GRAND CANYON INSTITUTE

Policy Brief

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Prop. 206: Impact on Developmental Disability Providers

Dave Wells, Research Director

Executive Summary

Prop. 206 has directly and indirectly impacted developmental disability providers. Part of the increase cost brings some workers up to the minimum wage as they were paid less than $10 an hour before (direct impact), and an additional amount will be provided to workers so they maintain a wage premium above the minimum wage (indirect impact). Governor Ducey's FY2018 budget set aside $15.6 million to cover added wage costs. The Joint Legislative Budget Committee (JLBC) estimates the costs at $22.5 million once sick leave and the $10.50 minimum wage on January 1, 2018 is considered. In sharp contrast the Arizona Association of Providers for People with Disabilities (AAPPD) estimate their costs for FY2018 at $58 million, plus a need for a $15 million additional supplemental allocation for FY2017.

The Grand Canyon Institute finds errors in the AAPPD calculation that when corrected requires no likely adjustment to the $7.7 million supplemental appropriation already provided for FY2017. The FY2018 appropriation should be between $18.5 and $21.1 million for FY2018, which is nestled between what the Executive Budget proposes and the JLBC estimate. The range of estimates is due to questions regarding what the average wage of direct caregivers was before January 1, 2017. The AAPPD argues that average wages were $9.54 an hour before Prop. 206 was implemented. By contrast, a survey of Arizona providers for the developmentally disabled by the National Association of State Directors of Developmental Disabilities Services and Human Services Research Institute found an average wage of $10.05 direct caregivers. The AAPPD number may have come from a survey of only 28 providers, while the national survey results included responses from 51 Arizona providers out of 322 identified in the state. Consequently, both average wage levels may be inaccurate, though the $10.05 level seems more in line with data found from other states, as the average wage was $11.11

across the 16 states and the District of Columbia in the national survey. The $10.05 figure is also more consistent with wage distribution of home healthcare aids for Arizona from the Bureau of Labor Statistics. Thus, $18.5 million is likely more accurate.

While the AAPPD calculations may be faulty, they have faced years of funding shortfalls due to a failure of the legislature to maintain benchmark funding since the recession. Rates rose just before the recession and then were cut sharply. Current provider rates adjusted for inflation are 12% below what they were in FY2007 and 21% below what they were in FY2009. An increase in rates of 8% to 9% related to Prop. 206 falls well short of that prior funding level.

The impact of Prop. 206 on wage levels and costs for disability providers is summarized below for the two average wage levels. The $18.5 million is likely more accurate.

	GCI from $9.54 avg. wage		**GCI from $10.05 avg. wage**	
	July-Dec. 2017	Jan.-June 2018	July-Dec. 2017	Jan.-June 2018
New Avg. Wage	$11.04	$11.39	$11.42	$11.77
Avg. Wage Increase	$1.60	$0.35	$1.37	$0.35
% Increase from Dec. 31 2016	15.8%	19.4%	13.6%	17.1%
Adjustments	Sick Pay +1.7% Turnover Savings -1.2%		Sick Pay +1.7% Turnover Savings -1.2%	
Total Increase	16.3%	20%	14.1%	17.6%
Low Wage +ERE as % of Total Costs	50%		50%	
Net Increase	**8.2%**	**10%**	**7.1%**	**8.8%**
Service Dollars Impacted	$379 M	$379M	$379 M	$379M
State Share	0.3076		0.3076	
Added Cost	$9.5 M	$11.6 M	$8.2M	$10.3 M
Total FY2018	**$21.1 M**		**$18.5 M**	

Details of Calculation

Arizona's minimum wage prior to January 1, 2017 was $8.05 an hour. In November Arizona voters approved Prop. 206 which raises the minimum wage to $12 in steps by 2020 starting with an initial increase to $10 an hour on January 1, 2017.

