

BRIEF REPORTS

Revenue and Expenses over Five Years in Intellectual Disability Service Providers in Pennsylvania

Scott Spreat*

ABSTRACT

Purpose: *The aim of this study was to ascertain the financial health of intellectual disability provider agencies in Pennsylvania over a five-year period of time.*

Method: *GuideStar was used to access the 990 tax forms of 79 provider agencies belonging to the PAR provider association.*

Results: *Data revealed that approximately 1/3 of the service providers had expenses that exceeded revenue each year. Despite this negative finding, net assets of the provider agencies grew and it was evident that additional money was entering the system. The threats of this sort of situation were discussed.*

Conclusions: *It appears to be a constant that 1/3 of provider agencies have expenses that exceed revenue each year. This data questions the long-term sustainability of Pennsylvania intellectual disability providers.*

Key words: *Fiscal health provider.*

INTRODUCTION

Benchmarks of fiscal well-being appear to vary widely across different industries. The steel industry, for example, considers profitability as low as 9.5% to be a matter of concern (Silva & de Carvalho, 2015). Similarly, the National Academy of Sciences, Engineering, and Medicine (2001) concluded that the fiscal well-being of the aerospace industry was suspect, with profitability of around 7.2%.

In the non-profit world, the term 'margin' is used to describe those revenues that exceed expenses over a given time. It is essentially equivalent to profit, and this operating margin can be an early indicator of financial health (Harrison & Montalvo, 2002). The Higher Education Funding Council for England (2018)

* **Corresponding Author:** Vice President for Evaluation & Research for Woods Services, Langhorne, PA, USA. Email: sspreat@woods.org

concluded that an operating margin of 5.2% was indicative of a fundamentally sound economic position. Harrison and Montalvo (2002), raising concerns about California's hospital system, put forth the rule of thumb that a non-profit organisation needs an operating margin of 3% - 5% to be considered healthy.

Whether one adopts a benchmark from the for-profit sector or the non-profit sector, it seems clear that a sustainable organisation must generate revenue in excess of expenses. This is necessary not only to pay immediate bills, but also to fund capital needs, enable borrowing, respond to emergency situations, and to avoid deterioration of the services and supports provided.

Over the past 50 years, the intellectual disability field has undergone a dramatic shift from a system in which aid was provided in large physically-segregated institutions operated by state governments to smaller community homes operated by private agencies. The supports and services, while still funded by the state and federal government, are now typically provided by private agencies. In a sense, the government has become a monopsony, in that it is the sole purchaser of these supports and service, and as such, the government controls the prices paid for supports and services. Concern has been expressed regarding the lack of provider involvement in the establishment of prices for supports and services for people who have intellectual disability. Concerns include the likely creation of shortages (Pettinger, 2017) and provider selection of services based on identified rate to be paid rather than on consumer need (Nix, 2011). There are also concerns that improperly set rates will result in the diversion of funding from other, better-funded areas to support the intellectual disability services. Perhaps the greatest concern has to do with the diminution of service quality and/or the loss of provider agencies.

There has been only limited focus on the fiscal health of the intellectual disability system. Spreat (2017) reported that about 1/3 of the private agencies in Pennsylvania that support individuals with intellectual disability have expenses that exceed revenues. Spreat (2017) also noted that these provider agencies function on operating margins in the neighborhood of 1.6%.

Objective

Passage of time afforded the opportunity to extend the Spreat (2017) study of the fiscal health of Pennsylvania provider agencies. While the initial study focused on tax reports from the 2012, 2013, and 2014 fiscal years, the current study was able

to include data from 2015 and 2016. The study will address the same questions addressed in the earlier study:

1. Do expenses exceed revenue for intellectual disability providers?
2. Are the net assets of provider agencies being maintained?
3. Is the government injecting increased amounts of money into the intellectual disability system?

