

CITY AND COUNTY OF SAN FRANCISCO

BOARD OF SUPERVISORS

BUDGET AND LEGISLATIVE ANALYST

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April 23, 2021

TO: Budget and Appropriations Committee

FROM: Budget and Legislative Analyst

SUBJECT: April 28, 2021 Budget and Appropriations Committee Meeting



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Budget Analysis Report

To: Budget and Appropriations Committee
From: Budget and Legislative Analyst's Office
Re: Nonprofit Pay Equity & Sustainability
Date: April 23, 2021



Summary of Requested Action

We were asked to provide an analytical report on nonprofit pay equity. Specifically, we were asked to answer the following questions: (1) is the City ensuring the viability and sustainability of essential services that are contracted out to nonprofit organizations? and (2) is funding for these critical services keeping up with the cost of doing business and City mandates?

For further information about this report, contact Dan Goncher at the Budget and Legislative Analyst's Office.

Executive Summary

- The Minimum Compensation Ordinance (MCO) and cost of doing business increases (CODB) are the two primary budget allocations the City provides for annually adjusting pay to City nonprofit contractors. Over the past five years, the City has allocated \$8.7 million in funding for the MCO, \$67.3 million in CODB increases, and has an additional \$10 million in a minimum wage reserve to assist departments in meeting salary requirements for their nonprofit contractors.
- The MCO was first authorized by the Board of Supervisors in 2000 and amended again in 2007 and 2018. The MCO establishes hourly wage level requirements for three sectors of City contract workers: for-profit contractors, nonprofit contractors, and public entities (primarily comprised of In-Home Supportive Services (IHSS) workers).
- The MCO wage increased from \$9.00 in 2000 to its current rates (as of December 8, 2020) of \$17.05 for nonprofit contractors, \$17.25 for public entities, and \$18.24 for for-profit contractors. Over the past 10 years of MCO wage rates, the MCO has outpaced the increase in Consumer Price Index (CPI) for the San Francisco Bay Area. The FY 2020-21 and FY 2021-22 MCO wage rates for nonprofits (\$17.05) are \$1.89 higher than what it would be under routine increases solely tied to the CPI (\$15.16).
- As part of the 2018 amendments to the MCO, the Board required the Controller's Office to convene a Nonprofit Working Group, comprised of City, nonprofit, and labor union staff, to consider and advise on how to address equity concerns as part of increasing the MCO. Specifically, the Working Group was charged with looking at (1) wage equity, which is the inequity that occurs when workers funded by a City contract receive a higher wage

Budget and Legislative Analyst

than workers performing the same work but are funded by a non-City contract; and (2) wage compaction (indirect wages), which is the inequity that occurs when the difference between wage levels is reduced because one worker funded by the City contract receives an increased wage while other workers do not. In response to the group's recommendations, the Controller's Office ran an application process in 2019 to provide funding to nonprofits to help cover both direct and indirect wage increases. Of the \$6.6 million provided to nonprofits, 84 percent of this funding went to nonprofits contracted through the Departments of Children Youth and their Families (DCYF), Public Health (DPH), Homelessness and Supportive Housing (HSH), and the Human Services Agency (HSA).

- Of these four departments, most continue to use the Controller's initial findings from the 2019 survey to help allocate additional MCO funding. DCYF uses its own Contract Management System database that is updated annually. However, allocating the MCO is challenging given that there is no legal requirement to, nor a citywide policy on how to, address wage compaction and wage equity nor an ongoing centralized process for managing nonprofit allocation needs. In addition, there is no reasonably efficient universal methodology nor reliable data to assist with allocations. DPH, for example, uses a fee for service rate and does not have salary level data by individual to develop or validate data.
- CODB refers to funding that the City provides its nonprofit contractors to adjust for overall increases in costs year over year. This is not a cost of living adjustment or "COLA" as the CODB funding may be used for other purposes beyond increasing employees' wages. However, the departments we spoke with reported that it is generally the City's policy to encourage contractors to pass along any CODB increase to their employees through salary increases, and it is generally the belief that employees receive an increase as a result. Over the past five years, the CODB allocation has averaged slightly below CPI increases, 2.7 percent increase in CODB funding compared with 3.2 percent increase in CPI for the San Francisco area. However, the City's allocations have met or exceeded the CPI in the last two years.
- While most departments apply CODB increases to only their General Fund monies, HSA and DPH apply the increase to leveraged state and federal funds and DCYF works to use their Children and Youth Fund monies to cover CODB increases.
- In most years CODB increases are provided over two years and baselined into nonprofits' budgets for the second budget year. However, the FY 2020-21 increase is from one-time funding, which presents difficulties for departments in allocating the funding and for nonprofits on how to spend it. Receiving funding late in the year for FY 2020-21 because of the delayed budget also created a timing challenge for departments to allocate the funding, which was handled differently across departments. However, the funding was provided to the contractors. Two-year CODB allocations, which is the typical practice, are preferred by both departments and nonprofits as they can better anticipate funding, update contracts as needed, and reduce uncertainty.

- Understanding how CODB and MCO funding sources affect nonprofit contractors specifically is challenging given the variation in nonprofits themselves and how they operate internally. In order to improve upon the work the City has done, finding opportunities to streamline the MCO process in particular in combination with the CODB allocation could help improve transparency and reduce confusion.
- There is no citywide policy outlining how to provide hazard or incentive pay to nonprofit contractors delivering essential services during COVID. Our discussions with DCYF, DPH, HSA, and HSH confirm that departments took different approaches in determining how to budget and provide any additional pay to essential nonprofit service providers responding to COVID directly or indirectly. Generally, departments have worked with their nonprofit contractors on a case-by-case basis to determine what additional funding is needed to respond to COVID and how best to budget this.

Policy Options

The Board of Supervisors could:

1. Request that the Controller's Office and Mayor's Budget Office explore and report back to the Board on opportunities to regularly set a CODB funding level that includes any anticipated increased needs for MCO funding, which would provide more predictable increases to departments and nonprofit contracts on an annual and ongoing basis.
2. Request that the Controller's Office consider leading a regular periodic survey, at least every three to five years, of the City's nonprofit contracting partners to help assess the state of their workers and sustainability of services. Such a survey should include: (a) the number of workers at or just above the MCO wage rate and (b) other funding sources leveraged to help address wage compaction and wage equity concerns.

Project Staff: Dan Goncher, Emily Firgens

Overview

The City relies on nonprofit service providers to partner in ensuring that communities across the City have access to City services. Nonprofits provide vital services for San Francisco residents from health care to education to work supports and more. Ensuring the strength and stability of nonprofits is essential for the City's operation. Our analysis reviews a variety of questions and policies regarding pay for City nonprofit contractors to support their sustainability.