The details on the Executive's calculation of $15.6 million or the JLBC's $22.5 million don't appear to be publicly available. However, the AAPPD has provided the basis for their calculations. In the table below the Grand Canyon Institute calculations are contrasted with the AAPPD for FY2018.[1]

Table 1

	AAPPD from $9.54 avg. wage		GCI from $9.54 avg. wage		GCI from $10.05 avg. wage	
	July-Dec. 2017	Jan.-June 2018	July-Dec. 2017	Jan.-June 2018	July-Dec. 2017	Jan.-June 2018
New Avg. Wage	$10.85	$12.44	$11.04	$11.39	$11.42	$11.77
min wage increase	$1.95	$0.50	$1.95	$0.50	$1.95	$0.50
Avg. Wage Increase	$2.31	$0.59	$1.60	$0.35	$1.37	$0.35
% Increase from Dec. 31 2016	24.2%	30.4%	15.8%	19.4%	13.6%	17.1%
Adjustments	ERE 1.173 Sick Pay +2.5% Inflation 1.026		ERE 1.0 Sick Pay +1.7% Turnover Savings -1.2%		ERE 1.0 Sick Pay +1.7% Turnover Savings -1.2%	
Total Increase	31.7%	39.2%	16.3%	20%	14.1%	17.6%
Low Wage +ERE as % of Total Costs	70%		50%		50%	
Net Increase	**22.2%**	**27.4%**	**8.2%**	**10%**	**7.1%**	**8.8%**
Service Dollars Impacted	$379 M	$379M	$379 M	$379M	$379 M	$379M
State Share	0.3076		0.3076		0.3076	
Added Cost	$25.9 M	$32 M	$9.5 M	$11.6 M	$8.2 M	$10.3 M
Total FY2018	**$57.8 M**		**$21.1 M**		**$18.5 M**	

[1] Arizona Association of Providers for People with Disabilities (2017), "Please Support Additional Funding for DD Services," 2 page handout-their calculations on page 2 and for Prop. 206 in FY2016 summarized in Table 1.

From a broad view, the AAPPD estimate of $58 million for FY 2018 should raise doubts because the minimum wage on January 1, 2017 went up by about 25 percent, and they want their rates to go up by about 25 percent. But direct caregivers are not their only cost, and their direct caregivers, though definitely paid lowly, were making more than minimum wage to start.

Reviewing Table 1, the first difference is in the percent increase in wages.[2] The average wage goes up by more than the minimum wage increase under the AAPPD assumptions. That's not a plausible outcome in labor markets. The maximum increase would be the increase in the minimum wage. Economic models generally presume that workers earning above the minimum wage currently will see a portion of the increase with workers whose wages are much higher than the minimum wage, workers seeing little or no gain. So while the direct caregivers will see higher wages, someone earning twice the minimum wage would likely see no change. Because direct caregivers were already above minimum wage, they would see a portion of the increase to the minimum wage, not something larger than the minimum wage increase. So rather than a $1.95 increase in the minimum wage leading to $2.35 rise in average wages, GCI estimates the increases as $1.60 if the avg. wage is $9.54 and $1.37 if the avg. wage is $10.05.[3]

Employee Related Expenses include the cost, if offered, of employer paid health insurance, dental insurance, life insurance, disability benefits, FICA (Social Security and Medicare tax), paid leave time, paid vacation, unemployment insurance, and retirement benefits. Most direct caregivers have relatively modest benefits. Almost all of the benefits are directly proportional to one's wages. So for instance, if you get a day of paid vacation, the cost would rise proportionately if your pay rose.

Likewise, life insurance, retirement plans, and FICA are all proportional to the wage increase, so do not add to the percentage cost. The exception would be fixed cost expenses which remain the same when wages increase, such as health insurance. For simplicity and because relatively few workers have employer-provided health insurance in this industry in Arizona, GCI conservatively uses a 1.0 adjustment, meaning ERE goes up at the same rate as wages.[4] Consequently, AAPPD's use of ERE to make the percentage change larger is incorrect. You do want to include the cost of ERE in determining expenses impacted by higher wages, but the percentage change is not impacted for ERE that is proportional to wages.

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[2] $9.54 avg. wage likely based on a survey of 28 providers based on Rau, Alia Beard (2016), "After minimum-wage hike, Arizona companies serving people with disabilities to face a funding crisis," November 23, http://www.azcentral.com/story/news/politics/legislature/2016/11/23/arizona-minimum-wage-increase-social-services/94150408/ (accessed November 6, 2017).

