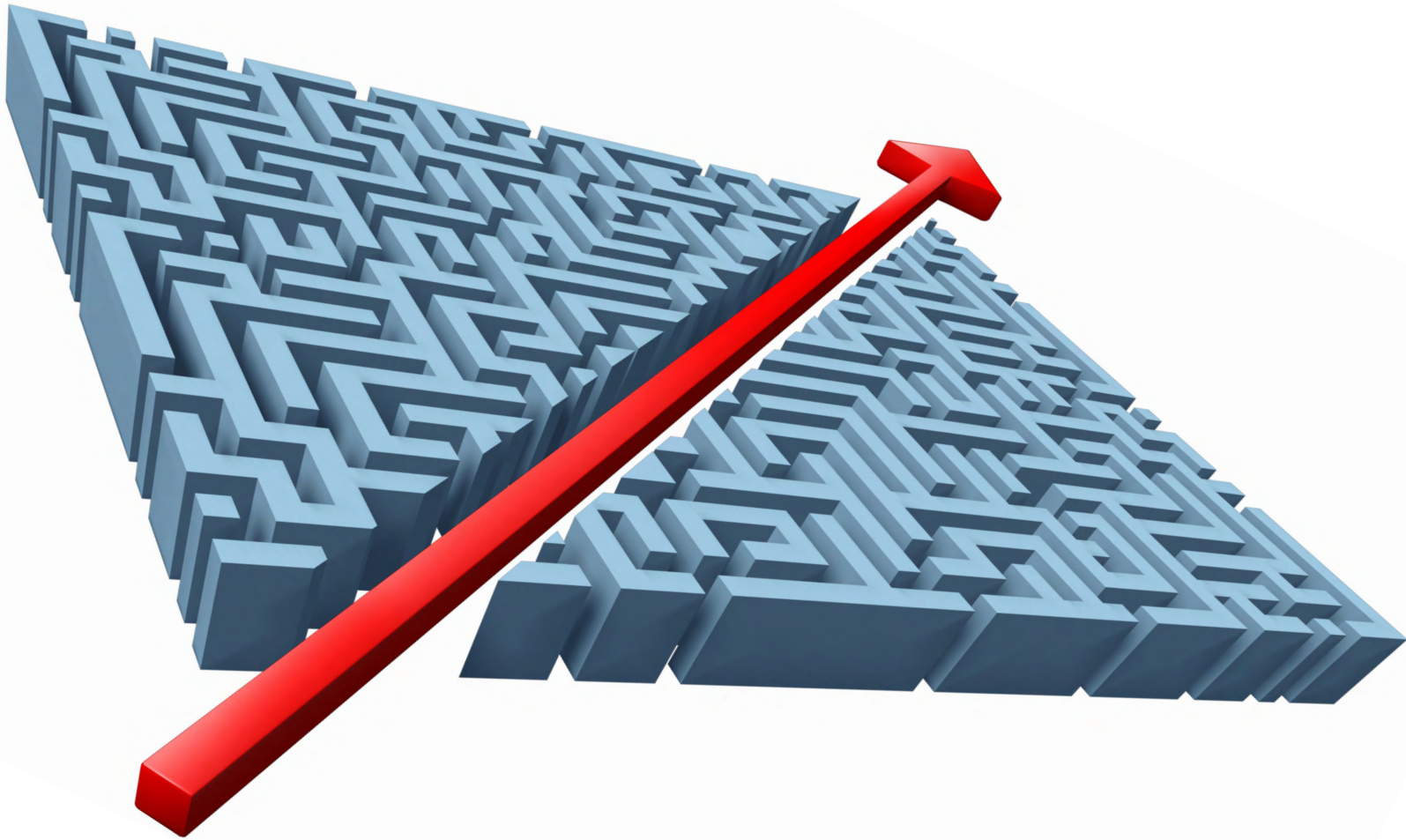


Toward Common Sense Contracting

What Taxpayers Deserve



**A Special Report focused on solutions
to improve government-nonprofit contracting issues**



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NONPROFITS**

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ABOUT THIS SPECIAL REPORT

This Special Report is designed to help overcome the serious problems charitable nonprofits encounter when entering written agreements with governments to deliver services to the public. Through extensive research and input from front-line nonprofit contractors and grantees, it provides real-world context and consequences to the problems documented through nationwide statistical data published by the Urban Institute's Center on Nonprofits and Philanthropy in its new *National Study of Nonprofit-Government Contracts and Grants 2013: State Profiles* and recent *Nonprofit-Government Contracts and Grants: Findings from the 2013 National Survey*. This report provides tested, replicable solutions to the government-nonprofit contracting problems and calls on all interested parties to join in efforts to promote common sense contracting.

ABOUT THE PROJECT

Since at least the 1960s, and accelerated in the 1980s, all levels of government have been entering written agreements with charitable nonprofits to deliver a broad array of services to the public. Governments have largely found nonprofits to be good partners: mission-driven rather than profit-focused, and more efficient and effective than unwieldy government bureaucracies. In return governments have paid late, changed contract terms mid-stream, and required increasing levels of burdensome complexity in applications and reporting requirements. These and other government contract and grant problems were exacerbated and exposed by the Great Recession. But there was little empirical research documenting the extent and severity of the harmful practices that weaken the ability of nonprofits to serve the public.

In 2009, the National Council of Nonprofits and the Urban Institute's Center on Nonprofits and Philanthropy began a multi-year collaborative project to identify the scope and depth of the problems that charitable nonprofits face when contracting with governments. In 2010, the Urban Institute published results from the first national survey, documenting the serious and widespread contracting problems. That study, which focused solely on nonprofit human service providers under contract with governments, found that many governments routinely fail to pay the full costs of the contracted services, impose unnecessary and wasteful burdens, and do not honor their legal obligations of the written contracts they signed — all of which add unnecessary costs to governments and nonprofits alike. A companion report by the National Council of Nonprofits provided additional context and proposed solutions that government officials and nonprofit leaders can adopt to improve services, restore value for taxpayers, and strengthen communities.

Since then, the National Council of Nonprofits has worked through its network of state associations of nonprofits and with governments at the local, state, and federal levels to help repair the broken contracting “system” by building relationships, identifying solutions and promising practices that can be replicated in multiple jurisdictions, and advocating for their implementation.

Special Report

Toward Common Sense Contracting: What Taxpayers Deserve

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This Special Report is dedicated to the many selfless government employees and officials who share the commitment of their nonprofit partners to improving the lives of their fellow residents. The fact that millions of people receive the services they need through nonprofits is testimony to the dedication of these public servants in overcoming the system's many frustrating flaws.

TOWARD COMMON SENSE CONTRACTING: WHAT TAXPAYERS DESERVE

Executive Summary

The latest data from the Urban Institute and the experiences highlighted in this report confirm that the government-nonprofit contracting problems first documented in the Urban Institute's 2010 landmark study were not an anomaly of the Great Recession. The serious problems persist nationwide. Nonprofits performing work on behalf of governments still confront policies, laws, and attitudes that deny reimbursement for the full costs of providing those services. Nonprofits continue to encounter wasteful application processes and costly reporting regimes that defy logic, consistency, or fairness. Once contracts are signed and work is commenced, governments often unilaterally change contract terms and conditions mid-stream, regardless of written commitments or the added costs those changes impose on nonprofits. And governments often pay nonprofits late – sometimes more than a year after the nonprofit incurred the cost on behalf of government. All five of these problems add billions of dollars in unnecessary costs to nonprofits and taxpayers alike.

Toward Common Sense Contracting: What Taxpayers Deserve explores the five categories of problems in detail, identifying various causes and consequences using the voices of nonprofits in the field. It goes farther than most studies by laying out numerous proven and often readily available solutions to these problems for the benefit of taxpayers, individuals needing services, governments, nonprofits, and foundations and private funders who are called on to fill the gaps and subsidize the broken government-nonprofit contracting and grants system.

Common Problems

Common Problems Before Contracts/Grants Entered

Even before governments enter into contracts/grants with nonprofits, two sets of problems commonly arise: (1) governments do not pay nonprofits the full costs of providing the services, and (2) governments routinely utilize wasteful contracting application processes.

More than half (54 percent) of all nonprofits surveyed by the Urban Institute reported problems with governments **not paying nonprofits the full costs of the services** the governments contracted to be performed. Often, this is due to artificial limits being set in advance, without regard to the true costs required. One of the most problematic ways this occurs is through the imposition of **arbitrary caps on reimbursement of indirect costs** (sometimes called overhead costs or administrative costs). Among nonprofits reporting that governments cap indirect cost reimbursement, the Urban Institute's latest survey reveals that three out of four nonprofits (76 percent) were unable to recover an indirect cost rate of more than 10 percent; a quarter (24 percent) are paid zero.

Studies reveal that the usual range of overhead rates for for-profit companies and nonprofit organizations alike is approximately 25 percent to 35 percent. Yet, governments have historically treated nonprofit organizations differently, imposing arbitrary restrictions on reimbursement rates that undercut the ability of their partners to succeed on behalf of taxpayers. Unrealistic limits on reimbursement of a nonprofit's legitimate costs undermine its efficiency, effectiveness, and ability to perform vital services on behalf of the governments.

Regarding **complexification of contracting application processes**, nonprofits on the front lines see daily the needless waste of taxpayer and donor dollars when government red-tape and costly protocols prevent them from delivering services efficiently and effectively. The problems experienced by nonprofits range from unduly complex applications and dysfunctional electronic submission processes to needless duplication and redundancy, and excessive formatting requirements.

Common Problems *During* Government Contracts/Grants

Once nonprofits commence work pursuant to government contracts/grants, problems commonly arise in three general categories: (1) governments changing the terms mid-stream, (2) governments routinely failing to pay on a timely basis, and (3) governments imposing complex and time-consuming reporting requirements.

Mid-stream changes to written agreements that governments previously signed and agreed to honor is most vexing, in part because it often increases the costs for nonprofits that are then not paid. These mid-stream changes, reported by almost half (44%) of nonprofits surveyed, take many forms, including cuts to agreed-upon payments, redefined eligibility for payments, nonprofits instructed to perform additional or increased levels of service, and new reporting and compliance requirements with no additional reimbursement for these added costs.

Late payments by governments is a problem that is both frequent (45 percent of nonprofits responding) and debilitating, given the significant dollar amounts reported by nonprofits that said they were paid late: on average state governments owed each nonprofit the past due amount of \$200,458, the federal government owed \$108,500, and local governments owed \$84,899. The substantial sizes of those late payments present serious challenges for nonprofits struggling to deliver reliable services. A subset of the problem is “**late contracting**,” when a government does not complete all of its own contracting procedures prior to demanding that the nonprofit begin performing services.

The **complexification of reporting requirements** – a problem reported by almost three-quarters (72 percent) of those surveyed – takes several forms, including duplicative audits, overlapping and inconsistent compliance procedures, retroactive imposition of reporting requirements, incompatible and inconsistent data collection, and a lack of standardization that inject vagaries into an already complex process. Rarely is it clear to nonprofits if and how the government even uses the information that often is expensive to collect and report.

Common Sense Solutions

Governments and nonprofits are natural partners, serving the same constituents in the same communities. It is in everyone’s best interest to work collaboratively to identify and implement meaningful solutions to common problems. This section of the report shares a sampling of common sense contracting and grantmaking solutions that meet the test of helping taxpayers, those needing services, and governments just as much as they help nonprofits.

Collaborative Problem Solving

1. **Government-Nonprofit Task Forces:** Policymakers seeking to reduce government costs, improve services, and protect taxpayers should create joint government-nonprofit task forces to identify and analyze challenges in contracting practices and procedures, and then develop and implement targeted solutions.
2. **Nonprofit Liaisons:** Governors, Mayors, and other executive branch officials should appoint and empower high-level Nonprofit Liaisons to oversee and promote contract and grant efficiencies and nonprofit sustainability.

Accountability for Full and Prompt Payments

3. **Payment of Indirect Costs Incurred:** Using the new OMB Uniform Guidance as a start, governments at all levels must reimburse nonprofit organizations for the full indirect costs that the nonprofits legitimately incur in delivering contracted services for government.
4. **Joint Training Programs:** Governments and their nonprofit contractors and grantees should conduct joint training programs designed to promote common understandings, collective problem solving, and mutual respect.
5. **Clear and Consistent Definitions:** Governments should provide and apply clear and consistent definitions of administrative costs, indirect costs, and overhead.
6. **Repeal of Arbitrary Caps on Indirect Costs:** Legislatures should repeal existing statutory caps on legitimate indirect costs that serve to undermine nonprofit effectiveness.
7. **Public Accountability through Disclosure of Indirect Cost Reimbursements:** Governments at all levels should publicly disclose for each program how much they pay in indirect costs.

8. **Prompt Payment Laws:** Governors and legislatures should ensure that state and local governments pay their bills on time by enacting and enforcing prompt payment laws.
9. **Prompt Contracting Laws:** Governors and legislatures should enact and enforce laws that ensure state and local governments complete the contracting process prior to commencement of work by nonprofits.
10. **Public Disclosure of Government Accountability:** Governments at all levels should inform the public on the timeliness of payments by government agencies to contractors.

Elimination of Unilateral Mid-stream Contract Changes

11. **Independent Government Office to Protect Charities from Contracting Abuses:** States should create an independent office, or Attorneys General should take actions, to ensure accountability so state and local governments honor the terms of their written agreements and stop unilaterally changing them mid-stream.
12. **Standardized Language for Contracts and Grants:** State and local governments should standardize contract and grant language, as well as reporting requirements, across multiple agencies to secure the savings attainable through reduced negotiating costs and standardized attachments and forms.
13. **Ongoing Provider Input:** Governments should institutionalize methods to regularly obtain input from nonprofits on how to improve contracting and grant processes, program design, and implementation.

Simplifying Complex Application and Reporting Requirements

14. **Document Vaults:** States and local governments should reduce redundancy in the application process by creating an electronic repository or “document vault” to house all commonly required documents from nonprofits relevant to bids for government contracts and grants.
15. **Standardized Monitoring and Reporting:** Governments should reduce redundant monitoring by standardizing and integrating reporting procedures across multiple government agencies.
16. **Standardization and Consolidation of Audits:** Government agencies should standardize and consolidate audit requirements to avoid repeated and unnecessary audits, reduce interruptions in nonprofit program services, and reduce taxpayer burdens of paying for multiple audit teams to review the same books and records.

Conclusion

The problems in the current government-nonprofit contracting “systems” across the country are profound, thoroughly documented, and, most importantly, solvable. The solutions presented in this report are tested, free or relatively inexpensive, and readily available. All that is needed are a commitment to identifying the solutions most appropriate to the jurisdiction and the motivation to take action. By way of this paper, the network of the National Council of Nonprofits extends an open invitation to all interested people – officials within government, frontline nonprofit employees and volunteers, individuals relying on services, taxpayers, and politicians – to help identify the problems that need solving immediately, craft the appropriate solutions, and take action to get them implemented.

TOWARD COMMON SENSE CONTRACTING: WHAT TAXPAYERS DESERVE

Introduction

In the three and a half years since publication of the Urban Institute’s landmark survey results on the status of government-nonprofit contracting issues, much has improved in relationships between governments and nonprofits around the country, yet little has changed in the latest data documenting continued nationwide problems with government-nonprofit contracts and grants. Indeed, since the release of that 2010 report,¹ government officials and nonprofit leaders have started to see each other less as adversaries and more as fellow victims trapped in and hurt by broken contracting “systems.” The recognition that their fates are intertwined led to several government-nonprofit collaborations, shared problem-solving task forces, specific time- and money-saving reforms, and mutual respect.²

And yet, the newest data from the Urban Institute³ and the experiences highlighted in this report indicate that major systemic progress has yet to occur. Nonprofits willing to perform work on behalf of governments still confront policies, laws, and attitudes that deny reimbursement for the full costs of providing those services. Nonprofits continue to encounter applications and bidding procedures that defy logic, consistency, or fairness. Once contracts are signed and work is commenced, governments often unilaterally change contract terms and conditions mid-stream, regardless of written commitments or the added costs those changes impose on nonprofits. For a multitude of reasons, the lack of funds in government treasuries being only one, nonprofits continue to identify late payments from governments as a frequent and serious problem. And despite efforts in some quarters to streamline reporting and auditing demands on governments and nonprofit alike, the complexity of the reporting requirements surpasses “daunting” to the point of being “debilitating” for many.

This report seeks to answer several “whys.” Such as, why are the data as bad as they are? What are the entrenched, root causes and what do the problems mean in terms of getting the public’s work done, or not done, in communities? Those questions are addressed in the “**Common Problems**” section of this report.

We also address the bigger question of why governments continue to do what has proven to fail; aren’t there better ways? We answer those in the section entitled “**Common Sense Solutions**,” the title of which makes clear our view that there are indeed tested, replicable, better ways to fix the broken “systems.”

Here are a few more “whys” that deserve attention up front: Why aren’t taxpayers outraged by the longstanding waste, inefficiencies, and unfairness of the *status quo*? And why aren’t foundations and private donors insisting on changes, given that they are subsidizing governments every time they fill a funding gap created when governments demand more from nonprofits and pay less than the full costs? To answer those questions, we focus on existing barriers to reform.

¹ Elizabeth T. Boris, Erwin de Leon, Katie Roeger, Milena Nikolova, *Human Service Nonprofits and Government Collaboration: Findings from the 2010 National Survey of Nonprofit Government Contracting and Grants* (Urban Institute Center on Nonprofits and Philanthropy; 2010) (“Urban Institute 2010 Study”); see also Urban Institute, *National Study of Nonprofit-Government Contracts and Grants 2010: State Profiles* (2010).

² See National Council of Nonprofits, *Partnering for Impact: Government-Nonprofit Contracting Reform Task Forces Produce Results for Taxpayers* (April 2013) (“*Partnering for Impact* Report”).

³ Sarah J. Pettijohn and Elizabeth T. Boris, with Carol J. De Vita and Saunji D. Fyffe, *Nonprofit-Government Contracts and Grants: Findings from the 2013 National Survey* (Urban Institute Center on Nonprofits and Philanthropy; Dec. 2013) (“Urban Institute 2013 Findings”); Sarah J. Pettijohn, Elizabeth T. Boris, and Maura R. Farrell, *National Study of Nonprofit-Government Contracts and Grants 2013: State Profiles* (Urban Institute; May 15, 2014) (“Urban Institute State Profiles 2013”). The 2013 Findings and Profiles – which surveyed all types of nonprofits (excluding higher education, hospitals, and others noted by the Urban Institute) – go much further than the 2010 versions, which focused exclusively on human services nonprofits.