METHOD

Participants

The participants in this study were 79 provider agencies that were members of PAR in 2016. PAR is a Pennsylvania provider association that seeks to promote the welfare of agencies offering supports and services to individuals who have an intellectual disability and/or autism. All of these 79 providers were in the participant group used in Spreat's (2017) earlier analysis. There was some mortality in the sample (from 86 to 79) as might be expected in a longitudinal study such as this. Reasons include the possibilities that some agencies have closed, some have downsized below the 990 threshold, some may have filed under different or merged names, and some may have been delayed in filing. This sample constitutes approximately 74% of the PAR membership. Inclusion was based solely on the availability of 990 tax forms for 2012, 2013, 2014, 2015, and 2016 listed in GuideStar.

It should be noted that while all agencies provide supports and services in intellectual disability and autism areas, these are not the sole businesses of all of the providers. One must also note that a variety of funding streams, not only waived group homes, fund these operations. Furthermore, one must note that the net assets referenced in the 990 tax forms are not entirely derived from funds paid by the Pennsylvania Office of Developmental Programs and should not necessarily be expected to subsidise programmes partially funded by the Office of Developmental Programs.

Data Collection

GuideStar was used to access the 990 tax forms for each member of PAR for the years 2012, 2013, 2014, 2015, and 2016. From this tax form, the following

information was extracted: annual revenue, annual expenses, and annual net assets. It is to be noted that the 990 tax forms obtained from GuideStar are publicly available existing data, and as such, no approval from an Institutional Review Board is required.

Data Analysis

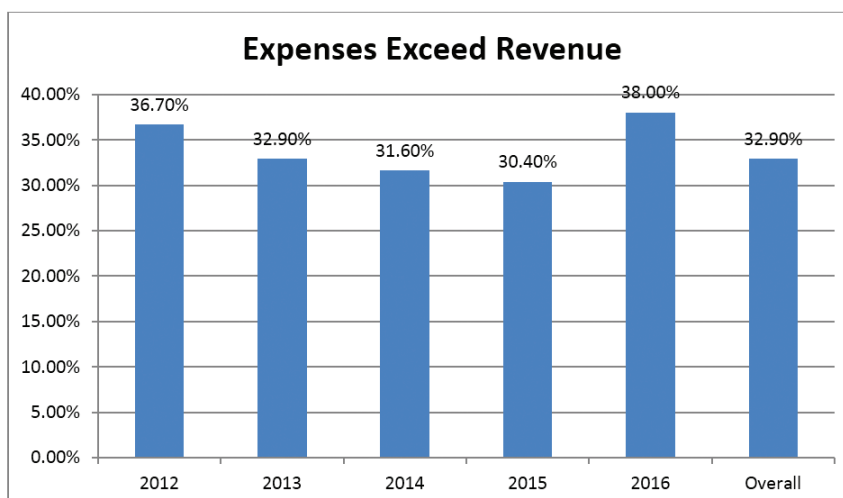
All collected data were analysed via the Statistical Package for the Social Sciences (SPSS). Analysis was limited to determination of descriptive information, with no inferential analyses being performed.

RESULTS

Do Expenses Exceed Revenue?

Operating margin was calculated by subtracting expenses from revenue in each year of the study. For each of the study years, the percentage of provider agencies for which the expenses exceeded revenue was determined, and these values are presented in Figure 1.