[3] For $9.54, GCI takes 46 cents as mandated, and then wages go up 70 percent of the remainder of the min. wage increase ($1.95-$0.46). For $10.05, none is mandated, so GCI presumes wages go up 70 percent of $1.95.

[4] To give an illustration of how fixed cost benefits lower the percent, assume a caregiver's income went up from $15,000 to $18,000, a 20% increase. If her only benefit was health insurance that the employer provided $3,000 toward, then the wage+ERE change would go from $18,000 to $21,000, a 17% percent increase. Thus fixed cost benefits to the degree they are received lower the overall percentage increase in wage+ERE. GCI's more careful analysis based on Oregon data adjusted for lower benefits in Arizona estimates that employer provided health insurance was 1.4% of total wage and ERE costs.

If no employees currently had any time off, then the cost of paid sick leave would be approximately 2.5%, adding 5 days of paid leave per year for full and part time employees.[5] However, the survey by the National Association of State Directors of Developmental Disabilities Services and Human Services Research Institute found 20% of Arizona employers already offer paid time off for all employees and of the remainder about 30% offer it to full-time employees only.[6] For those workers, Prop. 206 will not have an impact. When that adjustment is made the cost of the added sick time is 1.7%, not 2.5%.

In addition, AAPPD reports a 56% annual turnover rate. The National Association of State Directors of Developmental Disabilities Services and Human Services Research Institute survey reported a 48% annual turnover rate. Turnover entails search, training, and lost productivity. Using the midpoint of the two, 52%, GCI estimates higher wages will reduce turnover to approximately 44%, and save providers 1.2% on their payroll costs.[7]

The AAPPD also adds in an inflation adjustment that seems irrelevant since direct caregiver costs are rising by more than inflation. The inflation adjustment would be relevant for costs not impacted by Prop. 206. GCI applies an inflation adjustment in its calculation for added appropriations <u>outside of Prop. 206</u> for Developmental Disability Providers.

Finally, AAPPD assumes that for direct caregivers wages + ERE are 70% of total costs. This figure seems excessively high. It very well may be that for all their employees' wages + ERE are 70% of total costs, not just direct caregivers. Using wage and expenditure data from Oregon which is far more comprehensive than what's publicly available for Arizona, GCI found for Providers for those with Intellectual and Developmental Disabilities (IDD) that wages + ERE were approximately 50% of total state and federal spending on IDD services.[8] This figure

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[5] Prop. 206 allows workers with larger employers to accumulate up to 40 hours of paid sick leave. GCI estimates that 60% of workers are part-time at 25 hours per week and 40% are full-time at 40 hours per week, yielding 1.643 as the typical hours worked, 40/1,643=2.4% (portion full-time and part-time from national survey for Arizona from National Assoc. of State Directors of Developmental Disabilities Services and Human Services Research Institute.

[6] National Association of State Directors of Developmental Disabilities Services and Human Service Research Institute (2016), "2015 Staff Stability Survey Report," November (revised December), http://www.nationalcoreindicators.org/upload/core-indicators/2015_Staff_Stability_Survey_Report_V22.pdf (accessed March 6, 2017).

[7] Many studies including the data from Oregon indicate that higher wages will reduce turnover, though other workplace variables such as working conditions are more important. A Montana study found turnover costs in 2002 of $2,607 per FTE worker. For purposes of this study, $3,000 was used per worker employed 1800 hours annuals for $9.54. The higher minimum wage is presumed to reduce turnover costs by 15%. This provides only a rough estimate of actual cost savings. Montana Study: Traci, Meg (2002),:"Direct Service Staff Turnover in Supported Living Arrangements: Preliminary Results and Observations," Research Progress Report #17. July, http://mtdh.ruralinstitute.umt.edu/?page_id=1511 (accessed March 1, 2017), Additional research on turnover Hewitt, Amy, and Sheryl Larson (2007),. "The Direct Support Workforce in Community Supports to Individuals with Developmental Disabilities: Issues, Implications, and Promising Practices." Mental Retardation and Developmental Disabilities Research Reviews 13: 178-87 and Seavey, D (2010)."The Cost of Frontline Turnover in Long-Term Care." Sept.