Barriers to Reform

Nobody wants an antiquated, wasteful, and costly government system that hurts those in need, taxpayers, nonprofit board and staff members, government officials and employees, and the general public. Yet as documented in 2010,⁴ affirmed by the most recent data from the Urban Institute, and confirmed by multiple government and scholarly reports, the fragmented, multi-layered, and unduly complex government-nonprofit contracting “system” is in dire need of repair.

But change is not easy, for multiple reasons.

First is public awareness, or lack of awareness, due in large part to the nature of the subject matter. Many people instinctually react to the topic of “government-nonprofit contracting reform” with a touch of fear that it will be a foreign language and dreadfully boring, leading them to shut down mentally and turn away. Perhaps that’s understandable given the terms alone – “government” mixed with “contracting,” which suggest the vagaries of accounting and legal issues. Yet, as research shows, the so-called system is so broken that it is a national crisis, and as recent experience shows, solutions can be easy and inexpensive.

Another reason is the common lack of understanding by the public and policymakers about how nonprofits operate and how they are financed. The presumption is that nonprofits are staffed mostly by volunteers, sit on large endowments, and/or can turn to private foundations to fund their operations. These are gross misconceptions that preclude the public from empathizing or even recognizing the pain that nonprofits experience under government contracting and grantmaking policies. Most Americans, including many of the more than 14 million people employed by nonprofits, the 20 million who serve on nonprofit boards, and the 63 million who volunteer for nonprofits,⁵ simply do not realize that foundations provide less than two percent of the nonprofit sector’s revenues while nonprofits earn almost 33 percent of the entire sector’s revenue by performing services paid by government contracts and grants.

Revenue Sources - Nonprofit Sector



Sources: The Nonprofit Sector in Brief, National Center for Charitable Statistics, 2013 (2011 data); Giving USA 2012 (2011 data)

This lack of understanding interferes with reforming the government-nonprofit contracting process. For instance, we’ve heard elected officials suggest that nonprofits can just reach into their own reserves, apparently believing that endowments like Harvard’s and Yale’s are the norm rather than the extreme exception. In truth, the majority of nonprofits have just three months or less of operating funds in the bank.⁶ Other politicians and senior staffers

⁴ See Urban Institute 2010 Study; see also National Council of Nonprofits, [Costs, Complexification, and Crisis: Government’s Human Services Contracting “System” Hurts Everyone](#) (2010) (“Complexification Report”).

⁵ See Katie L. Roeger, Amy S. Blackwood, and Sarah L. Pettijohn, *The Nonprofit Almanac 2012* (Urban Institute); BoardSource, [Board Advocacy Campaign](#); “Volunteering in the United States, 2013,” Bureau of Labor Statistics News Release (Feb. 25, 2014).

⁶ Nonprofit Finance Fund 2014 [State of the Nonprofit Sector](#) Survey Report (April 2014). The NFF also found that, for only the second time in the survey’s history, more than half of all nonprofits surveyed (56 percent) reported that they could not meet the public’s increased demand for their services last year. Moreover, 41 percent reported that they ran a deficit last year.

suggest that nonprofits can simply turn to foundations for a grant, not understanding that most foundations have their own funding priorities and do not exist to subsidize government shortfalls.

Government austerity programs put in place since the start of the Great Recession have reduced government resources, along with the ability of governments to provide direct services to citizens. This decline has significantly increased pressure on nonprofits to fill service gaps caused when governments shut down programs while human needs still exist. The unspoken expectation is that nonprofits will indefinitely fill the gaps caused by governments abandoning the work and pay for their new workload through private sources, thereby effectively subsidizing governments. But stepping in to provide replacement services has been most challenging during a time when demand has been going up and private giving to charities has fluctuated between declining to remaining relatively flat.

A third reason that people remain distant and disengaged is ... government-nonprofit contracting truly is complicated. It certainly is easy to turn away when contemplating the sheer magnitude of the interwoven, multi-jurisdictional, overlapping and yet often conflicting accounting, funding, and legal components of the contracting solicitation/application/award/negotiation/documentation/reporting/payment/oversight/auditing processes. Consider all the intergovernmental challenges when a “simple” federal grant with particular reporting requirements flows to a state government. The state government adds its own restrictions and requirements as it forwards the funding to a locality, which in turn imposes conflicting program delivery limitations for its departments, and then re-labels the grant as a contract to a nonprofit. That nonprofit then looks at layers of additional and sometimes inconsistent and even conflicting reporting, accounting, service delivery, and other requirements, forcing it to divert limited resources away from mission to try to find ways to comply with often hidden, shifting, and unreliable requirements, limitations, and restrictions regarding a written agreement that some treat as a “grant” while others treat as a “contract” – each with its own set of unique features.

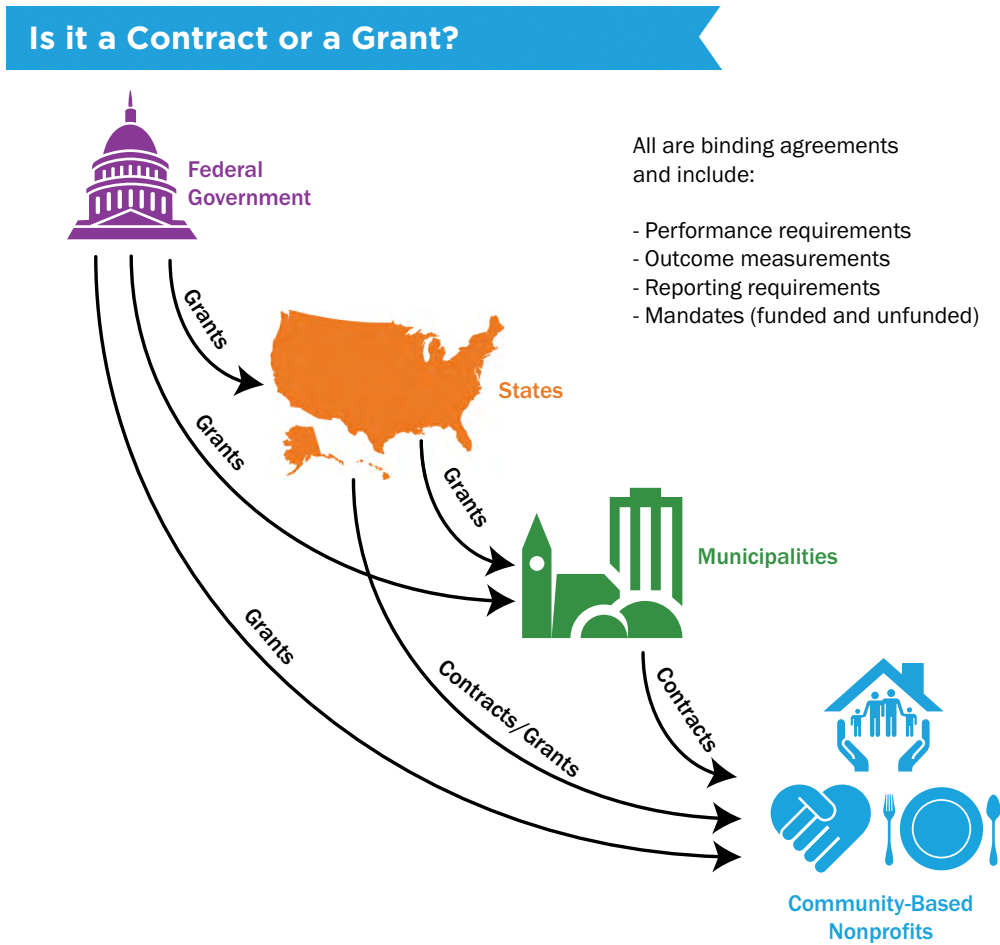
Just that one, apparently simple question – is it a “contract” or a “grant” – proves the point that it is much easier to ignore the challenges that governments and nonprofits face than to tackle them. The distinction between the terms “contract” and “grant” at various levels of government is technically important yet often ignored. In common parlance, many people mistakenly equate a “grant” as a “donation” or “gift” to go do whatever the nonprofit wants to do. For government funding, that is not true. When a government issues a grant to a nonprofit, both the government and the nonprofit sign a written agreement that is legally binding on both sides to perform. The federal government issues a “grant” to pay for another level of government or a nonprofit to provide goods and services for public purposes and enters a “contract” to purchase goods and services for the direct use of the federal government.⁷ States and local governments do not necessarily use these same definitions, however. Plus the distinctions between contracts and grants can prove confusing at times even for experts, as a recent judicial decision noted.⁸ The Urban Institute has documented how the confusion persists even among governments, with one county soliciting proposals for projects “marketed as grants programs to nonprofits even though they technically are not grants, which are prohibited by the county charter. Nonprofits apply for these grants that, when awarded, effectively become contracts with a particular set of requirements” (emphasis added).⁹

⁷ [The Federal Grant and Cooperative Agreement Act](#) prescribes when federal agencies are to use different forms of written agreements. When spending money for “property or services for the direct benefit or use of the United States government,” such as buying computers or services to make those computers work better, federal agencies are to use a “contract” (or “procurement contract”). 31 U.S.C. § 6303(1). When spending money to “carry out a public purpose of support or stimulation authorized by a law of the United States” and “substantial involvement is not expected between the federal [agency] and the” recipient of funds, such as when providing funds to protect children or seniors under a particular federal program, federal agencies are to use a “grant.” 31 U.S.C. § 6304.

⁸ See [CMS Contract Management Services](#), No. 2013-5093 (Fed. Cir. March 25, 2014) (a case in which a federal agency took different positions about what type of agreement it was or should be at different stages, another federal agency took a contrary position, one federal court determined the agreement needed to be one type, and the appellate court disagreed).

⁹ See Erwin de Leon, [Montgomery County Nonprofit Contracts and Grants](#) (Urban Institute Brief #2; Oct. 2013) at page 3 (“In Montgomery County ... funding opportunities initially appear to be grants. These funds, in practice, are treated as contracts and awardees are subject to the contracting process, which has a different and more stringent set of invoicing and reporting requirements than grants. For example, information requested from applicants [in the grant RFP], such as program outcomes and budget amounts, is less specific than what is required in the [contract] award agreement, which used contracting language and applies after funds are awarded. ... For nonprofits, the root of the confusion lies in the fact that they start applying for a grant that acts more like a contract.”).

The language issue is so basic, yet real. This report uses the terms “written agreements,” “contracts,” and “grants” in the general sense, unless a more particular use is noted.



But perhaps the biggest barrier to reform, in the end, is what we noted in an earlier report: “**Meaningful change takes time**.” Decades of evolving problems cannot be solved overnight.”¹⁰ Neither can problems be solved if they are unknown. We now turn to the documented problems.

¹⁰ *Partnering for Impact* Report at page 3 (emphasis in original).

Common Problems

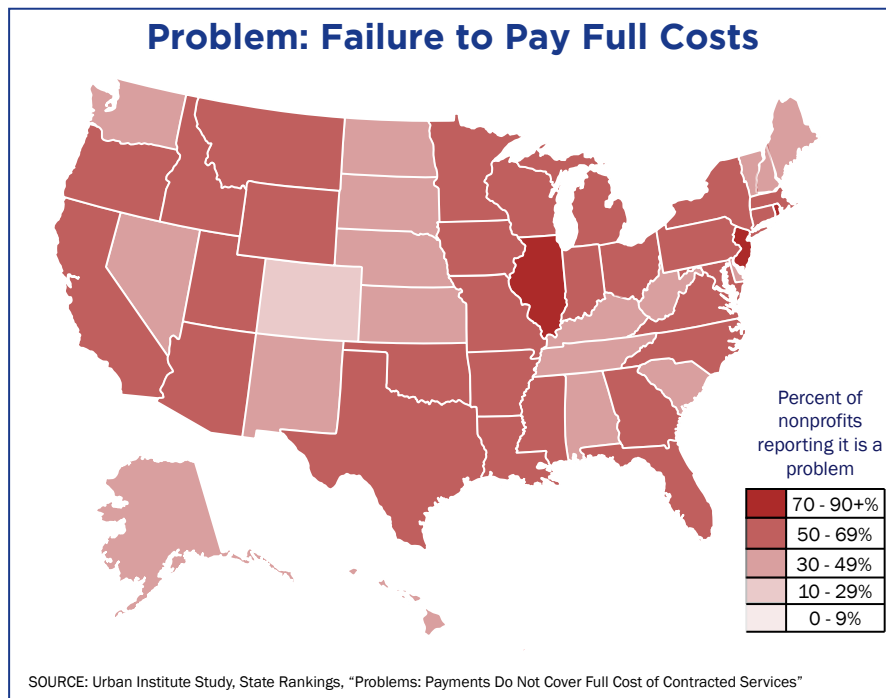
A. Common Problems Before Contracts/Grants Entered

National data reveal that even before governments enter into contracts/grants with nonprofits, two sets of problems commonly arise: (1) governments do not pay nonprofits the full costs of providing the services, often due to artificial limits set in advance without regard for the true costs, and (2) governments routinely utilize wasteful contracting application processes.

1. Not Paying Nonprofits the Full Costs of Services

Just as governments at all levels depend on and pay for-profit contractors to perform services like constructing schools and building highways, governments depend on entering agreements with charitable nonprofits to perform broad ranges of services that support and protect the most vulnerable people in communities, preserve our environment and culture, and much more. Yet governments contracting with nonprofits routinely fail to pay the full costs needed to perform those services. The newest data from the Urban Institute reveal that nationwide more than half (54 percent) of all nonprofits surveyed identified governments not paying the full costs of the contracted services as a problem.¹¹

In some states, however, nonprofits reported far worse. Three out of four nonprofits responding to the survey from New Jersey (75 percent) and Rhode Island (74 percent) reported problems with governments not covering the full costs of contracted services.¹² In a majority of states at least half of nonprofits reported problems with governments not paying full costs for the work they perform on behalf of governments and taxpayers. Even in states with the comparatively “least-worst” experiences, more than one out of four nonprofits reported problems with their government contracts not paying full costs: Alaska (31 percent) and Colorado (28 percent).



There is no reason to believe that government officials act with premeditated intent to injure or undermine their nonprofit contractor/grantees, but their actions have that effect when they routinely set rates in advance that do not pay the nonprofits the full costs they need to provide the services.

¹¹ Urban Institute State Profiles 2013 at page 119 (State Rankings: Problems with Payments from Government Not Covering Full Cost of Contracted Services).

¹² *Ibid.*

Experiences from the Field: *In Their Own Words*¹³

None of the contracts paid fully for the cost of the contracted services. In addition the State contract included many unfunded mandates. (CT)

Local government will not pay for ... the actual cost of providing services. (NC)

Unrealistic Reimbursement Rates

As the National Council of Nonprofits reported in 2010, many government programs reimburse nonprofits using outdated rates that have not been revised in years. More often, legislatures treat funding levels as a budgetary exercise rather than a contractual obligation and enact arbitrary schemes rather than provide for payment of actual costs.¹⁴ All of these practices shift the burden of paying the difference onto the backs of nonprofits that then are forced to scramble to try to raise the funds for the government services from elsewhere.

Under most government grants, the nonprofit must perform at least part of the work before it can be reimbursed. To ensure they pay only for legitimate expenses associated with the particular contract or grant, governments impose limits on what allowable expenses they will reimburse. That makes sense. What does not make sense is when governments impose arbitrary restrictions that guarantee that nonprofits will not recover the full legitimate costs they incurred to perform the services for which the governments contracted.

Experiences from the Field: *In Their Own Words*

School Lunch program dollars provides less than .82 per meal but costs us, with labor, new required food options, required posters and menu planning, more than \$1.85 per meal. That loss does not include the administrative costs and overhead. (AZ)

The rates we are paid did NOT keep up with the cost of workers comp, health insurance or fuel costs. (DE)

Our grant for social day care for seniors is paying two-thirds of the program costs and about half of full costs. (PA)

Cover costs including overhead? Not when contracts are level funded for years! (MA)

Arbitrary Caps on Indirect Costs

According to half the nonprofits surveyed across the country, governments do not adequately reimburse nonprofits for the indirect costs they incur to perform services for the government.¹⁵ A nonprofit's indirect costs (sometimes called overhead costs or administrative costs), with some exceptions, are equivalent to what for-profit businesses refer to as "overhead." Typically, overhead/indirect costs include items like rent, utilities, technology, administration, professional fees, and other expenses that are not tied to any one program but are vital to sustaining a healthy organization.

¹³ In late 2013, several state associations of nonprofits conducted a Pulse Poll to gather comments from nonprofit leaders in their states for examples to augment the statistical data collected by the Urban Institute survey. The representative quotes above and throughout this Special Report put the numerical data in context. To protect the identity of the Pulse Poll participants, only the state or region in which the nonprofit operates is provided. The notation (NS), for "no state," indicates that the survey participant did not identify the state. The comments in this section responded to the question whether government contracts and grants pay nonprofits the full costs of the contracted services (including associated administration and overhead).

¹⁴ See *Complexification* Report.

¹⁵ According to the Urban Institute research, exactly 50 percent of nonprofits surveyed nationwide reported a problem with governments limiting their program administrative or overhead costs, while 54 percent reported a problem as a result of governments limiting their general administrative or overhead costs. See Urban Institute State Profiles 2013: Government Contracts/Grants That Limit Program Administrative/Overhead Costs at page 124, and State Profiles 2013: Government Contracts/Grants That Limit General Administrative/Overhead Costs at page 125.