To answer the central questions of: (1) whether or not the City is ensuring the viability and sustainability of essential services that are contracted out to nonprofit organizations; and, (2) if funding for these critical services is keeping up with the cost of doing business and City mandates, we focused on four departments responsible for the majority of City contracts with nonprofits: the Departments of Children Youth and Families (DCYF), Public Health (DPH), Homelessness and Supportive Housing (HSH), and the Human Services Agency (HSA). In this report we look at the requirements and evolution of the City's efforts to support nonprofit workers through the Minimum Compensation Ordinance (MCO), allocation of cost of doing business (CODB) increases, and the opportunities and challenges with regard to implementing these policies. In addition, we analyze some of the unintended consequences of these policies and the wage equity questions they raise.

Related to nonprofit pay, we also review departmental policies with regard to COVID-19 hazard and incentive pay for nonprofit contractors providing essential services and the varying approaches taken by the four departments we focus on in this report.

Citywide Policy Requirements Encourage Higher Pay for Nonprofit Contractors

The History and Application of the Minimum Compensation Ordinance

The MCO requires most City contractors¹ to provide their covered employees² with: (1) no less than the MCO hourly wage in effect; (2) 12 paid days off per year or the cash equivalent if unable to provide time off; and (3) 10 days off without pay per year. These requirements are established in Chapter 12P of the City's Administrative Code, which was last amended in November 2018. With the 2018 amendments, described in more detail below, the City established new MCO hourly wage levels for three sectors of workers: for-profit contractors, nonprofit contractors, and public entities, which is primarily comprised of In-Home Supportive Services (IHSS) workers. Each sector has a different hourly wage level that increases annually on July 1. For nonprofit and for-profit

¹ Contractors are defined as a person or entity that enters into a services contract with the City or in the case of subcontractors, this applies to the subcontractor who enters into the subcontract with the contractor.

² Covered Employees are defined as: An employee of the contractor who performs any work funded in part or whole under the applicable contract or the project funded under the applicable contract either (1) within the boundaries of the City; (2) On property owned or controlled by the City, but outside of the City; or (3) Elsewhere in the United States.

workers these increases are in accordance with any increase in the prior year's Consumer Price Index (CPI); public entities' MCO wage rate increases slightly differently as written in the Administrative Code and discussed more below. Increases in the MCO are contingent on the sufficient funding in the budget to help nonprofits cover increased wage costs. As of December 8, 2020 the MCO hourly wage rates for each sector are:

- For-Profit Contractors: \$18.24
- Nonprofit Contractors: \$17.05
- Public Entities: \$17.25

Evolution of San Francisco's Minimum Compensation Ordinance

The Minimum Compensation Ordinance was initially adopted by the Board of Supervisors in August 2000³ and covers contracts that include professional services, construction, grants, Airport leases (including concession leases), and subcontracts. The MCO was established to help provide contractors and subcontractors with a wage that allowed them to better afford living in the San Francisco. The 2000 Ordinance set the MCO wage at \$9.00 per hour and required that in 12 to 18 months from the effective date of the ordinance, the hourly MCO wage increase to \$10.00 per hour so long that the Joint Report issued by the Controller, Mayor's Budget Office, and Budget Analyst found sufficient funds available to cover the anticipated costs of the adjustment. In the following three years, the City authorized an annual adjustment of 2.5 percent.

In August 2007, the Ordinance was amended to clarify provisions related to obligations imposed on contractors, processes for investigation, inspection and enforcement, and other various elements of the law.⁴ These updates to the MCO established an hourly wage for nonprofit contractors and public entities at \$10.77 with annual increases corresponding to the prior year's CPI increase. This provision was similarly established for for-profit contractors. However, when the Joint Report shows a budget shortfall there will be no automatic CPI increase in hourly gross compensation for nonprofit and public entities contracting with the City. The 2007 Ordinance required that, in years with a budget shortfall, the Mayor report on whether the proposed budget contains sufficient funding to cover the projected CPI increase for nonprofit contractors and public entities. In years where there is no budget shortfall anticipated, the Ordinance also requested a report on whether there is sufficient funding in the proposed budget to bring the rates for nonprofits and public entities into parity with for-profit contractors.

In November 2018, the Board approved amendments to the MCO, giving the Ordinance its current structure and increasing minimum compensation for nonprofit contractors to \$16.50 per hour as of July 1, 2019. The November 2018 MCO amendments also included annual increases starting July 1, 2020 and every year after on July 1 corresponding with the prior year's CPI increase. Contracts with public entities (IHSS workers) established an hourly gross compensation of \$16.00 per hour as of February 1, 2019, increased to: \$16.50 on July 1, 2019, \$17.50 on July 1, 2020,

³ San Francisco Ordinance [No. 216-00](#), File No. 001272.

⁴ San Francisco Ordinance [No. 212-07](#), File No. 070921.

\$18.00 on July 1, 2021, and \$18.75 on July 1, 2022. Starting July 1, 2023, the hourly gross compensation rate for public entities will increase by an amount corresponding to the prior year's CPI increase.

The November 2018 Ordinance maintains that the increases in hourly gross compensation will go into effect only if the City appropriates funds for the increases and the Controller certifies that such funds are sufficient to pay for the increased hourly compensation. If only a portion of the CPI increase can be covered then the wage will increase by that portion.

Contractors and Employees Covered by the Minimum Compensation Ordinance

The provisions of the MCO apply to contractors with five or more employees and organizations receiving \$25,000 or more in any fiscal year through a City contract; and, in the case of nonprofit corporations this threshold is \$50,000.⁵ Covered employees include those performing any work funded in part or whole under the applicable contract no matter where they reside in the U.S., inside or outside of San Francisco.