[8] For Oregon total spending on Intellectually and Developmental Disabilities (IDD)from Lewin Group (2016), "Bending the Curve: Opportunities to Promote Sustainability in Oregon's Long-Term Services and Support System:

included an assumption of ERE of 25%, greater than the 17.3% used in Arizona, because far more workers in Oregon are full-time and get benefits. In addition, it excludes any other sources of revenue from private pay patients. Private pay revenue would lower the wage + ERE cost as a portion of total cost.[9]

With these adjustments GCI finds that $18.5 million to $21.1 million for FY2018 is a more accurate estimate.

For the FY2017 supplemental, GCI estimates costs of $8.1 million for a $9.54 average wage and $6.9 million for a $10.05 average wage. These figures are consistent with the $7.7 million identified already for the supplemental allocation, so no added funding for FY2017 beyond what the Executive budget has identified is needed.[10]

Disability rate cuts outside of Prop. 206

While the AAPPD calculations may be faulty, they already had faced years of funding shortfalls due to a failure of the legislature to maintain benchmark funding since the recession. The current benchmark rates for disability providers are 5.2% above nominal FY2007 levels, but 6.8% percent below nominal FY2009 levels due a rise in rates in 2008 and cuts during the recession.[11] Consumer prices have risen 17 percent since 2007 and 13 percent since 2009. So collectively, once disability provider rates are adjusted for inflation, they are 12% below FY2007 levels and 21% below FY2009 levels. An increase in rates of 8% to 9% related to Prop. 206 falls well short of those prior funding levels.

Draft Final Report," Prepared for Oregon Department of Human Services; Aging and People with Disabilities and the Office of Developmental Disabilities Services, Feb. 10, http://www.o4ad.org/uploads/5/9/2/2/59228911/lewin_or_ltss_final_report.pdf (accessed March 6, 2017). For number of IDD employees, including wages, portion full-time, and benefits from Zuckerbraun, Sara, Joshua M. Wiener, et al.. (2015), "Wages, Fringe Benefits, and Turnover for Direct Care Workers Working for Long-Term Care Providers in Oregon", Prepared for Oregon Dept. of Human Services, January, Wages, Fringe Benefits, and Turnover for Direct Care Workers Working for Long-Term Care Providers in Oregon (accessed March 6, 2017)

[9] GCI estimates 15,243 direct care workers in Oregon from the report "Wages, Fringe Benefits, and Turnover for Direct Care Workers Working for Long-Term Care Providers in Oregon," The survey had an 82% response rate, so 1.25 adjustment was applied to give 19,053 estimated total workers. Avg. Wage =$12 with ERE at 25% and 1,825 annual hours per worker (assuming 65% @ 40 hrs. per week and 35% @ 26 hrs. per week) leads to a biennial wage + ERE bill of $1.043 billion. The Oregon Lewin report indicated total expected IDD biennial spending for FY2015-2017 of $2.017 billion, yielding a total wage + ERE cost of 51.7%, which given assumptions should be a high-end estimate, including that no other source of revenues are considered, e.g. private pay patients.

[10] Joint Legislative Budget Committee (2017), "Department of Economic Security: February 14 and 15, 2017 Appropriations Committee Hearings," p. 8, http://www.azleg.gov/jlbc/18desjlbcpres.pdf (accessed March 6, 2017).

[11] "State of Arizona Executive Budget Fiscal Year 2018," Douglas A. Ducey Governor, January 2017, p. 118, http://azgovernor.gov/sites/default/files/governor/documents/executivebudget-stateagencybudgets.pdf (accessed March 6, 2017).

Conclusion

The FY2017 supplemental of $7.7 million is adequate to address impacts caused directly and indirectly by Prop. 206. Likewise, GCI's estimated $18.5 million impact for FY2018 falls in line with the Executive and JLBC estimates of $15.6 million and $22.5 million, respectively. Funding to compensate for the impact of Prop. 206, however, will still leave disability providers below funding rates received prior to the recession.

Dave Wells holds a doctorate in Political Economy and Public Policy and is the Research Director for the Grand Canyon Institute, a centrist fiscal policy think tank founded in 2011. He can be reached at DWells@azgci.org or contact the Grand Canyon Institute at (602) 595-1025.

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Grand Canyon Institute

P.O. Box 1008

Phoenix, Arizona 85001-1008

GrandCanyonInsitute.org