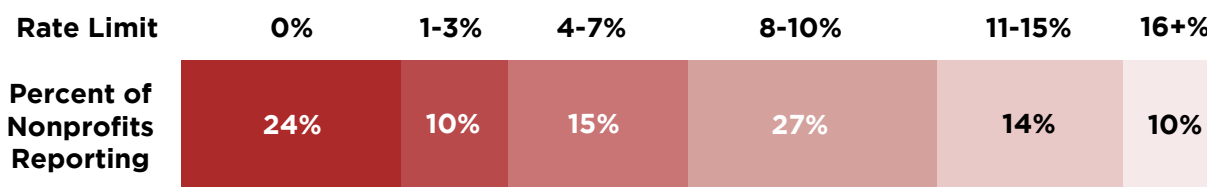
Studies reveal that in for-profit companies, the usual range of overhead rates is 25 percent to 34 percent average.¹⁶ That range is strikingly similar to the findings of multiple studies demonstrating that, among the most effective nonprofits, **an indirect cost range of between 20 percent and 40 percent is appropriate, with a range of 25 percent to 35 percent as being most realistic.**¹⁷ Yet, while such expenses by for-profit businesses are accepted as essential for creating more efficient and effective organizations that produce better outcomes, governments have historically treated nonprofit organizations differently, imposing arbitrary restrictions on reimbursement rates that undercut the ability of their partners to succeed on behalf of taxpayers.

Governments must realize that the low rates they set for nonprofits are inadequate and thus unfair because governments themselves usually operate with overhead rates of greater than 20 percent.¹⁸

The Urban Institute survey explored deeper for any distinctions between limitations on organizational administrative overhead (what it takes for the organization to operate) versus program administrative overhead (what it takes to deliver a particular program) as opposed to direct program costs.

According to the Urban Institute’s latest nationwide survey, of those nonprofits indicating government limitations in covering overhead expenses, one in four nonprofits (24 percent) reported that governments pay no general administrative/overhead costs of the organization, half (49 percent) reported that they were limited to 7 percent or less, and three out of four nonprofits (76 percent) were able to recover no more than 10 percent.¹⁹

Limits on General Administrative/Overhead Costs



SOURCE: Urban Institute 2013 Findings, Figure 8.

Hawaii has the dubious distinction of leading the nation in limiting **general** administrative/overhead costs (72 percent), according to nonprofits responding to the Urban Institute 2013 survey. For general administrative/overhead costs, the remaining states in the “worst ten” list are California (67 percent), Idaho (64 percent), Alaska (62 percent), Connecticut (61 percent), Illinois (61 percent), Maryland (61 percent), New Jersey (61 percent), Rhode Island (61 percent), and the District of Columbia (61 percent).²⁰ Overall, the Urban Institute found that the majority of nonprofits in 34 states said they performed work under government contracts and grants that limited reimbursement for organizational overhead.

According to the Urban Institute’s latest nationwide survey, of those nonprofits reporting limitations, about one in five (18 percent) reported that governments do not pay *any* program administrative/overhead costs of the organization, while more than two out of five (45 percent) reported that they were limited to 7 percent or less, and 73 percent were limited to recovering 10 percent or less.²¹

¹⁶ See Ann Goggins Gregory and Don Howard, “The Nonprofit Starvation Cycle,” *Stanford Social Innovation Review*, Fall 2009. Analysis based on 2007 data from Compustat and Standard & Poor’s Global Industry Classification Standard Structure for global companies traded on US exchanges with revenue greater than \$10 million.

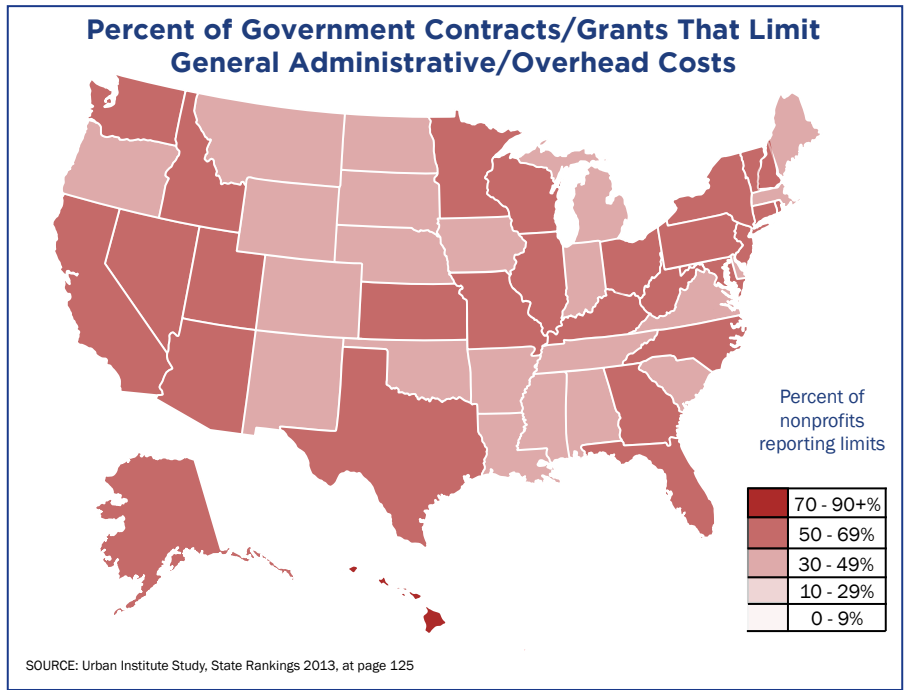
¹⁷ National Council of Nonprofits, *Investing for Impact: Indirect Costs are Essential for Success* (2013) (“*Investing for Impact Report*”) at page 8 and footnote 30.

¹⁸ See, e.g., Larry Satter, Chief Fiscal Systems and Consulting Unit, State of California, “Reform of Federal Policies Relating to Grants and Cooperative Agreements: Cost Principles and Administrative Requirements Comments” (May 2013) (“California has no departments with an indirect cost rate of 10 percent or lower, with 81 percent of our departments having rates higher than 20 percent and 76 percent of those having rates higher than 30 percent.”).

¹⁹ Urban Institute Findings 2013, Figure 8 at page 20.

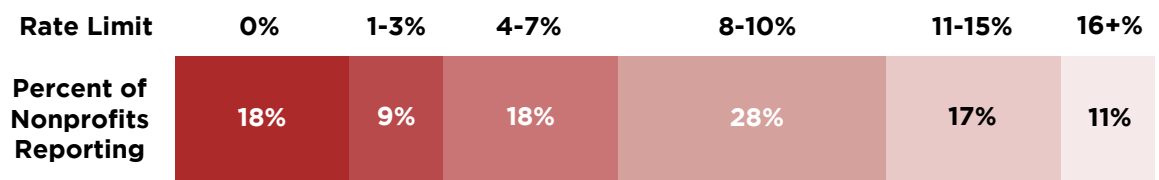
²⁰ Urban Institute State Profiles 2013 at page 125 (State Profiles: Government Contracts and Grants That Limit General Administrative/Overhead Costs).

²¹ Urban Institute Findings 2013, Figure 8 at page 20.



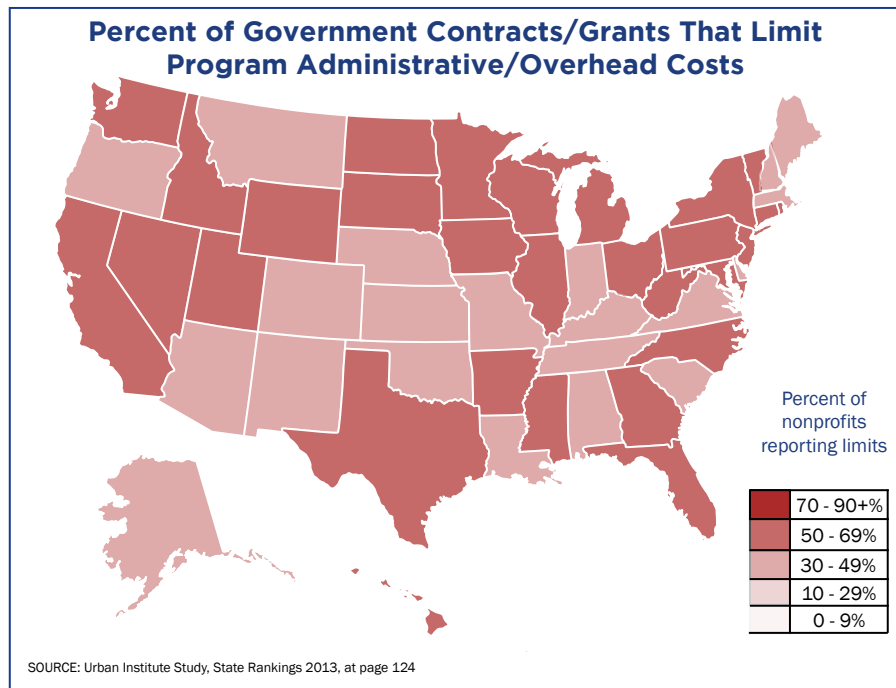
As for **program** administrative/overhead costs, Hawai`i, at 62 percent, once again led the nation with nonprofits there reporting that governments at all levels impose limits on program administrative/overhead cost reimbursement. Following the Aloha State on the “worst ten” list are Minnesota (60 percent), Arkansas (58 percent), California (58 percent), Utah (58 percent), Wisconsin (58 percent), Idaho (57 percent), Iowa (57 percent), Mississippi (57 percent), Connecticut (56 percent), and Ohio (54 percent).²² Overall, the Urban Institute found that the majority of nonprofits in 27 states reported that governments imposed limits on program administration expenses.

Limits on Program Administrative/Overhead Costs



SOURCE: Urban Institute 2013 Findings, Figure 8.

²² Urban Institute State Profiles 2013 at pages 124 (State Profiles: Government Contracts and Grants That Limit Program Administrative/Overhead Costs).



Experiences from the Field: *In Their Own Words*

Arbitrary Caps on Indirect Costs

New State grant for homeless services allows ZERO overhead and almost no program-specific costs besides staff time and direct client assistance. (AZ)

One grant only provides 2% overhead where my cost is over 20%. (MA)

Some contracts/grants include an adequate amount of indirect/admin/overhead and others provide less than adequate and others provide none at all. (DE)

One allows enough, but another (HUD) only allows 3% overhead, which doesn't come close to covering actual cost. (ME)

The contracts do not provide adequate administrative overhead payments. When they do provide for those costs it usually ranges from 3-7%. (NJ)

Generally speaking, local and state government grants will not pay for staff or overhead. They will pay for consultants, but this does not help a museum that already has the expertise in-house to plan or implement a project. (MD)

Indirect Costs Limits at All Levels of Government

County contract for aging services does not allow for any administrative or overhead expenses. Everything must be direct service related. (PA)

Our (typical) Fed grants allow for some inclusion of admin/overhead, but this amount is capped. Our large state grant did pay full cost. Local grants do not include any admin/overhead. (WV)

HUD only allows 5-6%, and HHS only 10% for administrative costs. This results in a loss to operate these programs. (CT)

The state agency we most commonly receive funding from is now allegedly awarding points to proposals that do not include overhead costs. (DE)

Disregarding Federally-Negotiated Indirect Cost Rates

Federal grants typically reimburse a nonprofit for at least a portion of its indirect costs. When individual nonprofits are the direct recipient of federal funds, they are able to negotiate an indirect rate with the federal government to be used when applying for federal grants. It is not uncommon, however, that a government agency imposes an arbitrarily determined cap on indirect cost reimbursement (whether dictated by a statute or determined through executive action) that is well below the nonprofit's negotiated rate. And as many nonprofits have found over many years, securing a negotiated indirect cost rate from the federal government is not a guarantee that state and local pass-through entities will pay the approved rate.

Experiences from the Field: In Their Own Words

Federal grants allow us to negotiate an indirect cost rate that can be applied to state grants. This helps with the allocation of administrative costs. However, we do have some state grants that cap administrative costs below our approved indirect rate. (PA)

No one will pay our approved federal indirect cost rate. Many times contracts put % caps on benefit costs, and that is difficult if salaries are low, benefit % are high. (NY)

Recent government contracts/grants, especially state and local, have started to cap administrative expenses at 10% even though our organization has a federally approved indirect rate. (AZ)

Federal pass-through at the state and local levels pay only a portion – at best – of operating costs. This includes CDBG, which has numerous layers and requirements, yet doesn't easily allow operating expenses without having a federal indirect cost rate, which simply isn't worth the effort for as little money as we get. (MD)

Unrealistic Expectations About Indirect Costs

Theories abound regarding why governments – and many foundations – do not pay nonprofits their legitimate indirect costs incurred, especially when all the research shows that the most effective and efficient organizations are those with higher rather than lower overhead rates. Some reimbursement restrictions are the result of statutory dictates by legislatures that insert arbitrary caps or other limits when creating a new program or designating a funding stream.²³ On other occasions, reimbursement restrictions are imposed by regulation, administrative fiat, or other unaccountable bureaucratic action. Complicating the matter even further, nonprofits find that different government grants – often within even the same governmental office – may differ in what costs may or may not be included in the calculation of indirect rates.

The one common denominator to so many of these different rates – whether established in statute, regulation, or rule, or even set per grant based on perceived “normal” practice – is that they all have been set arbitrarily in advance without regard to the actual costs.

The Results: Shifting of Burdens to Subsidize Governments

Multiple government and other empirical studies over many years demonstrate that when governments do not pay the full costs of the services they call on nonprofits to perform, it has a corrosive effect on the nonprofits and the people and communities they serve. Those studies will be discussed in the Solutions section of this report. For now, consider that among the real-world consequences of governments not paying the full costs of services is the problem that it diverts nonprofits away from their missions. Nonprofits exist to serve their communities, not to fundraise, so

²³ For example, at the federal level a Health and Human Services Grants Policy Directive ([HHS Transmittal 98.01](#)) provides this exception to the rule of honoring negotiated indirect cost rates: “Indirect costs under training grants to organizations other than State, local or Indian tribal governments will be budgeted and reimbursed at 8 percent of modified total direct costs rather than on the basis of a negotiated rate agreement, and are not subject to upward or downward adjustment.” For a state example, California requires that “all regional center contracts or agreements with service providers in which rates are determined through negotiations between the regional center and the service provider shall expressly require that not more than 15 percent of regional center funds be spent on administrative costs.” CA Welfare and Institutions Code § 4629.7.

government officials and employees should not blithely shrug and suggest that nonprofits just go fill the gaps through more fundraising – which carries additional costs. Yet, as voiced by frontline nonprofits in their own words, the failure of governments to pay for the services they want performed forces nonprofits to try to raise private funds to subsidize governments.

Experiences from the Field: *In Their Own Words*

Government expected nonprofits to raise funds to fill the gap between contract amount and cost of providing service for foster care, home visitation, mental health and family support services. (NE)

We had to fundraise to raise the balance of necessary funds for our program costs. (DE)

Overhead is tricky, mostly I have to have fundraisers for that. (NV)

Some of our government contracts/grants pay a significant portion of individual programs, but none would provide adequate administration and overhead to keep the program running without supplemental funding. (OR)

In order to fulfill the requirements of our 2 contracts, one for a domestic violence shelter and one for community based services, we have to supplement with fundraising and other foundation support about a dollar for every dollar that we receive. (MA)

Routine Failure of Governments to Pay Full Costs

Americans need a healthy nonprofit sector to provide a reliable social safety net and deliver a wide range of other services that are vital to the cultural, economic, educational, environmental, health, safety, and spiritual well-being of our citizenry and communities. Governments at all levels also need a healthy nonprofit sector. The foregoing discussion shows that common government practices undermine their nonprofit partners by not adequately reimbursing them for their costs – thus putting the people and communities served and governments at peril. Unrealistic limits on reimbursement of a nonprofit’s legitimate costs undermines its efficiency, effectiveness, and ability to perform vital services on behalf of the governments that impose arbitrary payment restrictions. Limiting a nonprofit’s effectiveness translates to an inability to achieve outcomes.

We close this discussion of the longstanding problem of governments failing to pay the full costs of services with the observation of one nonprofit leader, whose conclusions are so true that they must be highlighted here:

The irony for the field as a whole is that a technique meant to control costs actually undermines efficiency and program quality. The inability of nonprofits to invest in more efficient management systems, higher skilled managers, training, and program development over time means that as promising programs grow, they are hollowed out, resulting in burned out staff, under-maintained buildings, out of date services, and many other symptoms of inadequately funded ‘overhead.’²⁴

Good intentions that consistently lead to devastating results cry out for acknowledgement, and remedy – which we offer later in the Common Sense Solutions portion of this report.

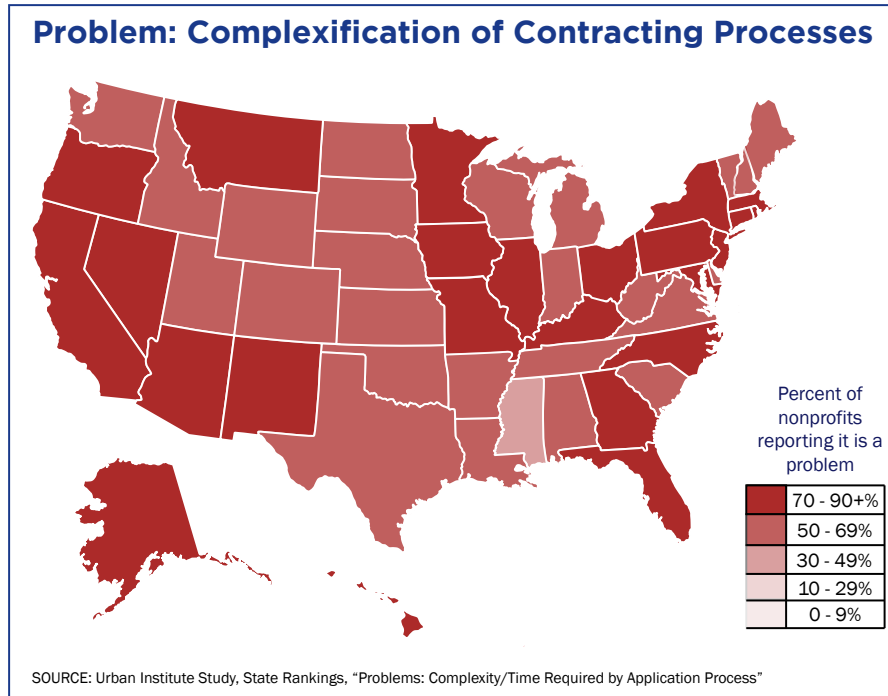
2. Complexification of Contracting Application Processes

According to the Urban Institute’s 2013 survey, an astounding 72 percent of nonprofits reported a problem with the complexity of, or time required by, government applications processes for contracts and grants.²⁵ Importantly, those are not complaints that applications were long or detailed – but that the processes were so burdensome in terms of complexity or time that they created a problem.