Figure 1: Expenses in Excess of Revenue

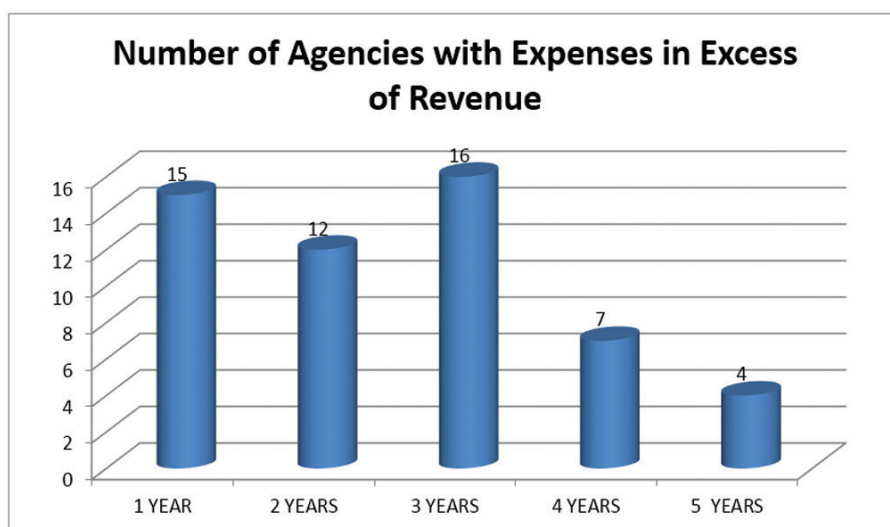


These data reveal no marked improvement or deterioration. It appears that about 1/3 of Pennsylvania intellectual disability provider agencies have expenses that exceed revenue each year. Aggregating the data across the five years of study to

enhance reliability (Strahan, 1980), it was determined that 32.9% of the agencies had expenses that exceeded revenues for the combined five-year period.

Four agencies had expenses in excess of revenues in each of the five years of study, and seven agencies had expenses in excess of revenues in four of the five years. Figure 2 presents the percentage of agencies whose expenses exceeded revenues multiple times. That is, there were twelve agencies whose expenses exceeded revenues for two of the five years of study. Sixteen (16) agencies had expenses in excess of revenue for three years of the five-year study.

Figure 2: Agencies with Expenses in Excess of Revenue



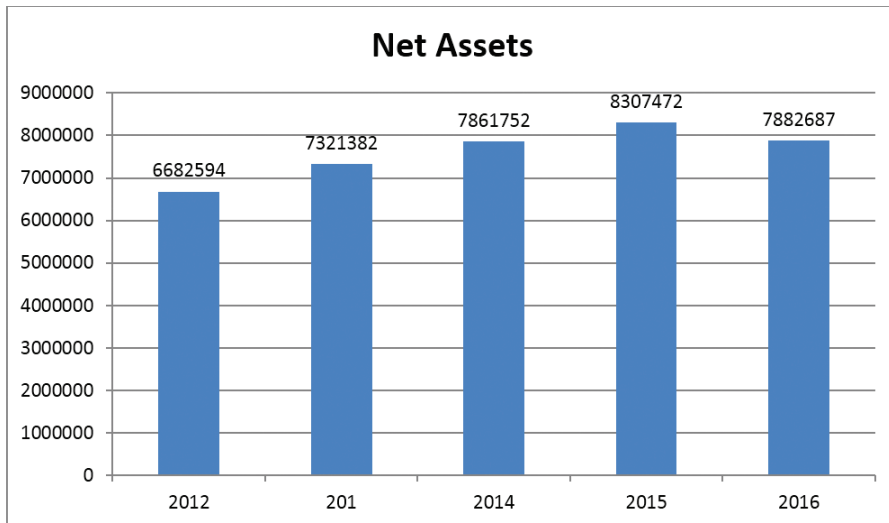
It is evident that about 1/3 of Pennsylvania provider agencies have expenses that exceed revenue each year. Thus, 2/3 of Pennsylvania provider agencies have revenues that exceed expenses each year. The mean size of the operating margin for the 79 Pennsylvania provider agencies was determined to be 1.0% (ranging from 0.2% to 1.5%).

Are Net Assets Being Maintained?