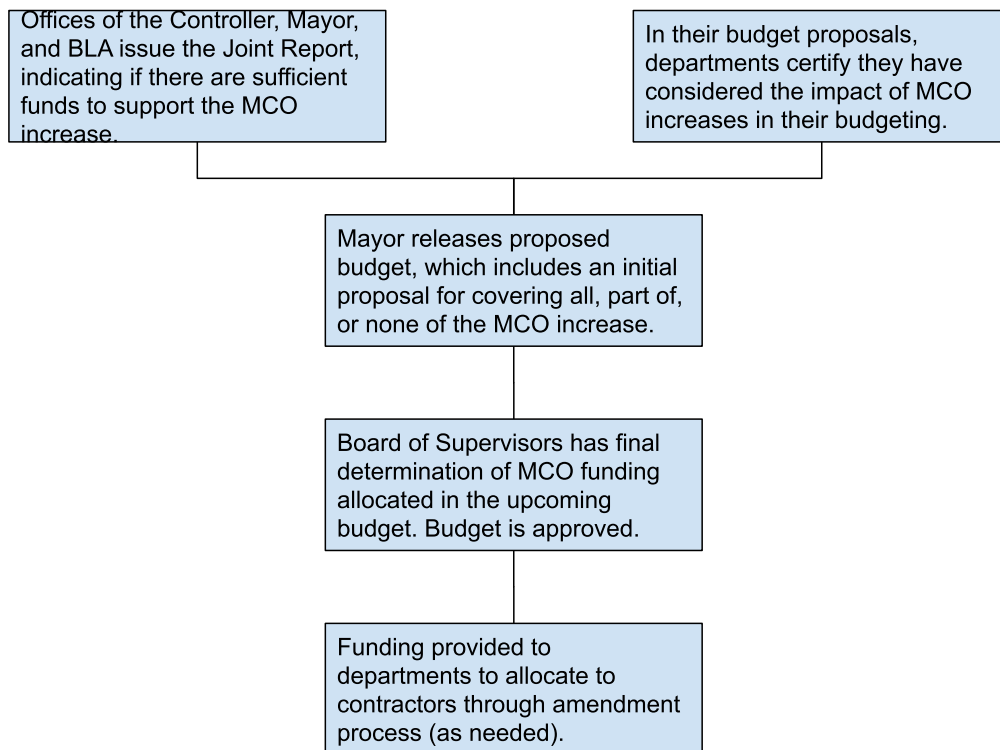
MCO requirements may be waived by approval of the Office of Labor Standards and Enforcement (OLSE) if the information is also verified by the contracting department. Waivers may be granted if services provided under the contract are only available from a sole source; the contract is necessary to respond to a public health or safety emergency and no entity that already complies with the MCO is capable of responding; the contract is for an essential project and there are not qualified prospective vendors that comply with the MCO; or services are being purchased through a bulk purchasing agreement, substantially reducing costs. OLSE's FY 2019-20 Annual Report indicates only three City contractors who obtained MCO waivers and all were for sole source contracts.

Current MCO Funding Allocation Process & Results of the Nonprofit Working Group

Exhibit 1 below provides an overview of how MCO funding is allocated, with the Joint Report indicating if there is sufficient funding, the Mayor and Board budget approval process, and departmental implementation.

⁵ The initial 2000 MCO ordinance applied to contractors with 20 or fewer employees; however, contract and contract amendments from October 14, 2007 are subject to five or fewer employees

Exhibit 1: MCO Budgeting Process



Source: Minimum Compensation Ordinance, Administrative Code Sec. 12P

As part of the 2018 amendments to the MCO, the Board required the Controller’s Office to convene a Nonprofit Working Group, comprised of City, nonprofit, and labor union staff,⁶ to consider and advise on how to address equity concerns as part of increasing the MCO. Specifically, the Working Group was charged with looking at: (1) wage equity, which is the inequity that occurs when workers funded by a City contract receive a higher wage than workers performing the same work but are funded by a non-City contract; and (2) wage compaction, which is the inequity that occurs when the difference between wage levels is reduced because one worker funded by the City contract receives an increased wage while other workers do not. The Working Group formally met three times to discuss the challenges with the MCO and propose how to allocate City funds across providers taking into consideration wage equity and wage compaction.

In April 2019, the Working Group published a set of seven recommendations that acknowledge the challenges of staffing and maintaining consistent services given the high cost of living and working in San Francisco, the varied experience and needs of the diverse nonprofits the City

⁶ The Working Group was comprised of the Controller, one representative from HSA and one from DPH, three nonprofit workers, two nonprofit executives, one representative from the San Francisco Labor Council, and one representative from SEIU 1021.

contracts with, and provided costs estimates for what the City would need to spend to address wage compaction and wage equity concerns.

In order to address wage equity and compaction, the working group estimated that the direct cost, or cost of lifting the lowest paid nonprofit workers on City contractors up the MCO, would be \$1.3 million. The working group estimated that wage compaction, or the “indirect” cost of lifting the wages for workers under \$30 per hour on City contracts, would cost \$12.9 million for a total of \$14.2 million. The group also estimated that the equity pressures created by the MCO for workers earning under \$30 per hour on non-City contracts would result in costs of \$12.7 million to the City if it was to be addressed.⁷ The Working Group recommended that the Controller run an application process where nonprofits submit information to the City regarding their needs and then have the City allocate funds based on the results of this survey and application process.

In preparing the FY 2019-21 two-year budget, the Mayor allocated \$3.3 million in FY 2019-20 and \$3.3 million in FY 2020-21 for the MCO and the Board of Supervisors increased this amount to \$5.8 million each budget year to offset the cost of the MCO increases. The Controller ran an application process to address the MCO-related costs of: (1) directly increasing wages of City contract workers at nonprofits to align with the new MCO; (2) wage compaction or the indirect change in wage levels because one worker funded by a City contract receives an increase while another worker doesn't; and (3) wage equity between workers on City and non-City contracts. The Controller's Office worked with City departments to distribute an application to over 850 nonprofits.

The Controller's Office worked with City departments, nonprofits, and labor stakeholders to allocate a total of \$6.6 million, the \$5.8 million budgeted for all departments and an additional \$800,000 appropriated to DCYF from the Children and Youth Fund to fund its own contractors' MCO costs. Upon completing the application process, the City distributed \$2.76 million for direct wage increases and \$3.8 million to address compaction across 515 contracts and 169 contractors. Ultimately, the City did not use any of the funding to address wage equity concerns as funds were limited and they chose to focus on workers funded through City contracts. The majority of funding, \$5.5 million or 84 percent of total funding, was distributed to DCYF, DPH, HSH, and HSA. Exhibit 2 below summarizes how funding was allocated to nonprofit contracts by department.

⁷ The three City staff representatives dissented to these estimates requesting that the group provide a range of costs to reflect the actual amount needed depending on the variable responses by nonprofits.

Exhibit 2: FY 2019-20 MCO Funding Allocation to Nonprofits by Department

Department	Number of Contracts	Total FTEs Funded	Total MCO Funding	Percent of Total Funding
Children, Youth & Their Families (DCYF)	166	372.30	\$1,112,070	17%
Homelessness & Supportive Housing (HSH)	69	762.60	1,789,840	27%
Public Health (DPH)	52	513.10	1,218,270	19%
Human Services Agency (HSA)^	82	584.90	1,384,350	21%
Subtotal DCYF, HSH, DPH, HSA	369	2,232.90	\$5,504,530	84%
All Other Departments*	146	524.10	1,062,110	16%
Grand Total	515	2,757.00	\$6,566,640	100%

^Within HSA's allocation, \$14,980 was provided to SF IHSS Public Authority.

