country as found in the nationwide survey of nonprofits by the Nonprofit Finance Fund, with 93% of respondents reporting increased demand for services. The National Council of Nonprofits' report, "A Respectful Warning Call to Our Partners in Government," cites a survey conducted by Guidestar to gauge the effect of the economic downturn on nonprofits which found that 58% of responding organizations reported an increase in demand for services.

In the face of this increase in demand for services over the past year, 43% of the organizations surveyed were unable to fully meet that demand. The results of studies conducted of nonprofits in Colorado, Illinois, Michigan, and New Jersey report similar findings.

Late payments on contracts with New York State were experienced by 69% of the Mid-Hudson Valley nonprofits in this study in 2009 and 2010. Payments were between 3 to 6 months late for 40% of the organizations, between 0 to 3 months late for 30% and between 6 to 9 months late for the remaining 30% of respondents. The issue of late contract payments by governments to nonprofit

organizations has been well-documented through a variety of state-specific and nationwide studies as one of several problems with the government–nonprofit contracting relationship.

Many of the experiences of the organizations in this study as a result of these late contract payments are similar to those found in other state and nationwide studies. Reports of cash flow problems, having to access a line of credit and dipping into the organization’s reserve funds are examples of how these organizations are dealing the shortfall in funding due to late contract payments. Organizations across the country are taking similar measures, as described in the literature review from reports out of Illinois, Connecticut, and Michigan as well as those outlined in the results of the recent nationwide survey of nonprofits conducted by the Urban Institute.

A majority of the organizations in this study expect government revenue to decrease, which indicates they will need to continue to find ways to fill the funding gap. This finding is in line with the results from the Nonprofit Finance Fund’s nationwide survey in 2009.

Over the past year more than half of the organizations in this study have had to develop a contingency budget and engage their board of directors to find solutions to the problems caused by late contract payments. Many have not been able to hire new staff or offer salary increases to current employees, all while most have also experienced a significant increase in the demand for their services. The past 12 months also saw many of these organizations reducing or cutting programs, having to reduce staff or cut salaries, delay payments to vendors and reduce staff hours.

In looking ahead to the next 12 months, even more of the organizations in this study are planning to have to engage their board of directors in response to late contract payments than had in the previous 12 months. More are expecting to have to develop contingency budgets and almost half



are anticipating having to collaborate or merge with another nonprofit, up by almost 30 percent from the past year. More will be using reserve funds to keep running while half will need to reduce or cut programs. While 18.2% responded that no actions were taken over the past year in response to late contract payments, only 8.3% responded that they will continue with business as usual in the coming year. This indicates that these nonprofits are anticipating deepening problems as a result of late contract payments.

The impacts of late contract payments on the populations served by these organizations are less clear than the impacts on the organizations themselves, according to this study. Only half of the organizations responded to this question, with four of those indicating their populations were not impacted.

The Mid-Hudson Valley nonprofits in this study also report experiencing some contract payments on time in 2009 and 2010, as reflected in the responses to survey question 14. This result was unexpected, as 92% of the organizations surveyed responded having received payments on time. What this seems to suggest is that these organizations have had mixed experiences with contract payments, with some of the payments being late, as reflected in the responses to question 10, and some payments being received on time.

The experiences of these organizations in the contracting relationships with New York State appear to be similar, according to this study. All of the responding organizations report that some state agencies are more efficient than others in their contracting processes. The reasons cited most often to explain the difference in efficiencies among the agencies have to do with communication with and knowledge and organization of agency staff.

Almost 80% of respondents report that they have opportunities to provide feedback to the government on contracting issues and procedures, with most doing so during meetings with the funding agency, followed by third-party advocacy and existing governmental feedback systems.

More than half of the respondents are familiar with the law in New York State entitled “Prompt Contracting and Interest Payments for Not-For-Profit Organizations,” although questions exist among some regarding interpreting the time frames mandated by and the enforcement of the law.

This study was most successful in confirming that nonprofits in the Mid-Hudson Valley are being somewhat affected by late state contract payments. The study was also able to illustrate fairly well what the impacts look like for the organizations themselves. The study was less successful in presenting the impacts of the late contract payments on the populations they serve.