It can be argued that net assets are the prime determinant of the fiscal health of an organisation. They enable organisations to borrow, acquire, and grow. They may enable the organisation to withstand temporarily difficult economic times. These data reveal growth in net assets across the first four years, but a small decline in

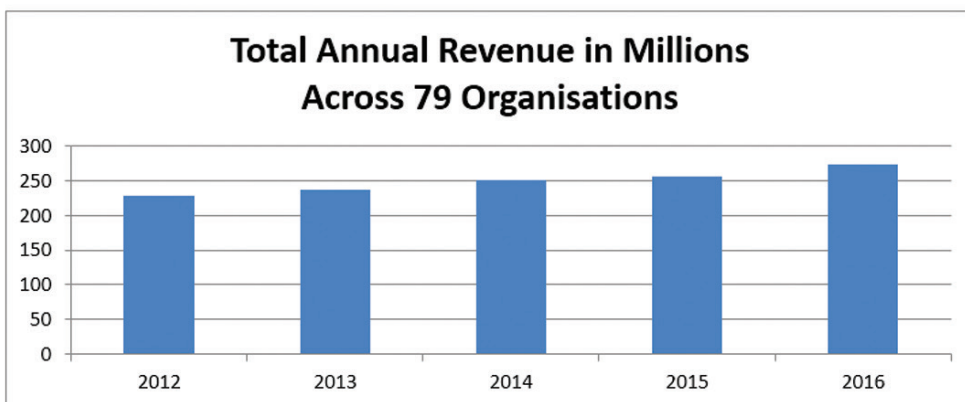
the final year of the study. Overall, the growth in net assets was determined to be 16.4%, or about 3.3% per year. Total net assets of the 79 organisations are plotted in Figure 3 below.

Figure 3: Total Net Assets of the Organisations



Is More Money Entering the System?

The total annual revenue of the 79 organisations was found to have increased by about 20.2% over the five years of study. While it can be argued that the provider organisations were required to provide additional services for this increased funding, it is clear that funding has increased over time. Whether provider agency fiscal health increased as a result of the additional funding is perhaps a matter of conjecture, but it must be noted that net assets did increase over this same time period. Figure 4 below plots the growth in revenue over the five years of the study.

Figure 4: Growth in Revenue over a Five-Year Period

DISCUSSION

Approximately 1/3 of Pennsylvania intellectual disability providers have expenses that exceed revenues in each of the five years of study. This value seems to approach constancy. Across the 79 provider agencies, approximately 31.6% lost money during at least one of the five years. These data question the long-term sustainability of Pennsylvania intellectual disability providers. While the picture of fiscal health is buoyed by the growth in net assets over the same period, it must be noted that a significant portion of provider net assets is their homes. Net assets can help sustain agencies over many years of losses. There are, however, limitations to the use of net assets to offset these losses. Net assets are not always liquid. In the case of many providers of intellectual disability supports and services, the net asset may be the home in which the supports and services are delivered.

It must be recognised that losses such as these must be subsidised in some manner. In many cases, agencies have essentially subsidised the insufficient governmental funding by dipping into their net assets. While this is reasonable in a crisis, it is not a sustainable way of conducting business. Others have increased fundraising efforts. One Philadelphia provider opened a for-profit business (bowling alley) to subsidise his non-profit social service efforts. In some cases, it seems reasonable to anticipate that those few funders who pay a reasonable cost for services provided are also paying for some of the services purchased by underfunded agencies.

The earlier report suggested a declining percentage of agencies losing money, and it questioned whether a positive trend was evident or whether there was

simply less water entering the Titanic. The addition of two more years of data seem to suggest the latter alternative. Whether the percentage of agencies losing money is 38% or 31%, there are strong indications that the industry is unhealthy. Of course, a non-profit agency can continue to function with repeated annual losses. Typically, this is done by drawing on the net assets of the corporation. There will not be a 1:1 correspondence between annual losses and the status of net assets because net assets may grow for a number of reasons (stock market performance, bequests, donations, and real estate inflation). In such situations, net asset growth would be reduced by the amount used to cover losses in net income. Nevertheless, if the business portion of an agency is losing money, someone other than the primary funder is subsidising the business for it to continue.