*Includes: Adult Probation, Arts Commission, City Administrator, Building Inspection, Environment, Status of Women, District Attorney's Office, First 5 Commission, Human Rights Commission, Juvenile Probation, Mayor's Office of Housing and Community Development, Office of Economic and Workforce Development, Public Utilities Commission, Public Works, and Sherriff.

Source: Controller's Memo, "MCO: Summary of FY19-20 Allocations to Nonprofit Suppliers." Published November 5, 2019.

The Controller's Office reported that there were data validation issues as part of their survey and application process. The Controller's Office worked with City departments to validate the information reported by contractors, including making sure the full-time equivalent (FTE) amounts matched the FY 2019-20 contract information. There were errors for DCYF contractors and majority of grantees did not complete the survey. Using an equity lens, DCYF leveraged existing database information to include for this process. In addition, HSH administered a separate MCO application process in FY 2018-19, which created some confusion among the Department's contractors, so the Controller used data from the original process and from the FY 2019-20 contracts to determine the allocation amounts for HSH's nonprofit contractors.

While this process presented many challenges from surveying nonprofits to validating and correcting data, it centralized the effort to allocate MCO funding across the City and work to address wage compaction concerns. However, this was a one-time process and has not been updated by the Controller's Office. Our discussions with departments found that DPH, HSH, and HSA utilized the information from the Controller's process in 2019 to help determine allocations for the FY 2020-21 MCO because there is no other reasonably efficient methodology for allocating MCO funding. DCYF reported that they analyzed their extensive database that is updated annually to inform MCO funding and allocation.

The City's MCO Wage Increases Outpace CPI Over the Past 10 Years

The MCO has outpaced inflation over the past 10 years when comparing against increases in the San Francisco Bay Area CPI. The MCO wage increased from \$9.00 in 2000 when it was initially implemented to its current rates (as of December 8, 2020) of \$17.05 for nonprofit contractors,

\$17.25 for public entities, and \$18.24 for for-profit contractors. These rates will be in effect for part of FY 2020-21 and FY 2021-22, according to the Controller’s Office.

Exhibit 3 below shows that the FY 2020-21 and FY 2021-22 MCO wage rates for nonprofits (\$17.05) are \$1.89 higher than what it would be under routine increases with CPI (\$15.16). From 2010 to 2016 the MCO and CPI rose at similar levels with only a few cents difference. The 2018 amendments to the MCO, increasing the wage rate to \$16.50 encouraged this larger jump in the difference between the City’s actual MCO wage and CPI-adjusted MCO wage.

Exhibit 3: MCO Wage Increases Actual vs. CPI for Nonprofits, 2010-2020

Year	CPI Percent Increase	Actual MCO Wage (Nonprofits)	CPI Adjusted Wage	Difference
2010	1.4	\$11.54	\$11.54	--
2011	2.6	\$11.69	\$11.70	(\$0.01)
2012	2.7	\$12.06	\$12.01	\$0.05
2013	2.2	\$12.43	\$12.33	\$0.10
2014	2.8	\$12.66	\$12.60	\$0.06
2015	2.6	\$13.02	\$12.95	\$0.07
2016	3.0	\$13.34	\$13.29	\$0.05
2017	3.2	\$14.00	\$13.69	\$0.31
2018	3.9	\$15.00	\$14.13	\$0.87
2019	3.3	\$16.50	\$14.68	\$1.82
2020	1.7	\$17.05	\$15.16	\$1.89

Source: OLSE Wage Rates, U.S. Bureau of Labor Statistics CPI Annual Increases

Note: For years where there were multiple MCO wage rates issued, we took the wage rate that was most recently provided for that year.

In 2019, the City began allocated funding to support nonprofits in covering this increase in the MCO wage rate. Over the past two budget years the City has allocated a total of approximately \$8.7 million for nonprofit MCO-related adjustments. This includes the \$6.6 million (\$5.8 million for all departments plus \$800,000 in DCYF funding from the Children’s Fund) in FY 2019-20 and \$2.1 million in Proposition F⁸ funding in FY 2020-21. This funding allocation provides MCO support to both nonprofit contractors and public entities (primarily IHSS workers).

The FY 2020-21 budget did not initially include appropriations to support a full increase of the MCO as of July 1, 2020 due to projected budget shortfalls. However, the Board appropriated \$2,215,000 to support nonprofit wages contingent on the passage of Proposition F, the Business Tax Overhaul, in November 2020. Voters approved Proposition F, freeing up the use of funding to

⁸ Proposition F was a business tax overhaul on the November 2020 ballot.

support a nonprofit wage increase. Using the information from their 2019 application process, the Controller’s Office estimated the cost of increasing the MCO for the remainder of FY 2020-21 and FY 2021-22, as show in Exhibit 4 below. The Controller’s Office estimates that increasing the MCO would cost \$1.6 million for the remainder of FY 2020-21 and \$2.8 million in FY 2021-22.

Exhibit 4: FY 2020-21 & FY 2021-22 Cost of Increasing MCO (in millions)

	FY 2020-21 (Beginning 12/8/2020)	FY 2021-22	Total
Direct Costs	\$0.8	\$1.4	\$2.2
Indirect Costs	0.8	1.4	2.2
Total	\$1.6	\$2.8	\$4.4

Source: Controller’s Office

This information, released by the Controller’s Office in December 2020, indicates that there are sufficient funds from Proposition F to cover the MCO increases for the remainder of FY 2020-21 and FY 2021-22.

In addition to annual budget allocations to support the MCO, there is also a \$10 million minimum wage reserve. This reserve has been in the budget since FY 2018-19 and serves as a contingency funding source if departments do not have the funds to implement the required nonprofit wage costs.

Challenges of Allocating and Implementing Minimum Compensation Ordinance Funding

Our discussions with departments revealed that there are significant challenges to implementing support to nonprofits to comply with the MCO. As discussed earlier, wage compaction and wage equity remain two of the primary concerns surrounding the MCO. Currently, there is no legal responsibility for the City to address inequities in wages for workers on non-City contracts or workers on City contracts making more than the MCO, and there is also no citywide policy defining the City’s responsibilities to cover these costs. In addition, the nonprofits themselves vary tremendously and many nonprofits live and work across multiple jurisdictions.