²⁴ Clara Miller, “[The Looking-Glass World of Nonprofit Money: Managing in For-Profits’ Shadow Universe](#)” *Nonprofit Quarterly* (Spring 2005).

²⁵ Urban Institute State Profiles 2013 at page 120 (State Rankings: Problems with Complexity of/Time Required by Government Application Processes). It is important to note that these rankings related to views about all levels of government in a jurisdiction – federal, state, and local – and not just the state government.

With nearly three-quarters of nonprofits surveyed throughout the country reporting this as a prevalent problem, it is hard to imagine practices being worse. But nonprofits in 22 states report conditions worse than the national average. Rhode Island ranks the worst, with 87 percent of nonprofits – almost 9 out of 10 – reporting contracting application processes to be a problem among all levels of government in the state. Rounding out the list of states where about four out of every five nonprofits reported this as a problem are Montana (83 percent), Maryland (83 percent), Arizona (82 percent), California (81 percent), Iowa (81 percent), New Jersey (81 percent), Alaska (80), Minnesota (80 percent), Oregon (79 percent), and New York (78 percent). Interestingly, even in the “least-worst” state, Mississippi, almost half (49 percent) reported contracting processes as problematic.



Everyone, including nonprofits, accepts that filling out applications forms can be tedious. But that’s not the problem. Being on the frontlines, nonprofits see daily the needless waste of taxpayer and donor dollars when government red-tape and costly protocols prevent the people’s business from being achieved efficiently and effectively. Such conditions cost governments and nonprofits alike, and divert taxpayer and donor resources away from actually providing services.

Before exploring the reasons for the common frustrations, recognize that it doesn’t have to be this way. A quarter of nonprofit leaders responding to the Urban Institute survey noted that they don’t experience these problems. And when asked in the Pulse Poll for comments whether “the process for applying for government contracts or grants complex/time consuming,” some nonprofit leaders shared:

We have had contracts/grants with the federal government for 25 years. We enjoy a great working relationship. (NE)

[S]ome of them are complicated and burdensome (e.g., CDBG), others are more streamlined and efficient. (MD)

What Does Complexification of Contracting Application Processes Look Like?

Nonprofits are reasonable. They understand the need for documentation and qualifications. Indeed, nonprofits want a robust application process that ensures that the organization best qualified to deliver the services in the community is fairly awarded the agreement. But when the overwhelming majority of nonprofits nationwide report that a problem exists with the complexity of, or time required by, government applications processes for contracts/grants, the problem merits serious attention. These kinds of practices are not limited to the federal government or a few state and local governments. They are consistently reported across the country.

Unduly Complex Applications

Thoroughness is, of course, necessary. But far too often there is a disconnect between what is essential for making an informed decision and what is demanded in an application. It appears that the people designing applications do not appreciate the massive cost in time that gets shifted away from meaningful mission work to wasteful processing work.

Experiences from the Field: In Their Own Words²⁶

RFP's are designed for multi-million dollar projects. We applied for a \$66,000 contract that took several days to complete. (DE)

It took me approximately 4 months to complete the grant, working every day and on weekends. I am an experienced grant writer. The Rubric did not match the grant info they asked you to supply in the narrative and other sections. (NC)

I find that some government grantors make changes in their grants and reporting forms every year. I have 2 grants that are incredibly time consuming because I feel like every year I'm applying for the first time even though I've had these grants for years. (CO)

The process can be simplified and still maintain its integrity. (CT)

Average time for a federal grant application is about 200 hours in the hands of our very experienced staff (resulting in a 60-80 page application). (AZ)

Federal grants (whether direct application or application through local administering-entity) are lengthy; fed-direct applications are very complex and lengthy - sometimes seem needlessly complex. (MI)

The additional pre-qualification requirement via the NYS Grants Gateway complicated and lengthened what had been a fairly timely process. This is very unfortunate. (NY)

The CDBG funds from the city requires quite a bit of info that does not apply to our grant request. (NV)

Federal application for less than \$13,000 required 35 page submission. (OR)

Demands from the government included in their requests for proposals have continued to increase. Smaller programs and rural areas of Maine, in particular, do not have the infrastructure to respond successfully for increasingly intricate requirements—resulting in resources moving away from these areas even though the quality of their actual work has been outstanding. (ME)

Dysfunctional Electronic Submission Processes

Online applications systems eliminate some technicalities such as how and where to staple or clip items, but frequently come with their own challenges, including when the electronic systems fail.

Experiences from the Field: In Their Own Words

Federal grant platform, grants.gov does not work even if all prior required forms are filed, and even after repeated calls to help lines. ... [O]nly after it was impossible to submit it were we informed (via email) that grants must be in 2 full weeks before the stated deadline because the federal servers

²⁶ The Pulse Poll asked nonprofit leaders “to provide examples” if in 2013 they found “the process for applying for government contracts or grants complex/time consuming.”

are too slow and have glitches. We spent 2 solid weeks on the application and that was the email response that what was sent to us, after the completed application was rejected by the server. (MT)

The federal grant process makes the Healthcare.gov website look like a toy. It took us 15 hours just to get registered, including going through one federal database after another. That was before one word of the grant was written. Then it got shot down, not on quality, but on the tiniest technicality, based on their ambiguous and misleading legalese, with absolutely no appeal process. They have become a massive obstacle to services rather than a supporter. (OR)

We applied to a state arts agency grant, which we found was very time consuming online and very difficult to save. A glitch on their website caused it to crash and we lost all the work we had done. (CO)

It's not as much complex as time-consuming and still paper-driven, even for those where we submit our application online. 1) It seems ridiculous that, if you are a current awardee and are reapplying, that you should have to go through the ENTIRE application process again. Most of the narrative and supporting documentation does NOT change. There should be a way to streamline the application process for those who are current recipients. 2) Some applications are still done on paper that must be single-sided and in a binder. 3) Even for those that are online, to get our contract finalized, WE (the recipient organization) have to print out a copy of the entire application, including attachments, single-sided and mail it to the contracting agency. I just did one of these and it was 50 pages of paper that cost us \$10 to mail! Why does it all need to be printed out when it's online? Better question: Why am I printing it out when the contracting organization has full access to the system and can print everything out themselves? (MO)

Duplication & Redundancy

In addition to the narrative, every application often requires numerous attachments. Even nonprofit organizations reapplying for a renewal to provide the same service they have provided for years must re-submit a new application at least every two to three years with all the same attachments. Government agencies end up with multiple copies of the same forms that then cost money and take up space in a file cabinet. This does not even take into account the fact that any nonprofit providing a service that must be licensed or certified by the state has already submitted most of these exact same documents annually as part of that approval process.

Experiences from the Field: In Their Own Words

Incredible amount of redundancy of paperwork and materials when you have multiple contracts, absurd micromanagement requirement (listing all staff by name rather than simply listing the position), etc. (NJ)

The information provided is enormous. Total package amounts to about 100 to 150 pages of material, mostly electronically transferred thru grants.gov. (AZ)

Take a look at the [city department] RFP and you will be shocked. Every year, we need to send in 6 copies of our Articles of Incorporation, 501(c)(3) and many other documents that they have had on file for our organization for years. (MD)

Lengthy process with data being resupplied they had on file (WV)

Fluctuating Application Requirements

State ethics and contracting laws appropriately prohibit individuals and organizations from improperly attempting to influence the drafting of Requests for Proposals (RFPs) and similar documents in ways that would provide them unfair advantages. These restrictions, however, have the unintended consequence of preventing government program and contracting officers, who often are generalists, from obtaining useful information from the nonprofit

service providers about what items need to be included or avoided to ensure the effective delivery of a particular service on behalf of government. This limits their understanding of the real-world impact of the RFP that contracting officers are drafting, sometimes resulting in changes in requirements after releasing a RFP. The government may come back with multiple changes in the scope of work they want to purchase in addition to more forms to complete or may change the proposal completely. Worse, they may cancel the project altogether after receiving completed applications from nonprofits.

Experiences from the Field: *In Their Own Words*

In at least two instances in the past year, two of our government [agencies], after the RFP process was complete, re-issued the RFP for no given reason, making all of the work null and void. (NJ)

Not only do the RFI's take up valuable time and writing grants or grant writing training cost significant dollars, it is terribly disrespectful and demoralizing when the [government] then withdraws awards of contracts or hadn't listened to almost 2 years of feedback and concerns! (NC)

Lengthy application, multiple bidder conference/question sessions which changed the nature of responses to certain questions. (MA)

One state grant application has been modified 3 times requiring changed data elements at each application... before they decided upon the final application. (CT)

The times for the grant period kept changing, which necessitated the creation of multiple budgets for the grant. (CO)

Excessive Formatting Requirements

Even the highest quality proposal in terms of program design and content can be disqualified if it does not precisely follow the application instructions, which may include using a specific size and color font or paper; margin size for pages; the number of pages, words, or even characters permitted for each item; whether the final document can be stapled, and if so where it must be stapled; and far more. At a certain point, these elements cross the line from seeking information to help identify the best qualified organization to deliver needed services to becoming traps for technical disqualifications. As such, they drain tremendous amounts of time away from mission delivery.

Experiences from the Field: *In Their Own Words*

[Government] went from number of characters per narrative to a count of the total grant application. Unfortunately, there is no pagination correlation between the online application and Word so many hours were spent copying and pasting trying to get the page length right. Very frustrating! (ID)

The major annual grant results in a large amount of data required that fills a 4 inch binder. We are also required to purchase specific types of production material (tabs, notebooks, etc.) to submit about 6 copies. This is a huge task that takes a full-time person about two to three months to complete. (MD)

B. Common Problems During Government Contracts/Grants

Once nonprofits commence work pursuant to government contracts/grants, problems commonly arise in three general categories: (1) governments regularly changing the terms mid-stream, (2) governments routinely failing to pay on a timely basis – *sometimes more than a year late*, and (3) governments frequently imposing complex and time consuming reporting requirements. Before turning to those most commonly-reported problems, it is useful to consider these observations from nonprofit leaders across America who contract with governments to deliver services in their local communities.

Experiences from the Field: *In Their Own Words*

We have very few administrative people to handle the tons of work of submission, reporting and monitoring of a grant. Implementation is the easy part! (NS)

We were given less money from [state contract] this year; however, the paperwork burden increases. I had to let go a contract employee who did most of the on-the-ground leg work. (NS)

Recurring grants have been cut each year for the past three years. The [government] expects the same project or product, but provides less money to complete it. (NS)

Through the development of joint government-nonprofit task forces to examine these challenges,²⁷ many states have found it beneficial to listen to nonprofit leaders who can see the often inane and wasteful problems and identify ways to save taxpayers money. Consider the following as urgent calls for basic cost/benefit analyses:

Experiences from the Field: *In Their Own Words*

[State] disputed \$0.04 cents which was due to rounding off of small numbers. Going forward, we modified our reimbursement requests to state that any discrepancy less than \$5 is negligible—not worth our time to fight over. The whole thing was ridiculous and a waste of both parties time and energy and money! (NS)

The state limited our contract to 6 months rather than a year...then extended it to a year, resulting in multiple redrafts of budgets and contracts at great administrative cost. And in the end all that work was for less money. (ME)

For the past several years including this one, we have not had full year contracts. We've had as many as four sequential contracts in a single year. This is a pointless recipe for extra work, both for the state and for us. (NS)

The amount of paperwork, revisions, and additional forms that kept popping up was outrageous. I agree that our tax dollars need oversight to be spent wisely, but any savings on potential waste were certainly spent by the person who was ensuring, tediously, that our application was "in order." (MT)

Demand for detailed information for small (\$10K) contract; Demand to explain line item budget variances as small as \$0.05. (MA)

1. Changing Agreement Terms Mid-Stream

Whether styled as a "contract" or a "grant," the document between a government and a nonprofit is a written agreement detailing the terms and conditions ultimately signed by both parties. Yet despite the legally-binding nature of signed agreements, nationwide more than two out of every five nonprofits (44 percent) reported that it was a problem for them when governments changed terms of the contracts/grants after the agreements were signed.²⁸ In 20 states, approximately half of nonprofits reported problems from governments changing the terms mid-stream.²⁹

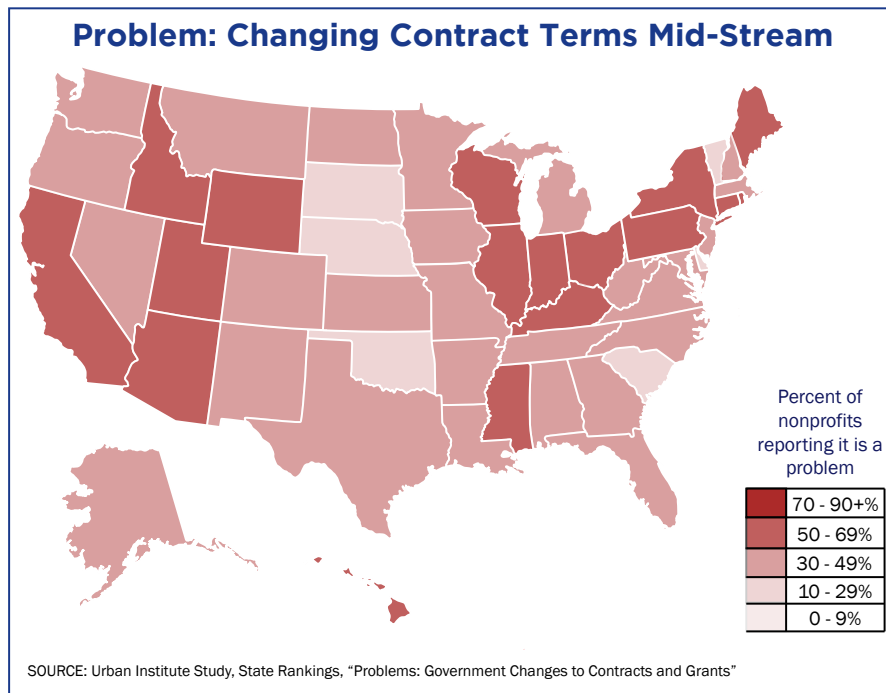
Mid-stream, after-the-fact changes to the legal agreement were reported as a problem by two out of every three nonprofits in these states: Rhode Island (67 percent), Wisconsin (66 percent), and Connecticut (63 percent). They are followed closely by the following states on the Worst Dozen list: Hawai`i (58 percent), Illinois (56 percent), Arizona (55 percent), Utah (55 percent), Indiana (54 percent), New York (54 percent), Kentucky (53 percent), Ohio (53 percent), and Wyoming (53 percent).³⁰

²⁷ See *Partnering for Impact* Report.

²⁸ Urban Institute State Profiles 2013 at page 122 (State Rankings: Problems with Changes to Government Contracts and Grants Mid-Stream).

²⁹ *Ibid.*

³⁰ *Ibid.*



At first blush, the notion of one party to a contract unilaterally changing the contract terms seems incomprehensible. The natural question arises: why don't nonprofits refuse and threaten to go to court? Consider these observations from the field:

Government organizations have you between a rock and a hard place. You are forced to do what they want, regardless of the RFP or contract. If you question or refuse to do the additional work, there is a high likelihood that you will not receive the funding again. You don't want to stand up to them because you are afraid to lose funding for your community. (Mid-Atlantic region) (emphasis added)

The State WIC office in particular has made retroactive changes to contracts that have caused local WIC offices [nonprofits] to have ineligible costs or delayed invoices for months causing offices across the state to close temporarily and then imply the local office behaved badly. When we asked who we should talk to, to correct the issues, we were told that if we go to legislators we risk a three year audit. (Western region) (emphasis added)

It merits reviewing what is happening, especially in light of the significant consequences. As the Urban Institute found, "Nonprofits that perceived changes to contracts and grants to be problematic were significantly more likely to ... reduce number of employees, cut programs or services, and close offices or program sites compared with nonprofits that did not report a problem with changes to government contracts and grants" mid-stream.³¹

What Does the Problem of "Mid-Stream Contract Changes" Look Like?

Often mid-stream changes to contract and grant requirements can have a devastating effect on nonprofits by imposing unplanned costs that are not reimbursed.

Experiences from the Field: *In Their Own Words*³²

The RFP did not specify many changes that occurred after the grant was awarded. The changes put an undue burden on our program financially. (NC)

³¹ Urban Institute 2013 Findings at page 31.

³² The Pulse Poll asked nonprofit leaders "to provide examples" if in 2013 "governments unilaterally made unwanted changes to your contracts/grants after you signed the agreement and started work."

They often change forms, reporting requirements, and allowable costs mid-contract. (WV)

Changing contract format after award announced and services started which delayed contracts and payments significantly. Then discovering that your contract is now partially reimbursable and requires three vouchers (which repeatedly get “lost” in the processing) to receive [payment]. A total change with no advance notice as to how money is received which was coupled with huge delays to getting the contracts and then getting partial payments. (NY)

In one case, they changed the start date so that expenses incurred during the beginning of the fiscal year were not reimbursable. (MA)

Cuts to Agreed-Upon Payments

When a government unilaterally decreases the amount it previously agreed to pay without proportionally reducing service delivery requirements, the nonprofit must scramble to cut something in the organization to cover the loss or risk operating at a deficit. This unanticipated burden falls on top of trying to fill funding gaps imposed at the outset when governments do not pay the full costs of services (see above).

Experiences from the Field: In Their Own Words

[Government] took \$100k without notice. The further down the food chain, the more difficult it is to work with governments. The feds tend to be more professional. (NE)

% funding decrease... without any decrease in the scope of services (NY)

Although our contract has been significantly cut, I have not received a contract amendment, revised scopes of service or any formal written letter. (CT)

The State changed our rate ... without our agreement. (MD)

The unwanted changes consisted of funding cuts (CO). Cut grant amount due to budget cuts. (NY) Arbitrary cuts. (NV) Rate change (CT)

Redefined Eligibility for Payments

Governments essentially impose cuts and increase nonprofit costs when they unilaterally retroactively redefine what they will pay for and under what conditions.

