PUBLIC CONSULTING GROUP

MEMORANDUM

TO: Department of Child Services (DCS)

FROM: Public Consulting Group (PCG)

RE: LCPA and RTSP Cost Caps

DATE: November 1, 2011

Overview

The Indiana Department of Child Services (DCS) established the process for instituting cost caps by administrative rule. The rule establishing the process for implementing the residential treatment service provider (RTSP's) cost caps can be found at 465 IAC 2-16, while the rule establishing the process for implementing the cost caps for child placing agencies (CPA's) can be found at 465 IAC 2-17. These cost caps set maximum allowable limits for specific cost areas such as salaries, administrative costs, occupancy expenses, and additional areas. On October 18, 2011, DCS published cost caps for RTSPs and CPAs summarized in the table below.

Cost Areas	LCPAs	RTSPs
Salaries	Based on agency size: • Less than $1.0 million in revenue - $100,000 • Between $1.0 million and $5.0 million - $125,000 • Greater than $5.0 million in revenue - $175,000[1]	Based on agency size: • Less than $1.0 million in revenue - $100,000 • Between $1.0 million and $5.0 million - $125,000 • Greater than $5.0 million in revenue - $175,000[2]
Fringe Benefits	25% of salaries [3]	25% of salaries
Minimum Direct Care Staffing Ratios	*Not applicable*	CCI - 5.7:1 CCI ESC - 3.8:1 Group Home - 6.6:1 Group Home ESC - 5.7:1 Private Secure - 3.2:1 DD Programs - 2.5:1 SMY Programs - 3.5:1[4]

[1] CWLA Salary Survey 2009
[2] CWLA Salary Survey 2009
[3] Analysis of Statewide Distribution of Provider Fringe Benefit Rates
[4] Licensing Rule Minimum Staffing Requirements by shift by Licensing Category, with exceptions made for DD and SMY programs to permit appropriate staffing ratios

Cost Areas	LCPAs	RTSPs
Minimum Caseload Ratio	7.0:1[5]	*Not applicable*
Administrative Costs	95% of Direct Costs[6]	20% of Direct Costs[7]
Allowable Profit Margin (for-profit agencies)	7.47%[8]	7.47%
Minimum Occupancy	*Not applicable*	80%[9]

PCG conducted significant national rate setting research in July 2010 to assist DCS in establishing the caps. PCG reached out to over 21 states to identify how costs were treated for residential child care and child placing agency programs. The cost categories reviewed included:

- Staffing Ratios
- Personnel Salary
- Fringe and Indirect
- Occupancy and Facility Costs
- Direct Administrative Costs
- Indirect Administrative Costs
- Profit
- Utilization/Occupancy

PCG compared the DCS proposed cost caps to the Child Welfare League of America (CWLA) Salary Study from 2009 and the other state research conducted. Where appropriate, PCG has applied the guidance found in Federal OMB Circular A-122 to determine whether the particular cost cap is reasonable when applied to DCS' duty to pay no more than a reasonable cost. That is, when PCG determines a particular cost cap to be reasonable, it is determining that a DCS decision not to pay in excess of those capped costs is a decision that would be made by a prudent person under the circumstances prevailing at the time the decision was made. The review is summarized below.

Staff Salaries

The staff salary cost caps were set based on CWLA's Salary Survey. The survey examines private and state child welfare provider data across the country and develops averages. The proposed salary cap ranges accounts for agencies of various revenue sizes including, less than $1 million, between $1 million and $5 million, and greater than $5 million.

The CWLA is a nationally accepted survey whose purpose is to capture employee compensation and benefit packages so that provider agencies remain competitive in terms of hiring and retaining employees. The benchmarks used for the Indiana DCS staff salary caps reflect the approximate national average for agencies of this size. Other methodologies used by states either established salaries against state salary pay grades or the median across providers. The national CWLA data incorporates factors for agencies of varying revenue sizes. In cases where states had salary caps they did not differ to account for changes in provider agency size.

PCG believes that the cost cap on staff salaries is reasonable. The CWLA Salary survey is a respected survey with both its questions and results directed to the types of child welfare agencies whose rates are the subject of the DCS rate rules.