Harvey and Tropman (2010) suggested several approaches that may have some utility in attempting to resolve this dilemma of expenses exceeding revenue. First, Harvey and Tropman counsel providers to reject all underfunded contracts. Rather than agreeing to make up any shortcomings via fundraising or drawing from one's net assets, no contract should be signed if it fails to cover legitimate costs. It is unlikely that any construction company working on a government contract knowingly signs a contract under which it will lose money. One must wonder why a CEO in the intellectual disability field would sign such a contract. A second suggestion pertains to a form of social entrepreneurship in which providers share the costs of services or combine the purchasing power in order to decrease costs. This approach has been called shared services (Bergeron, 2002). Harvey and Tropman (2010) suggested litigation as a third option, but the unfavorable outcome in the recent Idaho litigation would seem to discount this suggestion. For *Armstrong et al versus the Exceptional Child Centre et al*, the U.S. Supreme Court ruled that provider agencies lacked the standing to sue funders for failing to increase reimbursement rates (Heasley, 2015).

The notion that providers need to have revenues that exceed expenses by at least a small amount has been proven to be controversial. It has been argued that the retention of any sort of margin serves only to ensure that the money is not used for the benefit of people in need. While there is some degree of accuracy to this argument, one must recognise that the retention of margins is essential to the sustainability of non-profit agencies. Without margins, there are no provisions for emergency repairs, and the ability to borrow from banks is severely compromised. The elimination of reasonable margins will only further compromise the fiscal health of the system of provider agencies. It is for this reason that the rallying phrase of provider agencies has become "no margin—no mission."

Net assets can buffer an agency through challenging fiscal times by subsidising the underfunding from various governmental agencies. It must be noted, however, that many net assets are not liquid. Consider the real estate owned by many providers. Not only does it take considerable time to sell real estate, but also in many cases the real estate that must be sold is essential to the provision of supports and services. Nevertheless, one must consider the availability of net assets that may be used to offset the impact of annual losses. Consider the four provider agencies that lost money in each of the five years of study. The strongest of the agencies could continue to sustain these losses for 3.3 years, while the weakest agency already has a negative value for net assets. Obviously, these four agencies present extreme values, but they highlight the jeopardy facing the intellectual disability industry.

It must be recognised that while revenue has clearly increased, the data are somewhat difficult to interpret without reference to some measure of service units being provided. Given that there had been no rate increase for a number of years in Pennsylvania (in fact, a 10% reduction was imposed in 2012), the only reasonable explanation for increased revenue is that more individuals are being served. This is not truly an increase for providers of service, because they are now providing greater levels of service.

Is there a problem? Although an exceptionally large percentage of providers have expenses that exceed revenue, net assets increased by almost 16% over the five-year study. Companies, at least on paper, are worth more than they were five years ago. This suggests some validity to the Commonwealth argument that providers are doing well. It does not, however, excuse the funding agencies from failing to pay for at least the complete cost of the services and supports they have purchased. It appears that when a funder is able to set prices for services and supports they purchase, all risk of the venture falls to the provider agency.

CONCLUSION

Looking back at the study's objectives, it appears that the answers to the three questions are as follows:

- (1) About one-third of provider agencies have expenses that exceed revenue each year.
- (2) Despite these losses, net assets have grown by about 16% over a five-year period.

- (3) More money is entering the system, the value of which is likely offset by the provision of increased service units.

It would perhaps be unreasonable to rely on the political commitment to sustain the expansion of programmes and services for individuals who have an intellectual disability. A greater reliance on available and less expensive supports and services is needed. Perhaps this is why there appears to be growing support for adult foster care-type programmes, which can offer community integration at lower costs than traditional group homes. Other alternatives may involve mergers and acquisitions that may save money through the use of shared services (Bergeron, 2002).

Limitations

A major limitation is that this is a study of Pennsylvania providers of intellectual disability services, and the extent to which these findings may be applied to other states is not clear. Replications of this study in other states would be welcome.

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