The mechanics of the allocation process can also be difficult as the current process for allocating MCO funding is relatively new and was initially centralized through the Controller’s 2019 application and survey information, as previously discussed. In addition, there is not one easy to use formula that helps departments distribute MCO allocations. DPH, for example, uses a fee for service rate and does not have salary level data by individual to develop or validate data. While wage compaction was addressed through this process to some extent, there were concerns around the validity of the data and departments’ abilities to confirm the information submitted by nonprofits. The Controller’s process provides a template for centralizing MCO funding allocations, but this was a one-time effort and it is unclear how the process will move forward as this information has not been annually updated across the City and could quickly become out of date. A few departments expressed support in our interviews for addressing MCO increases through the

CODB allocation and not having separate allocation processes for the MCO and the indirect costs of wage equity and wage compaction. A combined process that provides one allocation amount has the potential to give nonprofits more flexibility in how the funding is spent and the potential to better match their internal needs. The CODB allocation is discussed more below.

Health Care Accountability Ordinance Appears to have Limited Impact on Nonprofit Contractors

The Health Care Accountability Ordinance (HCAO) is an additional policy requirement for City contractors. The HCAO requires that employers offer health plan benefits to their covered employees (employees working 20 or more hours per week), make payments to the City for use by DPH, or make payments directly to the employees. However, the HCAO does not apply to nonprofit corporations with fewer than 50 employees and does not include contracts that are grant awards from the City to a nonprofit corporation.⁹ However, DPH currently has contract agreements and not grant agreements. As such, the Office of Contract Administration requires that each contract have a corresponding MCO and HCAO declaration of compliance or approved waiver if applicable on file in order to approve the contract.

Our discussions with all four departments covered in this report indicated that the provisions of the HCAO have not been a concern for nonprofits. According to the departmental contracting and budget staff we spoke with, either few of their nonprofit providers are covered by the HCAO or meeting the requirements of the HCAO has not been identified as a concern. However, a few departments did discuss rising fringe benefit costs for nonprofit contracts, which could indicate that nonprofit organizations are facing additional overall health care costs.

Enforcement of the MCO and HCAO

The Office of Labor Standards and Enforcement (OLSE) is responsible for monitoring and investigating compliance with the MCO and HCAO policies. OLSE reports that within the past three years there have been 10 MCO and HCAO violation cases that have involved nonprofits and six of these cases have resulted in some amount of restitution to workers. Of these cases, seven have been closed and three remain open. Of the open cases, two involve payment of restitutions to workers.

While there are few reported cases of noncompliance with MCO and HCAO over the past three years, OLSE staff note that it is difficult to conclude how widespread compliance is. OLSE reports that cases are often the result of employee complaints, and that there may be many reasons why an employee is reluctant to file a complaint about an employer.

Cost of Doing Business Increases Provide Additional Support to Nonprofits

Cost of doing business increases (CODB) refers to funding that the City provides its nonprofit contractors to adjust for overall increases in costs year over year. This is not explicitly a cost of

⁹ San Francisco Administrative Code, Sec. 12Q.3(g) and Sec. 12Q.2.4(b)(11)

living adjustment or “COLA” as the CODB funding may be used for other purposes beyond increasing employees’ wages. However, the departments we spoke with reported that it is generally the City’s policy to encourage contractors to pass along any CODB increase to their employees through salary increases. The CODB funding allocated by the Mayor and Board of Supervisors is funding that is in addition to the MCO funding discussed above.

Citywide Budgeting of Cost of Doing Business Increases

Over the past five years the CODB allocation has averaged 2.7 percent per year. Exhibit 5 below shows the percentage change each year over the past five years. While this percent increase reflects the adjustment each nonprofit contractor can expect to see in their annual budget for that year, the City as a whole budgets a total amount that is distributed to departments. Exhibit 5 shows that over the past five years the City has budgeted a total of \$67,276,501 in CODB adjustments for nonprofits. While the percent CODB increase for each year has stayed at 2.5 or 3 percent, the total amounts budgeted have fluctuated more. While this may vary depending on the number of contracts and nonprofit funding provided in a current year, the total amount has ebbed and flowed between \$12.4 million, the lowest allocation in FY 2017-18, and \$16.2 million, the highest allocation in FY 2019-20.

Exhibit 5: Percent CODB Increases, FY 2017-18 through FY 2020-21

Fiscal Year	Percent CODB Increase	Amount CODB Budgeted	Percent Change in Budgeted Amount
2016-17	2.5%	\$12,433,327	--
2017-18	2.5%	\$12,909,117	3.8%
2018-19	2.5%	\$13,092,848	12.9%
2019-20	3.0%	\$16,241,209	24.0%
2020-21	3.0%	\$12,600,000	-22.4%
Total		\$67,276,501	

Source: FY 2016-17 through FY 2020-21 Budgets

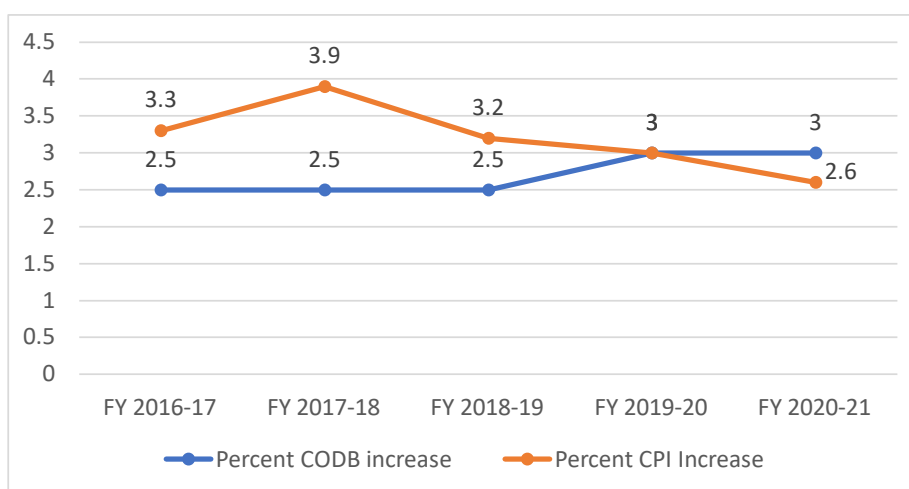
Typically, the budget includes CODB increases for both years of the two-year budget cycle. Over the past five budget years, the only year that the Mayor and Board did not propose the same increase in CODB funding was FY 2020-21. Given projected budget shortfalls from the impacts of COVID-19 there was disagreement over whether to provide the CODB increase. The eventual FY 2020-21 CODB increase approved by the Board was also for *one-time* funding of \$12.6 million. Typically, the CODB increase is budgeted as *ongoing* funding.