Experiences from the Field: In Their Own Words

Changed the ... eligible use of funds. (NC)

New restrictions on allowable expenses. (MD)

YES after starting work, the “rules of the game” changed on what was reimbursable. ... Perhaps unrelated are situations where you have performed the work in good faith, confirmed coverage, obtained proper authorization and then told the money will be recouped because the person was no longer eligible, retroactive 2 years ago despite checking coverage weekly! (MA)

Perform Additional or Increased Levels of Service

Requiring nonprofits to perform additional services without increasing their overall reimbursement for the services they provide is virtually the same as decreasing payments. The expectation, in either case, is to do more with less.

Experiences from the Field: *In Their Own Words*

Changed the category of service and standards we are to meet. Technically violated the contract/grant. (WV)

Our granting officer asked us to assist by hosting what would normally be another independent grantee. Of course we are happy to assist, but administering this extra grant under our name and umbrella did cost us (staff time, travel, etc. (MD)

One program that is funded with both state and federal dollars has conflicting benchmarks and requirements. (CT)

Increased Reporting and Compliance Requirements

When new requirements are added after an agreement has been established, the compliance costs associated with these changes have not been included in the budget, and therefore are unexpected. Changes do not just entail additional time to complete the new reporting requirements; it often includes costs to develop and implement new measurement tools, acquire unique software, and provide staff training. Retroactively imposing new requirements can result in a technical non-compliance by the nonprofit because the information needed may not even be available. This growing proliferation of reporting requirements add to a nonprofit's administrative costs, but do not appear to improve accountability or have an impact on the quality of the services provided. Moreover, these changes to perform additional, unanticipated compliance requirements often take staff time away from actually providing services, thus hurting the people the program is designed to help.

Experiences from the Field: *In Their Own Words*³³

[O]ur long-time [government grant source] came back and asked for documentation for which we were not contractually obligated. When we could not provide it, because we were not asked to keep it, they reclaimed some of the funding. (KY)

Contracts lack complete clarity and are often changed retroactively months after initial work has been completed. (OR)

Required to gather information that was not stipulated in the grant. (AZ)

Major changes in reporting requirements. (WV) More stringent reporting requirements. (PA) Especially on what they want reported on and forms. (MD)

2. Late Payments

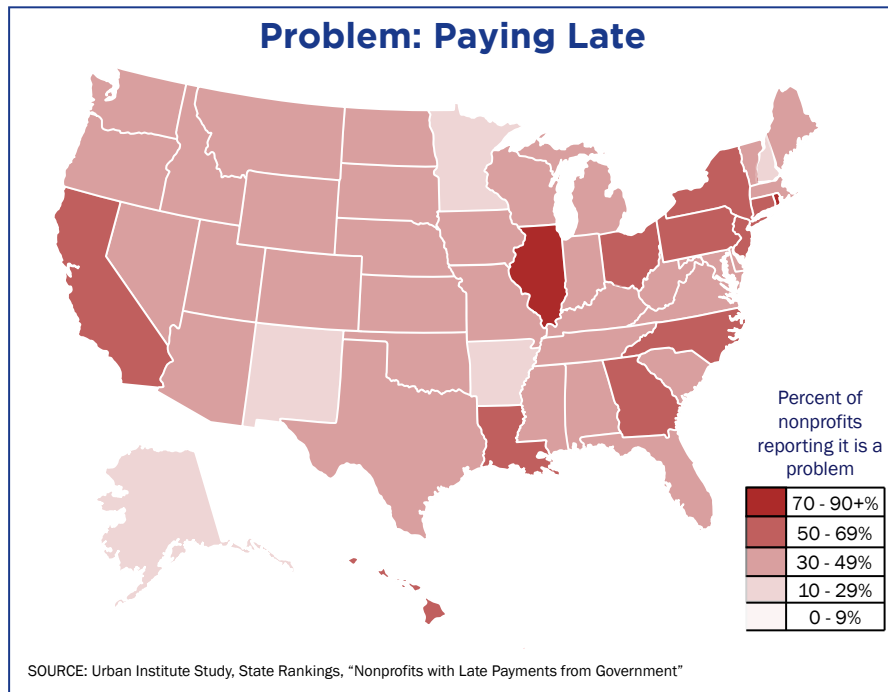
Nationwide, almost half of nonprofits (45%) surveyed by the Urban Institute reported governments paying them late under the terms of the legally-binding contracts/grants is a problem.³⁴ Not just that they were paid late – beyond the contract specification – but because they were *paid so late that it created problems*.

The situation is worse in many states. In Rhode Island, four out of five nonprofits (81 percent) reported they were paid so late beyond contract specifications that it created problems. In Illinois, it was three out of every four

³³ The Pulse Poll asked nonprofit leaders “to provide examples” if in 2013 their organization received “payments for government contracts/grants that were late (beyond the time agreed to under the contract/grant)”

³⁴ Urban Institute State Profiles 2013 at page 123 (State Rankings: Problems with Late Payments (Beyond Contract Specifications)). The Urban Institute's detailed research findings from early 2013 are consistent with the indicative size of the problem identified in early 2014 by the Nonprofit Finance Fund, which found that about half (51%) of the responding nonprofits reported that governments at all levels pay late on their written agreements with nonprofits. Nonprofit Finance Fund, [2014 State of the Sector](#) (April 2014).

nonprofits (75 percent)³⁵, and it was two out of every three nonprofits in Hawai`i (67 percent), New York (62 percent), and Pennsylvania (62 percent). Even in the least-worst states, governments still paid nonprofits so late that it created problems for about one out of every four nonprofits contracting with governments in Alaska (23 percent), Minnesota (22 percent), Arkansas (26 percent), and New Mexico (27 percent). The data reveal a widespread expectation among government officials that nonprofits will tolerate late payments.



The dollar amounts of the late payments are significant: on average state governments owed each nonprofit the past due amount of \$200,458, the federal government owed \$108,500, and local governments owed \$84,899.³⁶



The substantial sizes of those late payments present serious challenges for nonprofits struggling to deliver reliable services.

The length of delays in government payments adds significantly to those struggles. Around half of nonprofits surveyed reporting that late payments were a problem indicated payment delays of more than 60 days at the federal (48 percent), state (50 percent), and local (43 percent) levels. Even worse, about a quarter of those nonprofits reported delays of 91 days or longer at the federal (28 percent), state (26 percent), and local (21 percent) levels.³⁷

³⁵ The situation of Illinois' unpaid bills for all contractors and grantees has become so flagrant that several newspapers have launched an ongoing series entitled, "Deadbeat Illinois." Even the State Comptroller admitted that it "is unconscionable" for state government "to force businesses, hospitals, schools and service agencies to wait months on end for promised payment from the state." News release of Illinois Comptroller Judy Baar Topinka, "State Ends Fiscal Year \$6.1 Billion in the Red" (July 1, 2013).

³⁶ Urban Institute Findings 2013, Table 10 at page 33.

³⁷ Urban Institute Findings 2013, Table 9 at page 32.

Late payments by governments impose unreasonable and unnecessary costs on nonprofit contractors/grantees. Because that is fundamentally unfair, nonprofits in New York convinced the Legislature to require the state to pay interest for failing to live up to its own contractual obligations for timely payments. The Governor, however, vetoed the bill.³⁸ Even when states authorize payment of interest, they often impose exemptions and barriers.³⁹

Communities suffer severe consequences when governments do not pay their bills when due. Among nonprofits reporting late payments as problematic, 31 percent indicated that they had to reduce the number of paid employees, 25 percent had to increase their lines of credit, and 15 percent were forced to reduce the number of their programs or services.⁴⁰ The Urban Institute found that nonprofits reporting problematic late payments took those survival actions at a significantly higher rate than nonprofits without payment problems from government.⁴¹

But even those numbers regarding the consequences fail to tell the full story of the pain caused when governments do not honor their own signed written agreements.

Experiences from the Field: *In Their Own Words*

Reimbursement takes months and is sometimes quarterly. This is a real strain on cash flow and essentially forces the nonprofit to finance the government services. (MD)

Late payments deeply impact an organization's ability to keep continuity in services, and the burden falls on the grantee to sustain until payments are made. It is not unusual for us to wait 3 or 4 months for reimbursements on one grant source, and once we waited over 7 months, relying on a bridge loan that bore interest. (NS)

We are being forced to live off a line of credit, which incurs interest charges not included in our budget. ... Cash flow is a nightmare. It tarnishes our reputation, even though it is not our fault. No matter how compliant we are, the state keeps changing deadlines, requirements, and stretching out the payments – the contracts now say they can wait 365 days from the date of the contract to pay us! (NS)

It is incredibly difficult to manage an agency or program when you cannot depend on timely payment of vouchers from state or federal funders. It is hard to keep programs running smoothly and provide the required services when you can't get an executed contract, approved budget or budget modification, or voucher payments. (NS)

Our Dept. of Justice payments were held up for 6 weeks while a re-allocation process was occurring. Some organizations did not have enough cash and had to lay off some staff. (OR)

In 2012/2013, our contract year ... ran from July 2012 through June 2013. We received our first payment in March 2013 and did not receive the remainder of the grant until August 2013, after the contract year had ended. We had been assured that the funds would arrive in September 2012, within the contract year. This non-receipt of funds

³⁸ See Jessica Alaimo, "[Cuomo Nixes Accountability for State Payments to Nonprofits](#)," *Capital New York* (Oct. 22, 2013) ("Cuomo agreed that late payments from agencies to nonprofits are a problem, but in his veto statement the governor said he has taken other measures to prevent it. He vetoed a similar bill last year"). Technically New York law currently requires the state to pay interest to nonprofits when payments are made late, but no time frame exists for when these must be paid, so nonprofits rarely actually receive this compensation.

³⁹ See, e.g., California [Government Code 927.6](#) (the state escapes liability for paying interest penalty if its contract or grant with a nonprofit is more than \$500,000); see also Illinois State Prompt Payment Act, [30 ILCS 540](#) (state must pay "interest penalty of 1.0% of any amount approved and unpaid," but only after a 60 day grace period beyond the contract terms – meaning that a contract with a 60 day grace period written into it now has a 120 days of "grace" for the state, thus authorizing four months of lack of payment for the nonprofit that has already incurred the cost).

⁴⁰ Urban Institute Findings 2013, Figure 16 at page 34.

⁴¹ Urban Institute Findings 2013 at page 33.

created a situation whereby we were contracted to provide services but had to do that without the funds to do so. As a result, we had to furlough staff in order to mitigate cash flow. (NY)

Our cash flow is always impacted by the delays in receiving reimbursements. Consequently, while our bank will cover the shortfall, they also charge a “fee” each time they cover something. To date in 2013 we have incurred upwards of \$18,000 in “fees”. (NS)

The consequences are far greater than just those survival actions. This too-common practice diverts nonprofit resources away from mission, forcing nonprofit leaders (staff and board) to urgently stop their work to search for alternatives to meet normal cash-flow needs to pay their employees, employment taxes, rent and utilities, and other operating costs. Alternative measures include raising funds from other sources such as private donations or bridge loans, or by taking extraordinary actions like curtailing operations and laying off employees. These repeated problems cause burn-out of staff and board members, undermine planning, and ultimately increase the cost of providing services. In all of these instances, nonprofits and their private donors are essentially forced to subsidize government operations, at the expense of the people they serve and the nonprofits’ own sustainability.

This sobering example, unearthed by the public service series, “Deadbeat Illinois,” exposes the type of painful real-world problems that governments create when they fail to honor their written agreements to pay their nonprofit partners on time. The reporter tells the story of the leader of a nonprofit that contracts with the state to provide care for adults struggling with debilitating mental illnesses:

The state’s \$5 billion backlog of unpaid bills didn’t quietly creep up; it announced itself like the first violent flashes of lightning in a coming storm.

Stephen Langley, executive director of Stepping Stones of Rockford, felt it in 2007, the first time his nonprofit had to borrow money to make payroll while it waited for state payments to arrive. Over the past six years this has become more of the norm, Langley said.

Now, the organization ... survives on a month-to-month basis, struggling to keep enough cash on hand as it waits on the inconsistent ebb and flow of payments from the state....

“You have to make payroll,” Langley said. “And you have to maintain your insurances and make payments to the bank when the bank is the one that’s supporting your cash flow.” Other bills, still important, are deemed less critical. So at times the utilities are shut off. Some Stepping Stones group homes temporarily have lost water, electricity or heat. It must either borrow or wait for the money to turn the utilities back on....

Stepping Stones serves the chronically ill — people with major behavioral problems and medical needs. They’re the people who have not done well in programs with less structure and less staff involvement....

Stepping Stone’s cash-flow problem is shared by most Illinois nonprofits and organizations that rely on Medicaid funding. The money is filtered through the state, which purposely delays payments to keep enough cash itself to pay its own bills. Meanwhile, ambulances and emergency responders, health care providers, addiction facilities, group homes for severely disabled or ill adults and children and other programs that target some of the most vulnerable and at need in society, wait. ...

What’s hard, he said, is that instead of looking for ways to add services, innovate or build a better product, all energy over the next several years will be spent simply on scraping by.⁴²

⁴² Greg Stanley, “[Deadbeat Illinois: Late payments turn agency into deadbeat itself](#),” *Rockford Register Star* (July 28, 2013).

Unfortunately, that is not just one organization's story, nor is that story restricted to just Illinois. It's a familiar story for too many nonprofits across America.

What Does the Late Payment Problem Look Like?

To comprehend the Urban Institute's numerical data about the size and scope of the late payment problem, consider these experiences of nonprofit leaders who provided examples in response to the Pulse Poll in late 2013 when asked "to provide examples if their organization received payments for government contracts/grants that were late (beyond the time agreed to under the contract/grant)":

Experiences from the Field: *In Their Own Words*

Late up to 12 months. (NJ)

Funding came almost a year late. (NY)

Some of our State contracts went longer than 6 months without payment when [the State] already had the money from the federal government. (NJ)

Our new contract year started July 1, 2013, but we did NOT receive our new rates until November 19, 2013. This resulted in us having to carry a \$270,000 receivable for 4 months. (DE)

In one major grant, Programs did not receive payment for August, September and October services until after November 16th requiring them to use credit lines, incurring interest charges, and other resources to carry these grant program activities. (ME)

We receive money from the cities ... always a few months late. The State funds we receive always stop during the summer and it often takes until October to get these funds moving. (NJ)

City ...notorious for taking months to produce a check after a draw request is submitted. (KY)

The state frequently does not pay vouchers in a timely fashion. For example, for a contract that ended in September we are still waiting for 4 months' worth of voucher payments even though we have completed all requested paperwork and work-plan requirements. (NY)

Funding for many state grants runs at 3 months behind the delivery of service date.... this delay puts a fiscal burden on the grantee/non-profit. (WV)

[State] is a very slow payer. They are generally 3-4 months behind in paying on contracts. Of course, we have fronted all the money and are waiting for reimbursement. (PA)

These comments are not to say that all governments routinely pay late. Several nonprofits noted that governments usually pay on a timely basis. They also recognize that occasionally an issue will arise and that different levels of government treat them differently.⁴³

Still, it is enormously frustrating when the governments' broken systems create needless costs and burdens on nonprofits.

⁴³ See, for example, these comments to the Pulse Poll that show governments can pay on time when they treat legal obligations and partnership principles as priorities: "Generally on time" (CT) "Usually it's pretty quick, but a couple times the lag was problematic." (DE) "For the most part the payments have been made in a timely manner once the request was made." (MD) "the lateness of the payment ... has not been an ongoing issue. More of a one-time occurrence." (AZ) "State contracts are usually late and the federal grants via their PMS is excellent." (CT) State "funding was late, local funding was timely" (NY).

Experiences from the Field: *In Their Own Words*

This organization will likely be forced out of business due to abrupt administrative cuts and the inability of [state] to make payments on contracts in a timely manner. (NY)

Late government payments have resulted in furloughs, program/service cutbacks, and financial hardship for our organization. (NS)

[State agency] takes months to reimburse for invoices. We have been told a small invoice of \$3000 - \$4000 goes through 18 people before it is paid. (NC)

[State agency] is supposed to take 4-6 weeks from invoice, but regularly took 8-10 weeks or longer. Most importantly, the invoice has to go through multiple hands (aka sit on many desks) to get processed. ... Last January 2013, I had to have my Board Treasurer call [state agency] because we had not yet received our 1st reimbursement payment for a grant that started July 1, 2012. After the 6 month delay, we had to apply to [a] Foundation for cash flow loan because we were worried about making payroll." (MD)

Each unit of government requests invoices and associated documentation in different formats. This consumes extraordinary due diligence and often delays payment while we are attempting to address each individual entity's demands requirements...no consistency. Further compounding occurs when the primary funder contracts thru another government agency and we are the recipient, i.e., federal to state to county. (OR)

There have been repeated times when the program person has "misfiled" our reimbursement (which is the only way we are paid). ... There have also been multiple occasions when their bookkeeper forgot to enter our reimbursement into the accounting system ("sitting on her desk" has been stated more than once). (CO)

State payments late. Fed payments funneling thru state even later. State claims Feds are being tougher on them. (KY)

Late Contracting

A particularly aggravating subset of late payments occurs when a government does not complete all of its own contracting procedures prior to the intended start date for nonprofit services, otherwise known as "late contracting." For instance, a New York's State Comptroller's audit found that 78 percent of state contracts with nonprofits were late in 2012. The state violated its own statutory limits for timely contracting more than 3,200 times, but paid only \$237,538 in interest, hardly an incentive for state government to improve.⁴⁴

Experiences from the Field: *In Their Own Words*

Payment for services was not made until there was an approved signed contract budget and methodology and the [government agency] did not have the process completed on their end until several months into the contract period. Our organization provided services for five months without payment and then received back payment. (MN)

[State agency] prepared and mandated a new reporting form six months into the grant period. They also for the first time this year stated that no funds could be expended before a signed contract, our contract was delayed by 31 days and we cannot recoup any funding for the services provided. They have never, in my 20 years done this. (MI)

⁴⁴ Office of the New York State Comptroller, [Prompt Contracting Annual Report for Calendar Year 2012](#) (May 31, 2013).