[5] Licensing Rules (minimum of 8.0:1)
[6] Analysis of Statewide Distribution of Provider Administrative Rates
[7] PCG Consulting Analysis of Other State Rate Setting Practices
[8] Analysis of Statewide Distribution of Provider Administrative Rates
[9] PCG Consulting Analysis of Other State Rate Setting Practices

Fringe and Benefits

The 25% fringe and benefit cap, which includes all employee benefits and payroll taxes, is reasonable based on the peer state review and the CWLA Salary Study. The fringe benefit ceiling is based on the average fringe and payroll taxes as reported by DCS contracted CPAs and RTSPs. Indiana's peer state, Illinois, limits fringe benefits at 25% of the total salary costs.[10] The CWLA Salary Study also establishes a reasonable fringe benefit package as 24.5% for the Midwest region.[11]

Minimum Caseload and Direct Care Staffing Ratios

Most states establish caseload ratio limits based on the licensing requirements in regulation. Indiana has established cost caps related to staffing ratios at below the state mandated licensing requirements for CPAs. The caps that apply to the RTSPs and the CPAs have each been set to ensure that a provider is able to retrieve costs in excess of those that would be capable of being retrieved had the cost cap been set by applying only the staffing ratio required for licensing. For example, the CPA staffing ratio for licensing purposes is 8:1; if however a provider is staffed more heavily at 7:1 (the cost cap for rate purposes) it is allowed to retrieve these costs even though they exceed the costs that DCS licensing rules would require.

Similarly, for RTSPs, the cost cap staffing ratios were set below the minimum licensing requirements[12] for each shift. DCS reviewed the minimum staffing standards for each shift, first, second and third, and calculated a weighted average to use as the baseline. A cushion of 5% to 20% was added based on each program to identify the staffing limits.[13] The established ratios are well below the licensing requirements allowing programs flexibility in how facilities are staffed. For the Developmentally Disabled (DD) and Sexually Maladaptive Youth (SMY) programs DCS will permit providers to appropriately staff at ratios well below the minimums for licensed Child Caring Institutions (CCIs) in order to meet the special needs of these children and be reimbursed for the associated costs up to the cap amount. [14]

Staffing ratios for other states reviewed are set based on licensing standards. Accordingly, DCS' implementation of a cost cap that permits providers to retrieve costs for staffing in excess of what would otherwise be retrievable had the relevant licensing ratio been applied, is an excessive expenditure in light of our research into what other states permit. However, we cannot conclude that this expenditure, while excessive, is unreasonable. Indiana seeks to provide flexibility for residential facilities and has based this decision on state-specific data and cost report and provider input.

Total Administrative Costs

The administrative cost cap for CPAs is based on an analysis of provider administrative rates from state-specific data. Given the nature of the CPAs services, 95% of their costs should reflect administrative activities given their minimal fixed costs and low direct costs compared to RTSPs.

A predominate portion of residential expenditures are associated with direct service and the administration of the direct service provision. Only a small portion of costs should be associated with administrative activities, including indirect expenses. In the peer state review conducted, administrative caps ranged from 15% to 25% based. Illinois, a peer state of Indiana, established the limit at 20%.[15] An Urban Institute report notes that while many funding sources limit administrative costs to 10%, a more appropriate limit for non-

[10] Section 365.50 at 89 Ill. Reg

[11] CWLA Salary Study. 2009.

[12] 465 IAC 2-9 through 465 IAC 2-13

[13] Staff to child ratio incorporates changes for each shift. DCS calculation incorporates 1: 4.2 ratio based on weekly hours / 40 hours per week.

[14] Average of Report Staff Ratio Cap Analysis. I-Rate Report. October 12, 2011.

[15] Section 365.50 at 89 Ill. Reg

profit organizations is closer to 20%.[16] DCS' proposed cap is reasonable based on peer state review and national studies of nonprofit entities.

Minimum Occupancy

Based on Indiana provider reported information, the average occupancy percentage is 54.58% with the minimum being 41% and the maximum being 83%. The proposed cap of 80% is on target with other state limits. In the review of minimum occupancies established in other states, the average was in the range of 80% with the minimum being 73% for shelters in Vermont and the maximum being 98% in Illinois. South Dakota, Connecticut, and Oregon have all set the minimum occupancy at 90%. Iowa has a utilization cap of 80%.[17]

Allowable Profit Margin (for-profit agencies)

Other states only allow for-profit entities to report profit. Wisconsin has set a maximum of 10% and Illinois a 9%. Based on the statewide distribution reported by providers, DCS has proposed a cap of 7.47%. The profit limit is reasonable as it reflects the actual average reported by Indiana-specific for-profit agencies.

Conclusion

Based on our review of child welfare rate setting efforts across the country, nationally available data and Indiana-specific data, PCG confirms that the cost caps proposed by DCS are reasonable and fair.

[16] National Council of Non-Profits. "Failure to Pay Full Costs." Retrieved from http://www.govtcontracting.org/problems/failure-pay-full-costs on September 20, 2011

[17] Rules and Administrative Code. Conversation with Jody, Management Analyst with Iowa on May 19, 2010.