When comparing the CODB increases with changing CPI over the past five years, CODB has averaged slightly below CPI increases, 2.7 percent increase in CODB compared with 3.2 percent increase in CPI for the San Francisco area. This assumes that the prior calendar year’s CPI would correspond to the upcoming budget year’s increase. Exhibit 6 below shows that up until FY 2019-20, CODB increases were falling below the prior year’s CPI percent increase. FY 2020-21 is the first

year in the past five years the CODB increase exceeded the prior year's CPI. However, as previously mentioned, the FY 2020-21 amount is *one-time* funding that will not be baselined into nonprofit's budgets for FY 2021-22.

Looking forward, the City anticipates receiving \$636 million in one-time direct federal aid through the American Rescue Plan Act.¹⁰ This funding will offset revenue losses that were previously anticipated in the General Fund, leaving a shortfall of \$22.9 million in the upcoming two-year budget. This is an improvement of \$630.3 million from the previously anticipated projected deficit of \$653.2 million in January 2021. The full effects of this funding are still being determined. Because this is one-time aid, any potential funding available for nonprofit contractors should be allocated with this one-time purpose in mind. It offers the opportunity to consider using funds for technical assistance and strategic planning goals rather than for items needing on-going support.

Exhibit 6: Percent CODB Increase vs. CPI Increase, FY 2016-17 through FY 2020-21



Source: HSA, U.S. Bureau of Labor Statistics CPI Annual Increases

Department Policies for Allocating CODB Increases

Similar to the MCO increases, the CODB allocations must be approved by the Board through the annual budgeting process. As mentioned above, the budgeting process typically allocates two years' worth of CODB increases, which provides a level of continuity for nonprofits and departments when they head into the second year of the two-year budget cycle. A few of the departments we spoke with discussed challenges with the timing of the CODB increases, given that it can be hard to anticipate what the final budget will be and adjust contracts appropriately. DPH staff reported that this occurs when an extra half percentage is added toward the end of the budget process. Providing more certainty in what to anticipate each year through an annual, automatic CODB would be beneficial for both departments and nonprofits.

¹⁰ [Budget Outlook Update \(March Update to the Five-Year Financial Plan\)](#). March 31, 2021.

Once the budget is approved by the Board and Mayor, departments apply the CODB increases to their nonprofit contractors. Exhibit 7 below summarizes the varying policies for how the four departments we interviewed appropriate the CODB increases. Generally, the funding is only applied to General Fund dollars. However, HSA and DPH apply a CODB increase to leveraged state and federal dollars given how extensively their funding is blended. Departments will also often request that nonprofits provide an updated budget, which identifies where they allocated the CODB funding; however, some departments, like HSH, are not requesting an updated budget for the FY 2020-21 CODB due to the one-time nature of the FY 2020-21 CODB increase and timing purposes. This is also the case for DPH. The City is paying the calculated CODB for DPH contractors directly through a Direct Voucher payment, as timing would not allow for all contracts to be revised to add this funding into the budget detail. From our discussions with departments both on the implementation and nonprofit side, it is difficult to build a one-time CODB into salaries, which is an ongoing cost. While the one-time FY 2020-21 CODB allocations were likely an aberration due to COVID-19, a return to two-year CODB allocations is preferred by both departments and nonprofits as they can better anticipate funding, update contracts as needed, and reduce uncertainty.

Exhibit 7: Departmental CODB Allocation Policies

Department	Funding Sources Eligible for CODB Increase	How CODB Can Be Applied
Children, Youth, and Their Families	Apply General Fund portion of CODB funding then work to use the Children and Youth Fund to cover remaining nonprofit providers. (The Children and Youth Fund is approximately 70 percent of DCYF’s Operating Budget.)	Calculated as a percentage of a grant amount. It is added in the second and subsequent years of ongoing grants.
Public Health	<p>Allocation based on overall General Fund dollars, including work orders. This includes almost all non-grant funding, like MediCal and Realignment.</p> <p>Grant funding and funding provided through the Mental Health Services Act are not included in CODB increases.</p>	<p>CODB is allocated as a percentage of overall agency funding, to the bottom line of the contract. Agencies may spend the funding as needed, but they are encouraged to pass on the equivalent increase to employees.</p> <p>DPH budgets as units of services and allows an increase in service rates without the expectation of additional units.</p>
Human Services Agency	<p>CODB increase is typically applied to General Fund money and leveraged state and federal funds.</p> <p>CODB is not applied to pass-through funds, new programs, or add-backs.</p> <p>HSA’s set aside funds, the Dignity Fund and Public Education Enrichment Fund, cover CODB increases for providers supported through these sources.</p>	Once allocation is approved, HSA will notify providers of what the CODB can apply to, which in FY 2020-21 includes: salaries and associated benefits, operational costs (excluding direct client assistance, capital equipment or capital improvement costs funded by the Department), and indirect costs.
Homelessness and Supportive Housing	<p>Allocated to General Fund dollars. This excludes:</p> <ul style="list-style-type: none"> • Non-General Fund money (U.S Department of Housing and Urban Development or state funds are not included.) • Add-backs, Mayoral Enhancements, and/or new programs for the first time in the fiscal year. • Pass-through funds (Whole Person Care) • One-time funds, including carried over one-time funds. 	<p>Funding cannot be applied to:</p> <ul style="list-style-type: none"> • Direct client assistance dollars (rental assistance, subsidies) • Capital equipment • Capital improvements funded by HSH <p>Typically request nonprofits to re-submit allocated funds in budget; however, did not request FY 2020-21 budgets because CODB was one-time.</p>