The contracts were issued 8 months late, and the funding arrived a year late, causing terrific fiscal hardship. (NY)

Local government did not even execute contract until March, for a grant period that began in June of the previous year and for which we had to deliver the same levels of service. (NJ)

The first problem is getting contracts signed. For a July 1st start date, the contract wasn't signed until late October for one grant. But nearly all of them are late because it totally depends on the funding office. As a result, initial payments are invariably late. (NC)

Local government is the worst in signing contracts and then delaying payments – especially pass through dollars from state or federal government. (CT)

The renewal process is slow on some of the grants and resulted in our agency floating the bill. The slow renewal process sometimes end three months into the contract start date. The technical delay causes nonprofits to foot the bill due to systemic problems within the government agencies. (TN)

OMG! They are all late. It's unbelievable how slow any state agency is to sign a boilerplate contract that finally triggers the reimbursement cycle. One state agency we have had contracts with for 14 years and didn't receive this year's agreement until the end of September for the fiscal year. In my opinion, the legal counsel and sometimes program staff are completely disconnected as to the impact the delays cause the nonprofit. (MD)

When governments do not initiate contracts as specified in the application, they cost nonprofits additional funds as well. For new contracts, the nonprofit has been working to hire new staff, purchase needed supplies, obtain additional space, and more in anticipation of an agreed upon start date. Nonprofits must absorb the cost of these delays when the government fails to execute the contract as specified. For renewing contracts, nonprofits attempt to avoid interrupting service delivery.

3. Complexification of Reporting Requirements

Nearly three out of every four nonprofits (72 percent) nationwide “reported a problem with the complexity of time required by government reporting processes for contracts/grants,” according to the Urban Institute study.⁴⁵ The problem was even greater in Maryland, for nearly 9 out of 10 nonprofits (88 percent). And about four out of five nonprofits said that reporting burdens created problems in Connecticut (82 percent), Illinois (82 percent), Oregon (81 percent), Wisconsin (81 percent), California (80 percent), New York (80 percent), Montana (79 percent), and Rhode Island (79 percent).

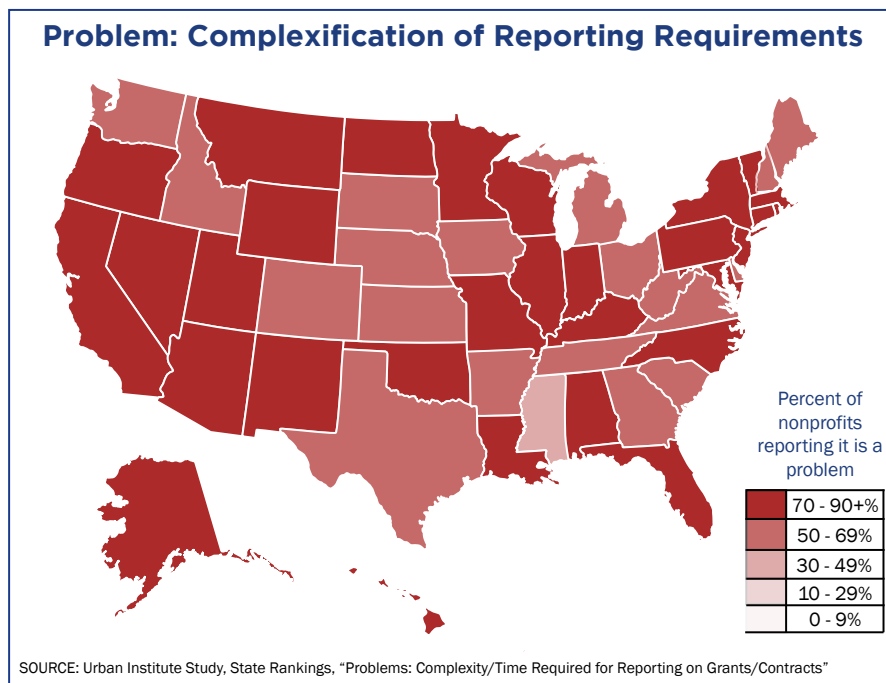
Reporting requirements add to administrative costs that are generally not reimbursed, resulting in a growing number of unfunded mandates.

No one suggests that accountability is not appropriate, but duplicative efforts that provide no additional accountability wastes already limited financial and human resources. There appears to be no recognition to the significant hidden costs that create real consequences. According to the Urban Institute’s research, nonprofits “indicating problems with time consuming reporting were also significantly more likely to ... reduce number of employees and the number of programs or services compared with their counterparts that did not report this problem.”⁴⁶ As one Pulse Poll respondent in Delaware observed, the growing “trend is for most contracts/grants to require more complex reporting.” And “it is getting worse - soon the reporting will take more time than performing the actual program,” predicted a nonprofit leader in Pennsylvania.

⁴⁵ Urban Institute State Profiles 2014 at page 121 (State Rankings: Problems with Complexity of/Time Required by Government Reporting Processes). Note that time-consuming and complex **reporting** requirements tied with time-consuming and complex **application** requirements as the issue most cited as problematic for nonprofits with contracts and grants.

⁴⁶ Urban Institute Findings 2013 at page 28.

Problem: Complexification of Reporting Requirements



What Does the Problem of “Complexification of Reporting” Look Like?

The problems described by nonprofits take several forms including the lack of consistency in forms and formats, changing requirements, and considerable amounts of redundancy. Additionally, it is unclear if and how the information that is demanded is even reviewed and used.

Duplicative Audits

It is well recognized that the government is responsible for ensuring that taxpayer dollars are spent as intended. Yet, nonprofits must endure multiple audits of the same financial records and the same programmatic records by multiple government agencies. This costs governments/taxpayers in duplicative expenses and diverts significant resources away from mission delivery. For example, if a nonprofit has five different government contracts and grants, in addition to their independent audits, they will be audited by five different government audit teams, at least five different times, looking at virtually the same information. If these five audits were combined into one audit conducted by one government audit team that shared with appropriate agencies, then there would be a considerable savings with no loss of accountability.⁴⁷

Experiences from the Field: In Their Own Words⁴⁸

In spite of the fact that there is a single audit act, each government entity still comes to audit both programs and finances, putting an undue burden on program and administrative staff. (AZ)

Not only did we have to provide our annual report to the funding agency, but we had to complete the state auditor’s report, participate in an audit by an independent auditor, and have an internal audit by staff at the granting agency. (NC)

The administration required to manage the extent of financial reporting strains our limited resources and requires up-to-date technologies and software, further reducing resources.

⁴⁷ Over the years, we have heard government officials lament this wasteful duplication of taxpayer resources paying for five different audits teams doing the same work. Some note that they sometimes run into federal or state legislative directives saying that information cannot be shared for privacy or other reasons.

⁴⁸ The Pulse Poll asked nonprofit leaders to provide comments if in 2013 they found “the process for reporting financial and program outcomes complex/time consuming.”

In addition to the annual independent audit, we undergo continuous audits with governmental entities on a monthly basis. In the past 30 days we have been audited by 5 agencies and have 2 reviews on the calendar before the end of December. (NS)

Costs of Compliance and Inconsistency

Often, each government agency, and even individual departments within a single agency, develops its own processes, procedures, and reporting formats it requires for financial and programmatic reporting. This results in the need for a nonprofit to spend time reorganizing the same data in multiple ways to comply with the variety of reporting requirements and formats.

Experiences from the Field: In Their Own Words

The NCGrants.gov site uses different budget categories than the state granting organization This creates extra work (and costs) for us for our accountants to develop the financial reports for both processes, both of which are part of the State of NC. (NC)

We spent a good deal of time having to count up and report on all kinds of outputs, such as emails, phone calls and web posts. These really didn't relate to program outcomes, and seemed extraneous and not useful. (VT)

If you miss a comma or a period or are off by one cent, it needs to be redone. (CT)

One contract requires a copy of the cancelled check, the bank statement and the check registry from our payroll service - 3 verifications for every expense. (MD)

Reporting for federal grants is time consuming and different agencies use different formats and different timeframes. It would be nice to have some consistency on reporting periods and required information. (WV)

Because the webware used by the agency will neither export nor import data, our organization is required to complete data entry twice for each client visit. (PA)

Financial reporting has become excessively burdensome whereby complete copies of every activity (personnel time docs and receipts) are required with every invoice. (OR)

Change after change to reports. State people don't understand how to write report format that allows us to effectively demonstrate what we do. They are bean counting. (KY)

We have 85 pages of data and narratives, plus 10 financial reports, all due within 8 days after the end of the quarter. It is challenging to close our accounting records for the month, and tabulate all of the client data in that short a time. We are just not that sophisticated and don't have the person-power. So many of our senior staff wind up working over holidays and weekends to produce these reports. (CT)

Retroactive Requirements

Without standardized policies and practices, governments are more likely to impose new requirements on nonprofits without notice, which are often retroactive. As addressed previously regarding the problem of changing contract/grant terms in mid-stream, such changes can be very challenging to comply with when the nonprofit did not know in advance that it needed to collect a certain data element in an easily accessible format.

Experiences from the Field: *In Their Own Words*

State government has changed requested data/information without prior notice. It is difficult to obtain such requests post performance. (ND)

Reports required additional formatting and content not originally requested by the grant, leading to massive changes for our local contract. (KY)

Reporting is ridiculously long and tedious. They want more information almost weekly and none of this was agreed upon in the original contract. (CO)

During an audit, a state auditor told me he “had to have a finding.” He “dinged” me for a policy that was not followed in my grant - but wasn’t even in place during the grant period. Now, I have to submit budget reports and timesheets with my reports - takes me up to 4 days to prepare monthly report for each grant... (MD)

The state keeps changing the rules about how they want us to report information and what information they want us to quantify. (PA)

Each of our government grant reports (1 state, 1 local) take at least 40 hours to complete. Reporting requirements vary from year to year and the government entity does not provide the information they will be requiring for the report at the start of the grant agreement, so we cannot accurately track the information they require. (NJ)

Paperwork & Forms

The failure to collect data in common formats based on a consistent understanding of the data significantly reduces the government’s ability to utilize the data to inform their decision-making or program improvement efforts.

Experiences from the Field: *In Their Own Words*

Every year there is one more piece of paperwork that seems redundant. (NJ)

We were required to produce an inordinate amount of paperwork and documentation for a small amount of money. (PA)

The documentation and paperwork takes more time than the actual project often times with duplication of efforts. (ND)

It is very aggravating that we fill out a final report to the granting state agency and then have to do a separate report to the state auditor. Seems there could be communication between the 2 state agencies. (NS)

Vagaries

The lack of standardization is also evident when each agency individually interprets the rules used to establish expectations of its nonprofit partner. When government agencies are inconsistent in their interpretations, nonprofits have to respond differently to each, in ways that sometimes conflict.

Experiences from the Field: *In Their Own Words*

Expectations change and our questions not answered consistently by different members of the same state agency. (MA)

We are still getting clarification on areas of the reporting. Often when we ask the same question we get different answers from different people and even different answers from the same person at different times. It seems that the questions on the reports are either outdated or do not fit nonprofit partners very well. (ID)

Time Diverted from Mission

And finally, the question must be asked: for what purpose are many of these reporting requirements used? Are they truly to protect taxpayers, clients, and the public? Or are nonprofits now reporting for reporting's sake? When real people are adversely affected, as the following comments suggest, the question is far from rhetorical.

Experiences from the Field: *In Their Own Words*

Paperwork has become more of an emphasis than the people we serve. (NS)

I have 5 grants that come through the State and on some the data requirements are very intense. And, there is not enough money to pay for administrative staff (even if there were funds, we'd still be limited to how much of the time I could charge) so it pulls program people away from their work. (NS)

One state contract now requires monthly client survey reporting, which is not only time-consuming for staff to collect/track, but often interferes with client services (we feel like we're hounding clients to complete govt'-required surveys in order to maintain our funding). (MD)

The obsessive requirements for reporting keep growing exponentially without any obvious program benefit. The amount of staff time absorbed in reporting of detail is significant and is increasing. We are glad to be compliant with reasonable reporting requirements on outcomes and expenditures, but are faced with an increasing demand for detail and NO additional funding to respond--so the cost inevitably comes out of decreased services to our clients. (ME)

As demonstrated by statistical and testimonial proof, the problems are real, common, and significant. Fortunately, solutions exist. We now turn to them.

Common Sense Solutions

National data, quantitative and qualitative, reveal a national crisis with respect to the antiquated, broken, and costly processes through which governments contract/grant with nonprofits to provide services. If governments and nonprofits work together to improve the efficiency and effectiveness of the dysfunctional contract/grant process by even just 1-2 percent, we can save billions of dollars nationwide for services, for private donors, and for taxpayers. Without intentional and sustained reform efforts, however, the habitual problems will continue to increase costs as well as reduce the quality and quantity of services to individuals most in need. Doing nothing perpetuates this cycle of waste.

Since 2010, the National Council of Nonprofits and its network of state associations of nonprofits have focused on identifying solutions to these and other recurring, systemic problems. The specific goal has been to promote solutions that can be replicated in communities across the country. Where possible, we have worked with governments to begin the journey of implementing various solutions. Why? Because governments and nonprofits are natural partners, serving the same constituents in the same communities. It is in everyone's best interest to work collaboratively to identify and implement meaningful solutions to common problems. The good news is that our network – often working with our partners in government – has developed or discovered easy and inexpensive ways to implement solutions that benefit everyone.

This section of the report shares a sampling of common sense contracting and grantmaking solutions. Here we identify replicable solutions that can overcome specific problems that prevent governments and their nonprofit partners from being as successful and efficient as possible. To be included in this section, the solutions had to meet the test of helping taxpayers, those needing services, and governments just as much as they help nonprofits.

Charitable nonprofits exist to solve problems in their communities. It is only fitting that they approach the government-nonprofit contracting problems discussed in the foregoing analysis with recognition that together they and their contracting and grantmaking partners can overcome the many challenges. We therefore begin by relating the promise and benefits of “collaborative problem solving” that governments and nonprofits have jointly put to use in productive ways in recent years.

Collaborative Problem Solving

1. Government-Nonprofit Task Forces

Policymakers who want to reduce the cost of government, improve services provided to constituents, and return greater value to taxpayers should consider creating a joint government-nonprofit task force to develop and implement recommendations to reform contracting practices and procedures.

Joint government-nonprofit task forces are not solutions in and of themselves, but they have proven to be an effective method for identifying problems and developing the solutions to fix them. Since publication of the 2010 nationwide study highlighting the serious problems surrounding government-nonprofit contracting, at least nine state governments have created joint government-nonprofit contracting reform task forces. A 2013 report, *Partnering for Impact: Government-Nonprofit Contracting Reform Task Forces Produce Results for Taxpayers*,⁴⁹ reviews the creation, recommendations, and implementation activities of those task forces and identifies trends and insights that can be applied to jumpstart efforts elsewhere. As participants in those nine task forces, the network of the National Council of Nonprofits has developed considerable experience in helping task forces identify state-specific problems and opportunities, develop solutions, and assist with implementation of cost-saving policies, practices, and procedures. In our experience, government-nonprofit contracting task forces consistently produce pragmatic recommendations that can save taxpayers' dollars and reduce burdens on nonprofit contractors and the people served.

⁴⁹ *Partnering for Impact* Report.

Some might presume that task forces made of “opposite sides” to contracts would be contentious, but that has not been the case. In fact, governments and nonprofits are natural partners that often see the same problems that prevent everyone from accomplishing their missions efficiently. They share common goals of fixing broken systems that hurt everyone. Thus, coming together to solve common problems makes sense.

Government-nonprofit contracting reform task forces have been created under many different scenarios and can produce positive, meaningful results when the participants share a common commitment to address shared problems.⁵⁰ Just as the best solutions will vary from jurisdiction to jurisdiction, no one-size-fits-all approach exists. Here we present four forms that task forces have taken.

a. Legislative Task Forces

When state legislatures create government-nonprofit contracting reform task forces, they typically mandate bi-partisan representation and nonprofit participation. State statutes have required task forces to address the dual goals of rooting out waste while maintaining and even enhancing public accountability. For example:

- The Connecticut Legislature created a task force, recognizing that “quality and effectiveness of services are predicated upon a viable and sustainable nonprofit sector,” and that “the pursuit of efficiency and streamlining processes is a mutual goal of both purchasers and service providers.”⁵¹
- The Texas Legislature established a task force to develop “recommendations for strengthening the capacity of faith- and community-based organizations (FCBOs) for managing human resources and funds and providing services to Texans in need.”⁵²
- The Illinois General Assembly, recognizing “the State’s budget crisis,” called for a bi-partisan panel “to recognize and address the redundant monitoring and reporting requirements, which divert time and resources away from client service delivery.”⁵³

These collaborative efforts identified many of the solutions discussed later in this report: improving audit quality, with a reduction in duplication of efforts by multiple taxpayer-funded audit teams; creating electronic information repositories (also known as document vaults) that cut down on repeated paper filings that consume government resources of staff time and storage space; reducing duplication; standardizing contracts; and even the simple act of soliciting nonprofit contractor input at the beginning of the process when it can save money and time, rather than at the end when it often is too late.

b. Executive/Administrative Task Forces

Governors, Attorneys General, and other officials also have formed government-nonprofit task forces that have identified workable solutions for their states. Like their legislative counterparts, executive-created task forces seek to reduce waste, improve efficiency, and maintain and even enhance accountability:

- The Governor of Connecticut created a high-level Cabinet on Nonprofit Health and Human Service – including significant nonprofit participation – to analyze and make recommendations to enhance client outcomes and the cost-effectiveness, accountability, and sustainability of the partnerships between the state and nonprofit health and human service providers.⁵⁴
- Through an Executive Order, New Jersey’s Governor established a bi-partisan Red Tape Review Commission to review government interaction with for-profit and nonprofit organizations and make detailed findings and recommendations, including an analysis of existing rules, regulations, and legislation that are burdensome to the state’s economy.⁵⁵ In recognition of the success the Review Commission is having in streamlining

⁵⁰ *Partnering for Impact* Report at pages 2-3: “Lessons Learned from the Government-Nonprofit Task Forces.”

⁵¹ Connecticut Commission on Health and Human Services, *State of Connecticut Commission on Health and Human Services Final Report* (March 2011).

⁵² 81st Texas Legislature, Regular Session, House Bill 492, [Chapter 295](#) (May 30, 2009).