This study attempted to take a brief look at the relationships with the contracting agencies. Most of these organizations are able to communicate about the contracting process with the agencies, although the quality of those interactions was not measured by the data collected in this study. The results of this study identify that it is the knowledge and skill of the individuals working at the various agencies that makes the contracting process at one agency better than another.

More data would be needed to say with confidence whether or not the laws in New York State, such as the ‘Prompt Contracting and Interest Payments for Not-For-Profit Organizations,’ meant to alleviate late contract payments make a difference for these agencies.

## **Conclusions and Recommendations**

Nonprofit organizations in the Mid-Hudson Valley, especially in the category of human services, are important partners with New York State in providing essential services to the people in this region. Although this study highlights a small sample of nonprofit organizations, its findings begin to tell a story of organizations critical to the communities they serve that are experiencing challenges with their state partners.

The results of this study reveal organizations that rely on state funding, in many cases for more than 50% of their operating budgets, are facing decreased revenue from the government. The news about the state's budget for the foreseeable future is grim and the prospect of the revenue these organizations need to fulfill their missions is not promising. This study shows that these organizations are already beginning to plan differently for the year ahead than they did in the previous year in light of the continued financial challenges in New York State.

The fact that this study found these organizations planning differently for the year ahead is in many ways good news. This shows that these organizations are looking at their situation realistically and planning for the challenges ahead. Some of the organizations are looking at options such as merging with another nonprofit and even changing their mission, which in some cases become necessary means to survival in the face of financial difficulties.

It will be important for these organizations to continue with prudent planning. It is also important, especially during economic downturns, to have sound financial management systems in place. The organizations in this study might also benefit from considering the development of new revenue streams to replace decreasing and unreliable government funding.

As these nonprofits engage their boards of directors, develop contingency budgets and take other actions to cope with financial strain, it may be useful to seek the services of a consultant (preferably pro-bono) to assist in their planning process. There are many resources available through organizations dedicated to working with nonprofits such as Guidestar, Independent Sector, the National Council on Nonprofits, the Nonprofit Finance Fund, and closer to the Mid-Hudson Valley, the Foundation Center and the New York Council on Nonprofits. These organizations will be able to provide guidance on best management and financial practices, capacity building and other issues to assist the nonprofits in getting through these difficult economic times.

This study also found that some state agencies are more efficient than others in their contracting processes. This suggests a possible area of reform on the part of the state government to consider ways to standardize contracting practices so the experiences of their nonprofit partners are more consistent. Efforts at the standardization of contracting practices across state government could ultimately save money for both the state and the nonprofits.

This study could have been improved if the scope of the research had been expanded to include federal and local governments as well as state government. By limiting the research to organizations with state contracts a large percentage of nonprofit organizations in the Mid-Hudson Valley were not included as many have contracts with county governments.

Issues with government contracting are often complex and the matter of late payments is but one of many problems affecting nonprofit organizations, as demonstrated by the results of the recent study conducted by the Urban Institute (Boris et al., 2010). It would have been useful to broaden the scope of this study from just late contract payments to include other contracting problem areas such as payments that do not cover the full cost of contracted services, complex and time-consuming

reporting requirements, and changes made to contracts and grants after initial approval. It would have also been interesting to have learned through the survey of any other issues the organizations in the Mid-Hudson Valley are experiencing in their contracting relationships with the government.

The results of this study could have been more significant if follow-up in-person interviews were conducted to clarify and expand upon responses to the on-line survey. Unfortunately, time constraints did not allow for such follow-up.

Since work on this study began earlier this year, the problems being faced by nonprofit organizations that have contracting relationships with government have come on to the national stage. In addition to increased news coverage in general, a nationwide survey was conducted by The Urban Institute on nonprofit government contracting and grants (Boris et al., 2010). This survey was the first phase in a larger project, which received funding from the Bill and Melinda Gates Foundation, which aims to develop and implement real solutions to the problems identified in the nationwide survey.

In conjunction with the Urban Institute's survey, the National Council on Nonprofits issued a report on how the government's human services contracting system is in need of improvement (National Council of Nonprofits, 2010). The report suggests action items for all parties to take to improve the situation. They have also launched a government contracting website which is a clearinghouse for this topic and includes current media reports, state-by-state information, discussion of possible solutions and an area for nonprofit organizations to tell their own stories relating to government contracts.