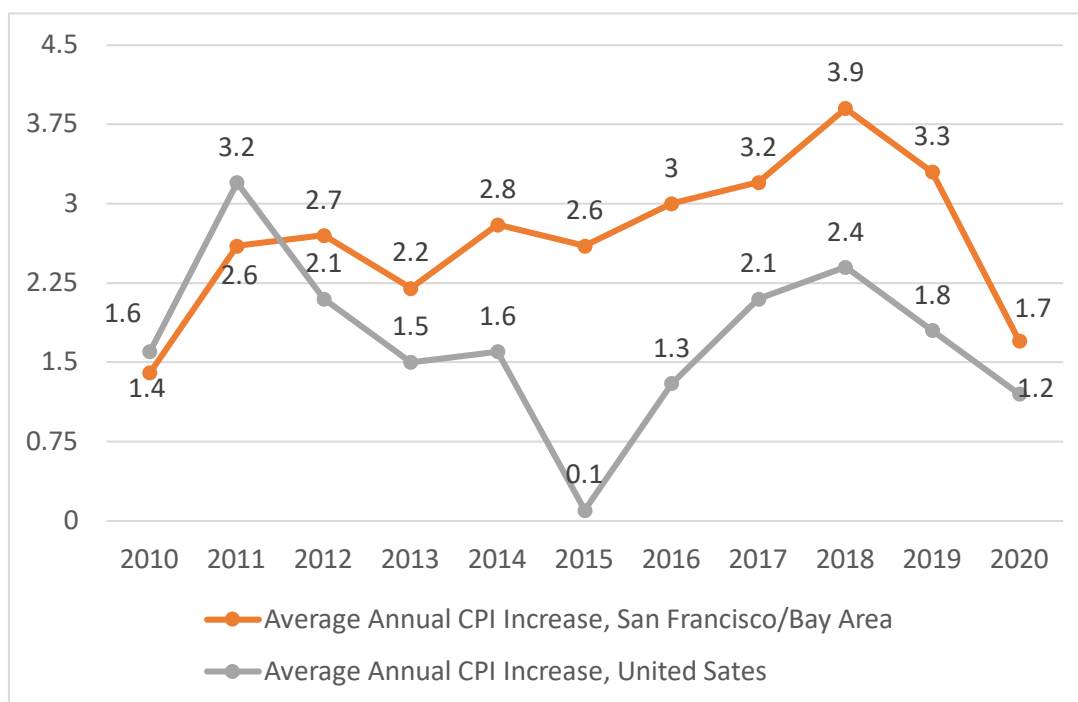
Source: Written polices and interviews with DCYF, DPH, HSA, and HSH

Rising Costs in the Bay Area

San Francisco and the surrounding Bay Area's high cost of living is well documented. According to the U.S. Bureau of Labor Statistics, the average annual total expenditures for a consumer in the San Francisco Bay Area in FY 2018-19 was \$87,287, which is 40 percent higher than the average for the U.S. (\$62,395).¹¹ Housing makes up the largest portion of average expenditures, at \$31,960 in the San Francisco Bay Area, which is roughly 37 percent of a consumer's overall annual expenditures. This is not surprising as it is also well documented that average Bay Area rent prices have grown considerably in the last 10 years. According to the Department of City Planning's Housing Affordability Strategies paper, a household would need to earn approximately \$169,000 per year to afford the median rent in 2019 of just over \$4,000 per month.¹²

Between 2010 and 2020, the average annual increase in CPI in the San Francisco Bay Area was 2.7 percent compared to 1.7 percent across the U.S. Exhibit 8 below shows the consistently higher increases in the Bay Area's CPI relative to the United States as a whole.

Exhibit 8: Average Percent Increases in CPI, San Francisco/Bay Area vs. U.S. (2010-2020)



Source: U.S. Bureau of Labor Statistics

As discussed earlier, while the CODB allocations have not increased over the past five years at the same rate as CPI increases, the MCO wage has risen more than what it would have had it been

¹¹ U.S. Bureau of Labor Statistics, [San Francisco Area Economic Summary](#), April 8, 2021.

¹² SF Planning, [Housing Affordability Strategies Report](#), March 2020.

only tied to CPI increases. However, over the past two fiscal years, the CODB allocations have met or exceeded the CPI and (as previously discussed) the City has provided an additional \$6.6 million and \$2.1 million in FY 2019-20 and FY 2020-21 respectively to support nonprofits in meeting the MCO requirement. Taken together, the City appears to be getting closer to meeting the increased needs of nonprofits given the increase in the MCO and other costs. However, it is still incredibly challenging to live in the San Francisco Bay Area on a salary of \$17.05 an hour given the high cost of living. An hourly wage of \$17.05 equates to an annual salary of \$39,464, which is considered “very low income” by the U.S. Department of Housing and Urban Development (HUD) as it is less than 50 percent (39.6 percent) of the San Francisco metro area median income.

Generally, large drivers of rising costs include increasing housing and food costs. Our conversations with departments confirm that nonprofits reported similar challenges with these expenses. Nonprofits voiced concerns to departments more generally around increasing salaries and worker retention as being the main drivers of their rising costs.

In addition, nonprofits experience rising costs unique to their subsector. For example, meal providers at HSA see increasing food costs whereas HSH reports contractors that master lease a site will sometimes see increases over the CODB in their leases. Rent is a cost burden that typically hits a nonprofit all at once when their lease is up for renewal. However, given the variety of services and structures of nonprofits the City contracts with we do not have a comprehensive picture of the scale of each of these areas of increased costs.

A December 2019 report from San Francisco State University analyzes the state of San Francisco’s nonprofit sector, finding that between 2012 and 2016 nonprofits in San Francisco were generally able to keep up revenue to meet their expenses.¹³ The study also found during this period that nonprofit employment and wages fell and did not maintain the same pace of employment and wages paid in for-profit and government sectors. However, for 501(c)3 nonprofit corporations the number of employees increased eight percent and wages paid increased 19 percent. The study also found that between 2012 and 2016 almost all nonprofits (94 percent) stayed in San Francisco during this time – this was slightly lower compared to statewide (99 percent) or the rest of the Bay Area (98 percent). While the study finds that the sector as a whole is financially healthy it stresses a similar theme that there is variation depending on nonprofit size and subsector.

Additional Considerations for Nonprofit Pay

Pay Inequities Between City and Non-City Staff

As part of this report we sought to better understand the extent of pay inequities between City and non-City staff that are contracted to perform comparable work. Throughout our discussions with departments we were told anecdotally of inequities in pay between City staff who are paid more than non-City staff contractors who are performing similar work. While this is a concern it is unclear the scale of this issue. DPH confirmed that this is a concern brought up frequently and

¹³ San Francisco State University, San Francisco’s Nonprofit Sector 2019 Final Report. December 2019.

recently in the case of Case Investigation, Contact Tracing workers for COVID-19 response. Nonprofit workers advocated and were able to receive a salary premium to make their wages more comparable to the civil service health workers. However, this case appears to be unique given the circumstances of responding to the COVID-19 pandemic.

There is no known legal or policy requirement that the City match compensation between City and non-City workers for similar jobs. Further, it would be challenging to match full City compensation through additional resources to nonprofit contractors given the level of benefits available through City employment. However, concerns continue regarding the inequity in not matching compensation. Further study about the scale and extent of these wage differences is needed to better understand the problem and potential solutions.