⁵³ “Streamlined Auditing and Monitoring of Community Based Services: First Steps Toward a More Efficient System for Providers, State Government, and the Community,” [Task Force Report to the Illinois General Assembly](#) (January 2011) (“*Illinois Task Force Report 2011*”).

⁵⁴ Connecticut Governor’s [Cabinet on Health and Human Services website](#).

⁵⁵ New Jersey Governor’s Office, [Executive Order 41](#) (2010).

government contracting and other problem areas, the Governor recently issued another Executive Order touting some of the successes and extending the Review Commission through 2015.⁵⁶

- In New York, the Attorney General appointed a Leadership Committee for Nonprofit Revitalization, which found that state laws “and regulatory practices have placed unnecessary and costly burdens on the nonprofit sector,” and “[r]edundancies throughout the system waste scarce taxpayer and nonprofit dollars, and bury nonprofits in duplicative paperwork and audits.”⁵⁷
- The Secretary of the North Carolina Department of Health and Human Services formed a task force of Department officials and nonprofits to develop solutions to ten specifically identified inefficiencies that nonprofits were experiencing in their DHHS contracts. The Department-level collaboration made several recommendations for reform, including prompt payment and reimbursement of full costs of performing contracted services, crafting clearer definitions to avoid confusion and delays, standardization of contracts and of monitoring processes, and shared training.⁵⁸

c. Permanent Contract/Grant Streamlining Councils

Governments and nonprofits recognize the value of resolving problems together. Eight of the government-nonprofit task forces analyzed in *Partnering for Impact* found the joint efforts so beneficial that their recommendations specifically included a call for the establishment of a formalized group of government and nonprofit officials to continue working together on contracting as well as other common issues.⁵⁹

In 2012, the Maryland Legislature created the Council for the Procurement of Health, Educational and Social Services to monitor and engage state agencies in implementing reform recommendations from the Task Force that studied procurement issues. The Council, which includes four representatives of nonprofit service providers, is also charged with providing ongoing oversight of the procurement process for human services and reporting to the Governor and Legislature.⁶⁰

The Texas Legislature created the Texas Nonprofit Council in 2013 following the recommendation of two legislative task forces.⁶¹ The Council is to work with the Interagency Coordinating Group of state agencies to strengthen collaboration between government agencies and the nonprofit sector. Specifically, it has the responsibility for making recommendations for improving contracting relationships between state agencies and nonprofits, developing best practices for cooperating and collaboration with them, and identifying and addressing duplication of existing services and of gaps in state services that nonprofits could fill.

Other states are considering various permanent structures to tap into the expertise of nonprofit contractors for improving contracting efficiencies.⁶²

⁵⁶ New Jersey Governor’s Office, *Executive Order 155* (2014). The Red Tape Review Commission recently issued a [progress report](#) noting positive reforms for nonprofit contracting/grantmaking. New Jersey’s Department of Children and Families has implemented an electronic system for bidding on contracts that reduces time and duplicative paper submissions. The State Board of Social Work Examiners has revised its licensing requirements for greater flexibility, and the Board will now defer to accreditation standards set by national social work organizations, rather than utilizing its own.

⁵⁷ “[Revitalizing Nonprofits: Renewing New York](#),” Leadership Committee for Nonprofit Revitalization Report to Attorney General Eric T. Schneiderman (February 2012).

⁵⁸ *Partnering for Impact* Report, at pages 8-9.

⁵⁹ See, e.g., *Final Report*, Connecticut Commission on Nonprofit Health and Human Services (March 31, 2011) (“Recommendation #1: An ongoing body, similar to this Commission, should be created and charged with tackling the issues before us, working to add value to the process of implementing the specific recommendations, achieving specific results over specific timeframes, and as this Commission has been, should be comprised of a cross-section of representatives from State Agencies, Private Providers and their representative organizations, Labor, and persons who are recipients of benefits under health and human services programs”); see also Hawai`i SCR-40 Dashboard Working Group Final Report (2013 set of recommendations of a Hawai`i government-nonprofit working group urging the state to, among other things, re-engineer business processes, improve communications between state agencies, and designate the State Procurement Office as a center of excellence in communicating with, and sharing best practices, training and advisory support with participating health and human services organizations).

⁶⁰ Maryland Laws, [Chapter 213](#) (enacted May 2, 2012).

⁶¹ Texas Government Code § [535.055](#) (enacted June 14, 2013).

⁶² See, e.g., Massachusetts [Senate Bill 1486](#) (2014) (proposing a permanent interagency coordinating group on the government-nonprofit partnership with the “goals of: (i) increasing the impact of state funds granted or contracted to nonprofits; (ii) improving efficiency in the grant and contracting systems and processes between state government and nonprofits; and (iii) strengthening accountability in the government-nonprofit partnership by improving the use of data and technology to inform decision-making and oversight. Further, the coordinating group shall: (i) identify and develop on-going opportunities to improve the impact, efficiency, and accountability of the government-nonprofit partnership; and (ii) make recommendations as to the need for legislation, ad hoc Commissions, or task forces”).

d. Informal Government-Nonprofit Dialogue

Nonprofits do not have to wait for government officials to invite them to discuss contracting and grant reforms. Often their work to develop solutions can be implemented without the need for legislation, chief executive action, or publicity.

For example, with the considerable assistance of charitable nonprofits in the state, Oregon's Department of Human Services successfully streamlined the process for conducting background checks for nonprofit employers whose organizations serve children, elderly, and those with disabilities. After clearly identifying the problem and conducting research to determine the root cause of extensive and costly delays, the state brought in nonprofit service providers to work collaboratively with the government team to create a vision and plan to eliminate duplication and decrease processing time. As a result of their joint efforts, processing a background check fell from nine business days to just four hours, and 22 percent fewer background checks were required each month when duplication was eliminated. The state's staff of 44 was reduced to 32, with all 12 being reassigned to other positions.⁶³ This collaborative process at a single agency saved government and nonprofits time, saved taxpayers money, and helped intended beneficiaries receive safe services more quickly.

Donors Forum, the state association of nonprofits in Illinois that also serves as a regional association of grantmakers, pioneered an excellent model for collaboration and problem solving by the public and private sectors. Its efforts culminated in the highly-endorsed "Partnership Principles for a Sustainable Human Services System."⁶⁴ Ultimately, this led to and was integrated into the creation of a legislatively created task force designed to completely overhaul Illinois' human services contracting and grant system across six state agencies. Successful partnerships also have been established in Maine and New York City.

Similarly, in 2013, the National Council of Nonprofits empaneled the National Task Force on Government-Nonprofit Contracting Reform. Task Force members are experts from government and nonprofit organizations who live in different regions of the country. They have come together to identify, exchange, and disseminate nonpartisan policies and practices that result in real systems improvements to best serve local communities.⁶⁵ They bring tremendous energy as they enthusiastically exchange information – in part because they have no other forums in which to work on vexing problems that they encounter daily. Their selfless devotion of time and sharing of their expertise is just the latest example of quiet collaboration between governments and nonprofits to better serve the public and save taxpayers money.

2. Nonprofit Liaison

Governors, Mayors, and other executive branch officials should appoint high-level Nonprofit Liaisons to oversee and promote efforts of the government and nonprofits to work together on policy issues that threaten the sustainability of charitable nonprofits on which governments rely to provide basic services to constituents.

Across the United States, few government structures exist to monitor the health and well-being of the nonprofit community upon which so many Americans rely. This is true despite the fact that charitable nonprofits contributed an estimated \$836.9 billion to the US economy in 2011, making up 5.6 percent of the country's gross domestic product (GDP),⁶⁶ and employs more than 10 percent of the workforce (13.7 million workers), contributing \$587.6 billion in wages and salaries – or 9.2 percent of all wages and salaries paid in the United States in 2010.⁶⁷ However, a few inspired government officials have discovered – and implemented – ways to open and maintain communications, thereby creating opportunities for government and nonprofits to work together on policy issues that threaten the sustainability of charitable nonprofits on which governments rely to provide basic services to constituents.

⁶³ John M. Bernard, "[Fixing a Process that No Longer Makes Sense](#)," *Governing* (February 21, 2013).

⁶⁴ Donors Forum, [Fair and Accountable: Partnership Principles for a Sustainable Human Service System](#).

⁶⁵ "National Task Force to Improve Government-Nonprofit Contracting Practices Begins Work," National Council of Nonprofits [news release](#) (June 26, 2013).

⁶⁶ Sarah L. Pettijohn, "[The Nonprofit Sector in Brief: Public Charities, Giving and Volunteering, 2013](#)" (Urban Institute; 2013).

⁶⁷ Katie L. Roeger, Amy S. Blackwood, and Sarah L. Pettijohn, [The Nonprofit Almanac 2012](#) (Urban Institute; 2012).

- In his first week in office in 2011, Connecticut’s Governor became the first in the nation to appoint a cabinet-level official to serve as liaison with nonprofits providing services to the state’s residents on behalf of government.⁶⁸
- The Governor of New York appointed an InterAgency Coordinator for Not-for-Profit Services who is responsible for tackling persistent problems that add costs and complicate otherwise effective government-nonprofit relations, including reforming contracting practices. The official is taking action on ways to streamline processes to help taxpayers and nonprofits.⁶⁹
- Several years ago, the Mayor of Denver created the Denver Office of Strategic Partnerships (DOSP) to serve as a liaison between the City of Denver and the nonprofit sector. Beyond providing a way “for both nonprofit and City staff to develop an understanding of each other’s strengths and capacities” to strengthen Denver’s communities, DOSP has trained hundreds of nonprofit leaders on how to apply for federal grants, bringing outside dollars to the City.⁷⁰ This has evolved into a cross agency-nonprofit initiative to standardize the contracting system while eliminating waste.

In these and other locations, elected officials have seen that governments and taxpayers benefit when ongoing dialogue is established – at the highest level – with solution-oriented charitable nonprofits. The core purpose of a nonprofit liaison is to establish a constructive way for government officials and nonprofit leaders to interact and communicate directly to identify problems and create coordinated reform efforts. Liaisons could also assume an ombudsman role, identifying and resolving systems problems through direct intervention on behalf of nonprofit contractors and grantees.⁷¹ Through these arrangements government executives are able to make better informed decisions based on ideas and solutions tested in the real world by organizations dedicated to serving their communities.

We recognize that un-informed cynics might look at the bad rankings of Connecticut, Illinois, and New York in the Urban Institute data and suggest that the liaisons in Connecticut and New York and the Donors Forum-led collaboration in Illinois have done no good. That would be the wrong interpretation. In our view, political and community leaders in those states saw the tremendous waste and the harm flowing from the broken systems and stepped up as leaders to take affirmative, corrective steps to solve the problems. Systems that have “complexified” over decades will not be repaired overnight. Of course, they won’t be repaired at all without determined leadership.

Accountability for Full and Prompt Payments

Since 2010 when the Urban Institute first documented the five widespread problems with government-nonprofit contracting practices, the National Council of Nonprofits and its network have been identifying and promoting solutions to those problems.

A. Failure to Pay the Full Costs of Services

As noted above in the Common Problems section, half of all nonprofits (54 percent) report problems with governments not paying the full costs of the contracted services. Significantly, the data reveal that governments routinely fail to pay for indirect costs that nonprofits incur on behalf of governments. While governments pay defense contractors, highway paving companies, and local accounting and law firms their costs – plus profits – for delivering goods and services, governments routinely and systematically do not pay nonprofits their actual costs incurred, especially their indirect costs for such things as accounting, information technology, human resources, training, governance, and management. As even government studies reveal, this short-sighted practice threatens the sustainability of nonprofits on which governments rely.

⁶⁸ “Malloy Appoints State Representative Deborah Heinrich to Cabinet-Level Position Advocating on Behalf of Nonprofit Providers,” Connecticut Governor’s [news release](#) (January 2011).

⁶⁹ “Coming Soon! A NYS Standard Contract,” *NY Nonprofit Press* (Oct. 6, 2012).

⁷⁰ [2011 Annual Report](#), Denver Office of Strategic Partnerships.

⁷¹ These roles exist at both the federal and state levels for for-profit organizations. For example, the Small Business Administration [National Ombudsman](#) will “assist small businesses when they experience excessive or unfair federal regulatory enforcement actions, such as repetitive audits or investigations, excessive fines, penalties, threats, retaliation or other unfair enforcement action by a federal agency.” In Florida, the [Vendor Ombudsman](#) acts “as an advocate for vendors who may be experiencing problems in obtaining timely payment(s) from a state agency.”

The Government Accountability Office (GAO) investigated concerns about the fiscal strain on nonprofits in its 2010 study on indirect costs.⁷² GAO found that nonprofits typically bridged the gap between the costs incurred and the level of reimbursement by making difficult choices to favor program services over the well-being of the organization. The reason behind their decisions goes to the mission-oriented culture of the nonprofit community, which GAO summarized as follows: “because many nonprofits view cuts in clients served or services offered as unpalatable, they reported that they often compromise vital ‘back-office’ functions, which over time can affect their ability to meet their missions.”⁷³ The study concluded:

As the federal government increasingly relies on the nonprofit sector to provide services, it is important to better understand the implications of reported funding gaps, such as compromised quality of important administrative functions, including information technology, human resources, legal, and accounting operations [i.e., indirect costs].... [T]hese challenges potentially limit the sector’s ability to effectively partner with the federal government, can lead to nonprofits providing fewer or lower-quality federal services, and, over the long term, could risk the viability of the sector.⁷⁴

The GAO’s findings were supported by earlier independent research showing that arbitrary limitations on overhead/indirect costs have reduced the ability of nonprofits to successfully accomplish their missions, because a strong organizational infrastructure is necessary to ensure efficient and effective services. In 2004, a joint project by the Urban Institute’s Center on Nonprofits and Philanthropy and Indiana University’s Center on Philanthropy found that “the public sector practice of providing little support for overhead costs was directly related to the existence of” the weakest organizational infrastructures occurring among nonprofits that “relied on the public sector for half or more of their revenue.”⁷⁵ In a separate study, the Bridgespan Group examined the problems that nonprofits face regarding externally-imposed, artificially-low overhead costs and identified the importance of breaking what it termed the “vicious cycle of misleading reporting, unrealistic expectations of funders, and pressure to conform.”⁷⁶ Its analysis determined the following:

The cycle has grave consequences for an organization’s ability to have impact. As unrealistic overhead expectations place increasing pressure on organizations to conform, executive directors and their boards can find themselves under-investing in infrastructure necessary to improve or even maintain service-delivery standards, particularly in the face of growth. In the short term, staff members struggle to “do more with less.” Ultimately, it’s the beneficiaries who suffer.⁷⁷

In light of these universal findings, something must be done.

3. Payment of Indirect Costs Incurred

Governments at all levels must reimburse nonprofit organizations for the full indirect costs that the nonprofits legitimately incur in delivering contracted services. Paying indirect costs will ensure that taxpayer dollars are invested to achieve the greatest impact, because research demonstrates that the most efficient and effective charitable nonprofits are those that invest in accountability, technology, and other necessary infrastructure items that are considered “indirect costs.” Federal, state, and local governments should reimburse nonprofits for indirect costs, regardless of whether the nonprofit is a prime contractor/grantee or subrecipient, and regardless of the source from which the funds originate.

In 2010, 2012, and 2013 the National Council of Nonprofits recommended that the White House Office of Management and Budget “mandate that federal pass-through dollars actually pass through fully to the deliverer

⁷² Government Accountability Office, “[Nonprofit Sector: Treatment and Reimbursement of Indirect Costs Vary among Grants, and Depend Significantly on Federal, State, and Local Government Practices](#),” Report GAO-10-477 (May 2010) (“GAO Report”).

⁷³ *Ibid.* at “What GAO Found.”

⁷⁴ *Ibid.* at page 22.

⁷⁵ Urban Institute and Indiana University, “[Getting What We Pay For: Low Overhead Limits Nonprofit Effectiveness](#),” Nonprofit Overhead Cost Project (Brief No. 3; Aug. 2004).

⁷⁶ William Bedsworth, Ann Goggins Gregory, Don Howard, “[Nonprofit Overhead Costs: Breaking the Vicious Cycle of Misleading Reporting, Unrealistic Expectations, and Pressure to Conform](#)” (The Bridgespan Group, April 2008).

⁷⁷ For more information about these and other studies, see *Investing for Impact* Report.

of services.”⁷⁸ That recommendation was based, in large part, on the studies noted above, including the in-depth analysis by the Government Accountability Office into the reimbursement practices of state and local governments. That GAO report identified significant underpayment for the indirect costs of nonprofit contractors and grantees. As a result of these practices, GAO found that nonprofits may be forced to “reduce the population served or the scope of services offered, and may forgo or delay physical infrastructure and technology improvements and staffing needs,” actions that undermine organizational sustainability.⁷⁹

Importantly, GAO found that state and local governments have not been required to reimburse nonprofits for indirect costs, even when the funds flow from a federal funding stream. In research to determine state policies with regard to reimbursing nonprofits for indirect costs, GAO reviewed six federal grant programs and investigated how indirect cost reimbursements to nonprofits were handled in three states and found substantial inconsistencies. The GAO findings in 2010 were alarming. For example, under one federal program advancing the same federal public policy and utilizing the same federal funding source, GAO discovered that a nonprofit providing services in Wisconsin was reimbursed for up to 14 percent of its actual indirect costs, Louisiana imposed an arbitrary cap of only 9.4 percent, and Maryland imposed an artificial cap paying nonprofits providing the same services zero for the indirect costs they incurred. “These differences, including whether nonprofits are reimbursed at all, largely depend on the policies and practices of the state and local governments that award federal funds to nonprofits.”⁸⁰

In June 2013, various charity watchdog groups surprised the world of philanthropy by officially reversing their thinking and publicly repudiating “*The Overhead Myth*,” that is, the conventional views about keeping indirect costs artificially low. Specifically, Charity Navigator and the Better Business Bureau’s Wise Giving Alliance, joined by GuideStar, launched an effort to “correct a misconception” about what matters most in deciding to support a charity. The three groups declared that “the percent of charity expenses that go to administrative and fundraising costs commonly referred to as ‘overhead’ – is a poor measure of a charity’s performance.”⁸¹ Their analysis, reminiscent of the warnings in the GAO report, concluded that “many charities should spend more on overhead” and that funders failing to pay indirect costs “starve charities of the freedom they need to best serve the people and communities they are trying to serve.”⁸²

The Office of Management and Budget provided definitive instructions on the issue of payment for indirect costs with the December 2013 issuance of the Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, designed to streamline federal grants rules and procedures.⁸³ The new Uniform Guidance streamlines eight former circulars into one. Among many topics, it explicitly requires pass-through entities (typically states and local governments receiving federal funding) and all federal agencies to reimburse a nonprofit’s indirect costs by applying the nonprofit’s federally negotiated indirect cost rate, if one already exists. If a negotiated rate does not yet exist, then nonprofits are empowered to request negotiating a rate or elect the default rate of 10 percent of their modified total direct costs (MTDC). As discussed previously, the most recent Urban Institute nationwide data (that excludes higher education and hospitals) found that governments arbitrarily limit indirect costs for necessary program and organizational expenses; one in four nonprofits (24 percent) reported that governments do not pay any indirect costs of the organization, and half (49 percent) reported that they were limited to 7 percent or less.⁸⁴

The OMB Uniform Guidance makes clear that a nonprofit’s indirect costs are legitimate expenses that need to

⁷⁸ National Council of Nonprofits, *Costs, Complexification and Crisis: Government’s Human Services Contracting “System” Hurts Everyone* (2010), at page 24; *Comments of the National Council of Nonprofits on OMB Advance Notice of Proposed Guidance* (April 30, 2012); *Comments of the National Council of Nonprofits to the Office of Management and Budget* (June 2, 2013).