Another example that the issue has been recognized as problematic and is being brought on to the national scene was the introduction of the *Nonprofit Sector and Community Solutions Act* (H.R. 5533) on June 15, 2010, which aims to strengthen the partnership between nonprofit organizations and the federal government.

The Office of the New York State Comptroller has also been active in addressing the issue of contract delays to nonprofits. State Comptroller Thomas DiNapoli has hosted a series of forums throughout New York State on contracting issues with nonprofits and is proactive in communicating through press releases and reports regarding the issue. In July of this year he made recommendations to improve the state's contracting processes.

The above examples serve as encouraging signs that the real problems being faced by nonprofit organizations in the Mid-Hudson Valley, New York State and around the country in regard to government contracts are finally being heard and discussions about real solutions are beginning.

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## APPENDIX A: Survey Instrument

## Nonprofits and government contracts

### 1. Demographics and organizational information

The focus of this section is to learn a little bit about your organization.

1. Where is your organization located?

2. What nonprofit category does your organization fit into?

- Arts and culture
- Education
- Environment and animal
- Health
- Religious
- Human Services
- Other (please specify)

3. How many employees does your organization have?

4. What is your organization's annual operating budget?

5. What percentage of your revenue comes from state contracts?

6. Is the service provided by your organization considered critical to people in need?

- Yes
- No

7. This year, did your organization experience:

- A significant increase in demand for your services
- A slight increase in demand for your services
- No change in demand for your services
- A decrease in demand for your services

## Nonprofits and government contracts

8. Was your organization able to fully meet demand for your services this year?

Yes

No

## Nonprofits and government contracts

### 2. Contracts and contracting agencies

The focus of this section is your organization's current situation regarding state contracts and your organization's experience with the contracting agencies.

9. Does your organization have contracts with one or more state agency? If more than one, please specify the number of agencies.

10. Has your organization experienced late payments on any of these contracts in 2009 and 2010?

Yes

No

11. How late have payments been?

0 - 3 months

3 - 6 months

6 - 9 months

9 - 12 months

over 1 year

12. Briefly describe what impacts the late contract payments are having on your organization.

13. Briefly describe what the resulting impacts are of these late contract payments on the population/s your organization serves.

14. Have any contracts been paid on time in 2009 and 2010?

Yes

No

15. In your organization's experience, are some agencies more efficient with their contracting processes?

Yes

No

16. In your experience, what factors contribute to better efficiency in the contract process by an agency?

## Nonprofits and government contracts

### 3. Planning and outlook for the future

The purpose of this section is to get an idea of how your organization is planning given the reality of late contract payments.

**17. In response to late contract payments over the past 12 months, has your organization taken any of the following actions - please check all that apply:**

- Engage board of directors
- Collaborate or merge with another nonprofit
- Develop contingency budget
- Rely more on volunteers
- Freeze hires and salaries
- Use reserve funds
- Reduce/cut programs
- Reduce staff or salaries
- Delay vendor payments
- Reduce staff hours
- Reduce or refinance occupancy costs
- Reduce employee benefits
- Change mission or vision
- Sell assets
- Restructure/reduce areas served
- None - business as usual
- Other (please specify)

## Nonprofits and government contracts

**18. In planning for the next 12 months, does your organization plan to take any of the following actions? Please check all that apply, including those repeated or continuing from the previous 12 months:**

- Engage board of directors
- Collaborate or merge with another nonprofit
- Develop contingency budget
- Rely more on volunteers
- Freeze hires and salaries
- Use reserve funds
- Reduce /cut programs
- Reduce staff or salaries
- Delay vendor payments
- Reduce staff hours
- Reduce or refinance occupancy costs
- Reduce employee benefits
- Change mission or vision
- Sell assets
- Restructure/reduce areas served
- None - business as usual
- Other (please specify)

**19. Do you expect government revenue for your organization to:**

- Increase
- Decrease
- Stay the same

**20. Does your organization have the opportunity to provide feedback to the government on contracting issues and procedures?**

- Yes
- No

## Nonprofits and government contracts

21. If yes, by what means - please check all that apply

- During meetings with funding agencies
- Through existing governmental feedback systems
- Through third-party advocacy
- Other (please specify)

## Nonprofits and government contracts

### 4. Thank you!

Thank you for your cooperation and taking the time to complete this survey.

**22. If you have any additional comments about your organization's experience with government contracting, please write them below.**