How Much Funding for Services is the City Not Covering?

An additional question that was raised as part of this report is related to how much nonprofits contracting with the City rely on additional sources of funding to provide services and what portion of funding for services to residents the City does not cover as part of their contracts. This too was a difficult question to answer given the variety of nonprofits and services provided and the lack of a comprehensive database that records the other funding sources a nonprofit is leveraging. Some departments are able to address this issue by providing a CODB to funding sources that are leveraged. For example, HSA and DPH report that CODB increases are applied to the leveraged state and federal funds. DCYF reports that it tracks other sources of funding for all its providers. Data from FY 2019-20 shows that DCYF awarded over \$101.3 million across 389 program contracts. Combined, these programs received an additional \$194.6 million from other funding sources. Across all of these contracts, DCYF funding accounted for approximately 34 percent of total funding received by these programs.¹⁴ This information provides an indicator for how much additional funding City monies help leverage through DCYF, but it does not indicate if City funds are inadequately covering costs.

COVID-19 Hazard and Incentive Pay Policies

Citywide Policies on Nonprofit Contractor Budgets during COVID

Over the course of the City's pandemic response, the Controller's Office has issued a series of policy guidance on payment continuity for nonprofit providers as it relates to disruptions to services because of the shelter-in-place orders. The initial policy, provided on April 4, 2020, authorized continued City payments for non-essential services provided by nonprofits even if these programs were closed or services provided remotely. The guidance also sought to provide the City and its nonprofit contractors with budget flexibility to accommodate new needs and adapt to potential changes in service delivery. The guidance, initially set to expire on May 3, 2020,

¹⁴ The Shelter-in-Place order issued in March 2020 impacted programming and reporting. DCYF followed Controller's guidance including making continuity of payments to nonprofit providers. In addition, the program budget numbers are not revisited at the end of the budget for year-end reconciliation.

was extended to May 31, 2020 and then again to June 30, 2020. On August 6, 2020 this policy was extended until September 30, 2020. At that time departments could request extensions for contracts that were still experiencing COVID-related disruptions in service.

This policy provided continuity of payment for City nonprofit service providers who were unable to perform their work or needed to modify services in order to follow public health guidance concerning COVID.

Departmental Action on Nonprofit COVID Pay

There is no citywide policy outlining how to provide hazard or incentive pay to nonprofit contractors delivering essential services during COVID. Our discussions with DCYF, DPH, HSA, and HSH confirm that departments took different approaches in determining how to budget and provide any additional pay to essential nonprofit service providers responding to COVID directly or indirectly. Exhibit 9 below provides a summary of these different approaches. HSH was able to provide the most comprehensive COVID-related bonuses to front-line nonprofit providers through an allocation of \$10.1 million in Proposition C (Our City, Our Home) funding. This funding from HSH is intended for front-line workers and not for managerial-level, administrative/indirect costs, or staff to work remotely. Generally, departments have worked with their nonprofit contractors on a case-by-case basis to determine what additional funding is needed to respond to COVID and how best to budget this.

Exhibit 9: Department Response on COVID Pay for Nonprofits, as of April 2021

Department	Nonprofit COVID-Related Pay Response
Children, Youth, and Their Families	<ul style="list-style-type: none"> • Provided additional funds as needed for nonprofits. This has varied as providers have had to pivot their service model depending on needs (e.g. moving from part day to full day programming to offer services through the Community Hubs supporting distance learning in light of school closures).
Public Health	<ul style="list-style-type: none"> • Allowed contractors to reduce their units of services up to 25 percent, which allows for an increase in their unit of services rate. This helped compensate for the reduction in clients while still allowing them to draw down their necessary contract funding. • Case Investigation, Contract Tracing contractors received a salary premium. • Some contractors who hired new staff received a higher rate.
Human Services Agency	<ul style="list-style-type: none"> • \$2 increase in hazard pay for IHSS workers providing back-up care. • Covered additional cleaning or other expense increases related to COVID. • Nutrition grants received additional funding to meet increased needs.
Homelessness and Supportive Housing	<ul style="list-style-type: none"> • January 2021: Allocated \$10.1 million in Proposition C funding to provide one-time COVID-19 provider bonus pay to eligible nonprofit employees providing HSH services and housing during the pandemic. <ul style="list-style-type: none"> ○ Allocation calculated based on number of FTE front-line workers earning less than \$25/hour. Bonus is an additional \$5/hour and covers 12 months of costs. Includes an additional 20 percent on top of this FTE calculation to address a grantee’s internal pay structure or equity concerns. ○ Does not include new programs or agreements that negotiated a higher wage. • Spring 2020: Used FY 2019-20 General Fund savings to provide incentive pay to nonprofits responding to COVID.

Source: Interviews with DCYF, DPH, HSA, and HSH

Conclusion

The City relies on nonprofit providers to deliver vital services. The nonprofits themselves vary significantly in size, service area, and service delivery and it is therefore difficult to get a full picture of their individual needs and challenges. Further, City departments have varying types of contractual relationships with, and abilities to determine need of, their nonprofit partners.

Increases in the MCO wage requirement have outpaced CPI increases over the past 10 years, which has put greater strain on the City's nonprofit providers. The past five years of annual CODB allocations has fallen just shy of the CPI increases with the CODB increase averaging 2.7 percent per year since FY 2016-17. The City has made a number of additional efforts to fund increases for nonprofit contractors and ensure their sustainability, including \$8.7 million in support for nonprofits to comply with the MCO over the past two years. Despite these efforts, concerns remain around nonprofit sustainability and the inequities that arise as a result of the MCO for nonprofits.

Understanding how CODB and MCO funding sources affect nonprofit contractors specifically is challenging given the variation in nonprofits themselves and how they operate internally. In order to improve upon the work the City has done, finding opportunities to streamline the MCO and CODB funding processes and add more predictability could help improve transparency and reduce confusion. In addition, the City should look to strategically using one-time funding sources for investments that can help build nonprofit capacity without adding to their ongoing costs.

Policy Options

The Board of Supervisors could:

1. Request that the Controller's Office and Mayor's Budget Office explore and report back to the Board on opportunities to regularly set a CODB funding level that includes any anticipated increased needs for MCO funding, which would provide more predictable increases to departments and nonprofit contracts on an annual and ongoing basis.
2. Request that the Controller's Office consider leading a regular periodic survey, at least every three to five years, of the City's nonprofit contracting partners to help assess the state of their workers and sustainability of services. Such a survey should include: (a) the number of workers at or just above the MCO wage rate and (b) other funding sources leveraged to help address wage compaction and wage equity concerns.