⁷⁹ GAO Report at page i.

⁸⁰ *Ibid.* at page 11 (emphasis added).

⁸¹ *Letter to the Donors of America*, by Better Business Bureau Wise Giving Alliance, Charity Navigator, and GuideStar (2013).

⁸² See generally *Overhead Myth website*. See also the groundbreaking work in Illinois by Donors Forum, which in 2012 established the “*Real Talk about Real Costs*” campaign to create a community of practice through which nonprofits and funders could learn, discuss, and identify solutions to the long-standing problem of underfunding indirect costs. While the group has focused on Illinois, its work is expected to have a ripple effect so that these conversations are held in communities throughout the country.

⁸³ Office of Management and Budget, “*Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*,” (published in the Federal Register, December 26, 2013).

⁸⁴ Urban Institute 2013 Report, Figure 8 at page 20.

be reimbursed for the organization to be sustainable and effective. Upon issuance of the Uniform Guidance, the National Council of Nonprofits summarized its significance:

The new guidance means that nonprofits should be able to focus more on their missions and should be under less pressure to raise additional funds to essentially subsidize governments. In turn, charities with no government contracts or grants could see less competition for scarce philanthropic dollars.⁸⁵

Once the new OMB Uniform Guidance goes into effect in late 2014, governments at all levels will be required to pay the indirect costs incurred by charitable nonprofits for services provided in communities when federal discretionary funds are involved.⁸⁶

Conventional wisdom on nonprofit indirect costs is beginning to reach alignment with what for-profit businesses have known all along: continually spending less on indirect costs erodes efficiency and effectiveness, preventing organizations from producing better and lasting outcomes. Contracts and grants that fail to cover indirect costs actually reduce a charitable nonprofit's effectiveness and efficiency. For government-nonprofit contracts and grants, a shift in thinking on indirect costs is long overdue and worthy of immediate attention by policymakers whose job is to ensure that taxpayer dollars are invested to deliver the greatest impact, both today and into the future. Governments at all levels have the opportunity now to reverse outdated policies and practices regarding indirect costs and strengthen the service delivery system within their jurisdictions.

Additional Considerations on Indirect Costs

Research from the National Council of Nonprofits, documented in *Investing for Impact*, details how a combination of inconsistent terminology by governments, arbitrary application of those terms, and unrealistic expectations impair the ability of nonprofits to deliver services for which governments at all levels contract with them. Each of these issues requires further discussion and policy revisions.

4. [Joint Training Programs](#)

[As governments and their nonprofit contractors and grantees get up to speed on the changes required under the OMB Uniform Guidance and changing attitudes about indirect costs, the parties should conduct joint training programs designed to promote common understandings, collective problem solving, and mutual respect.](#)

The issuance of the OMB Uniform Guidance creates the urgent need for all parties to the grants and contracts affected by federal funding to understand their rights and obligations, and, in particular, the revised rules for cost allocation. The anticipated efficiencies achieved by uniform standards will be lost if the key stakeholders remain unaware of the changes or are ill-prepared to take advantage of them. Particularly in this time of transition, the parties should work together to develop joint training programs for government and nonprofit employees.

Government officials at the state and local levels will be called upon to revise their existing statutes and rules in order to come into conformance with the new federal standards. In particular, they must receive training on how the cost allocation rules have changed and on the alternative approaches that are permissible – and those that are not. Most will also need instruction for the first time on using federal standards for negotiating what costs are properly recoverable.

Many small and midsize nonprofits may not currently have the knowledge, systems, and records to accurately calculate their full costs. Nonprofits must develop the capacity to understand and properly allocate their costs related to contracts and grants – thus leading to more sustainable organizations. They also will want to learn how to negotiate for a reimbursement rate higher than the *de minimis* rate. Thus, the OMB directive on indirect costs has the added benefit of creating a financial incentive for charitable nonprofits to better understand and take control over their own costs for all purposes, and not just for government contracting.

⁸⁵ [Statement from National Council of Nonprofits on OMB Grant Reforms](#) (December 18, 2013).

⁸⁶ The Uniform Guidance deals with many other issues, including aspects of auditing and allocation of costs.

State and local governments, working in conjunction with state associations of nonprofits, can develop training programs on the new OMB Uniform Guidance. Joint training programs are key to ensuring full and common understanding by all parties affected by contracts and grants, thus reducing inconsistencies, duplication, and costs.

5. Clear and Consistent Definitions

Governments should provide and apply clear and consistent definitions of administrative costs, indirect costs, and overhead.

People often presume that accounting is black and white and that accounting terms are defined distinctly and applied consistently. When it comes to the topic of indirect costs, however, that presumption is wrong. Several similar, yet distinctly different, terms – indirect costs, administrative costs, and overhead costs – are often unwittingly used interchangeably, causing great confusion and harm. The inconsistent understanding and usage of these and other terms in the current OMB Circular A-122 and IRS Form 990 have contributed to the systematic underfunding of the work of charitable nonprofits, eroding their sustainability – which, as noted by the Government Accountability Office, threatens government and the public.⁸⁷

Since 1980, the federal government, through OMB Circular A-122 (that is being replaced by the Uniform Guidance), had instructed nonprofits to categorize the costs that they incur in delivering the services to the federal government into two general buckets: either direct or indirect. The A-122 then further separated indirect costs into two subcategories: either administrative costs or facilities costs. *Administrative costs* include management and general expenses such as the salaries of executives and accounting personnel and library expenses. *Facilities costs* are items such as depreciation and capital improvement, interest on debt associated with certain buildings, and operations and maintenance expenses.⁸⁸

Yet the federal government, through the IRS Form 990 that applies Generally Accepted Accounting Principles (GAAP), tells nonprofits to categorize and annually report their costs in three separate buckets, with completely different labels: Management & General, Program Services, and Fundraising. *Management & General costs* are typically activities that are required by organizations to operate, but may support multiple programs and the organization as a whole, such as accounting, human resources, staff development, rent, and utilities. *Program costs* are those that are easily attributable to a specific program or project. *Fundraising costs* are self-explanatory.

Superimposed on top of competing federal categorization systems is the confusion caused when laypeople use the similar-sounding term of “overhead.” When charity watchdog groups refer to “overhead,” they generally define this as administrative (including facilities) and fundraising costs combined.⁸⁹ When governments use the terms indirect or administrative costs, however, they do not include any fundraising costs. Governments consider the costs associated with fundraising as being separate and distinct costs unrelated to programs and unallowable for reimbursement purposes (notwithstanding that the nonprofit incurred the fundraising costs as a direct result of needing to fill financial gaps caused by governments not paying the full costs for services in the first place).

Policymakers can significantly improve compliance and performance by clearly defining each term and codifying these definitions so they are consistent at the federal level and across states and localities. The new OMB Uniform Guidance should serve as a catalyst for efforts to clarify and standardize definitions and interpretations. The Uniform Guidance combines numerous OMB Circulars, specifies more costs that are directly reimbursable, and clarifies numerous definitions and cost allocation rules. OMB and the Council on Financial Assistance Reform (COFAR) are actively working with stakeholders to identify terms and components of the Uniform Guidance that would benefit from additional explanations and training. As part of this review process OMB and COFAR issued the first set of answers to Frequently Asked Questions (FAQs), and more FAQs reportedly are being developed.⁹⁰ Federal agencies

⁸⁷ GAO Report at page 11.

⁸⁸ OMB Circular A-122.

⁸⁹ See, e.g., [Charity Navigator Financial Range Tables](#), which define “administrative expenses” as follows: “Percent of total functional expenses spent on management/general.”

⁹⁰ [Frequently Asked Questions for New Uniform Guidance](#) at 2 CFR 200, Office of Management and Budget, February 12, 2014.

have been given until the end of June 2014 to submit revisions to their existing regulations in order to conform to the new Guidance; OMB is scheduled to publish final regulations by the end of 2014.

6. Repeal of Arbitrary Caps on Indirect Costs

Legislatures should repeal existing language in statutes that set arbitrary caps on legitimate indirect costs and undermine nonprofit effectiveness. Legislatures should also stop creating new caps, significantly restrict the ability of government officials to create exceptions, and require public disclosure of indirect cost reimbursement policies and practices.

Some reimbursement rates are the result of statutory dictates by legislatures that insert arbitrary caps or other restrictions when creating a new program or designating a funding stream. These may seem fair in the abstract because they are being applied on a “uniform” basis without singling out an individual entity for underpayment. However, this means that all nonprofit contractors are being hurt, rather than all being treated fairly. After all, legislative bodies rarely impose similar uniform caps on contracts with for-profit entities (which also receive profits from government contracts). Plus, as shown, the artificial caps on reimbursement of a nonprofit’s legitimate indirect costs undermine its efficiency, effectiveness, and ability to perform vital services on behalf of the very governments that are imposing the arbitrary limits. Legislatures should replace arbitrary and artificial limits with mandates to establish standard contract and grant language and policies that fairly include full reimbursement of indirect costs.

Going forward, legislatures, as well as executive department and agency leaders, should ensure that payments of indirect rates lower than actual costs are the extremely rare exception, and even then permitted only when based on publicly available criteria and with the identification of the government department and official making the decision to withhold payment of the full costs.⁹¹ The OMB Uniform Guidance mandates that federal awarding agencies must accept and pay the negotiated indirect cost rates of nonprofit grantees. The Uniform Guidance makes clear that different rates may be paid only when capped by federal statute, or when the head of the federal agency makes a documented justification, notifies OMB, and makes “publicly available, the policies, procedures and general decision making criteria that their programs will follow to seek and justify deviations from negotiated rates.” Much of this must be done at the beginning of the process; that is, prior to issuance of a notice of a funding opportunity, and not as a last minute variance. Each of these steps is a necessary safeguard designed to ensure fairness for contracting and grant partners and accountability for the public.

7. Public Accountability through Disclosure of Indirect Cost Reimbursements

Governments at all levels should disclose for each program how much they paid in indirect costs (and percentage). They should also disclose whether indirect cost rates were determined through negotiations, arbitrarily set limits, or other method; how much money each state or local government retained of federal funds for its own overhead or administrative purposes rather than paid to pass-through entities (subcontractors and subgrantees); and how each state or local governmental entity actually used those funds.

⁹¹ See, for example, how the Uniform Guidance restricts variances:
§ 200.414(c) Federal Agency Acceptance of Negotiated Indirect Cost Rates.

“(1) The negotiated rates must be accepted by all Federal awarding agencies. A Federal awarding agency may use a rate different from the negotiated rate for a class of Federal awards or a single Federal award only when required by Federal statute or regulation, or when approved by a Federal awarding agency head or delegate based on documented justification as described in paragraph (c)(3) of this section.

(2) The Federal awarding agency head or delegate must notify OMB of any approved deviations.

(3) The Federal awarding agency must implement, and make publicly available, the policies, procedures and general decision making criteria that their programs will follow to seek and justify deviations from negotiated rates.

(4) As required under § 200.203 Notices of funding opportunities, the Federal awarding agency must include in the notice of funding opportunity the policies relating to indirect cost rate reimbursement, matching, or cost share as approved under paragraph (e)(1) of this section. As appropriate, the Federal agency should incorporate discussion of these policies into Federal awarding agency outreach activities with non-Federal entities prior to the posting of a notice of funding opportunity.”

This government accountability proposal addresses two issues. First, it is fundamentally unreasonable for governments to pay for-profit entities their indirect costs plus profits and then deny or pay smaller indirect costs to reimburse nonprofit entities. Second, when federal funds are involved, Congress and the federal executive branch need to know whether funds that they authorized to be used as pass-through dollars are actually being passed through to the entities performing the work on behalf of government for the American people. Only through reporting of indirect cost reimbursements will the American people and their elected officials be able to see whether funds are used as intended.

These same principles apply to the federal government as well. The Uniform Guidance requires reimbursement of negotiated indirect cost rates or the *de minimis* rate for multiple reasons, including promoting the sustainability of community-based organizations performing services on behalf of governments. The reporting requirement would answer the questions of whether more subrecipients are receiving reimbursement for their indirect costs and whether the amount they are receiving results in an increase from their current level of reimbursement. Those questions relate directly to concerns repeatedly expressed by the Government Accountability Office about the sustainability of nonprofit contractors/grantees that are not reimbursed for their actual costs.

B. Late Payments

As shown in the Common Problems section, almost half (45 percent) of charitable nonprofits with government contracts and grants reported problems with governments paying them later than the legal requirements in the written agreements that governments signed. This withholding of payments forces nonprofits and their private donors to subsidize government operations, at the expense of the people they serve and the nonprofits' own sustainability.

8. Prompt Payment Laws

Governors and legislatures should ensure that state and local governments pay their bills on time. State statutes requiring prompt payment, backed by a substantial and mandatory late-payment interest penalty, must be enacted and must be enforced. Legislatures should extend state prompt payment laws to local governments to ensure that the state and its political subdivisions all honor their written commitments and treat nonprofit contractors and grantees fairly.

Many states have prompt payment laws that require government agencies to pay interest penalties for payments made beyond a statutory deadline. But legal protections are not provided evenly across business and nonprofit sectors. For instance, California law provides late-payment penalties for for-profit businesses and smaller nonprofits, but exempts nonprofits with contracts of \$500,000 or more from the protections.⁹² Moreover, the presence of such a law does not mean it will be applied in a way to actually ensure payments. Just consider Illinois, which owes more than \$5 billion despite a statute mandating that “if payment is not issued to the payee within [a] 60 day period, an interest penalty of 1.0% of any amount approved and unpaid shall be added for each month or fraction thereof after the end of this 60 day period, until final payment is made.”⁹³ Thus, the statutory right to prompt payment can be illusory to the nonprofit employees who get laid off or the individuals in need who are not served when governments fail to meet their contractual obligations. Public leadership is needed at the highest levels to stop this repeatedly occurring practice.

9. Prompt Contracting Laws

Governors and legislatures should ensure that services provided on behalf of state and local governments are performed pursuant to written agreements that are signed prior to commencement of work. State statutes requiring prompt contracting, backed by a substantial and mandatory late-contracting interest penalty, must be enacted and must be enforced.

⁹² See [California Government Code § 927.6](#). “However, a nonprofit organization shall only be eligible to receive a penalty payment if it has been awarded a contract or grant in an amount less than five hundred thousand dollars (\$500,000).”

⁹³ Illinois State Prompt Payment Act, 30 ILCS 540; see also Illinois Local Government Prompt Payment Act, 50 ILCS 505.

Nonprofit contractors cannot get paid without having a contract in place. Yet in several states, governments award contracts to nonprofits expecting the nonprofits to begin performing immediately – but then fail to officially sign the contract documents for several months, leaving nonprofits in limbo. To counteract this problem, a few states with this recurring problem have enacted not only prompt payment but also prompt contracting laws.

New York State has perhaps the toughest prompt contracting statute in the country. Yet a culture has flourished there of not paying nonprofits on a timely basis or contracting with them on a timely basis.

As noted in the Common Problems section, New York’s Comptroller found that in 2012 state agencies failed to meet contracting timelines for approximately four out of every five contracts (78 percent), results that are virtually unchanged from 2011, when 80 percent of contracts were reported late. Without strong political leadership – and without substantial penalties, duly enforced, to ensure accountability – even prompt contracting laws can be illusory. There is no real substitute for government agencies working directly with their nonprofit contracting partners to get the paperwork and administrative burdens out of the way early so that the focus can return to where it belongs: on the people and communities that the nonprofits serve.⁹⁴

10. Public Disclosure of Government Accountability

Governments at all levels should establish disclosure mechanisms that inform the public on the timeliness of payments by government agencies to contractors, whether the agencies are required to pay late penalties, and how much and when those payments are made.

Each year, the New York State Comptroller publishes a report detailing the compliance by state agencies with New York’s prompt contracting laws. Except for some bad press the state may get for a few days after the report is released at the end of May, the contracting and payment performance of state agencies receive little public scrutiny. Florida’s Department of Children and Families, on the other hand, reports much more frequently, publicly disclosing a monthly “scorecard” of strategic indicators, including percentage of “payments presented & processed timely.”⁹⁵

Government agencies should report the timeliness of their payments to contractors and the results should be posted monthly on a central website. The public and individual contractors have a right to know how their governments are operating, and which government agencies and departments are performing most (and least) efficiently and effectively. Timely data on contracting and payment performance will provide contractors with needed information to gauge their ability to withstand payment problems, while also providing incentive for government agencies to improve operations that benefit the public good.

Elimination of Unilateral Mid-stream Contract Changes

More than half (52 percent) of nonprofits reported problems because governments were changing the terms of their written contract/grant agreements after they were signed. The public needs to have faith that its own government will honor its commitments rather than change them when convenient. Such changes increase operational, financial, and administrative strains on nonprofits. The following proposals would reduce the interruptions documented by the Urban Institute survey.

⁹⁴ Since 2011, Connecticut’s Office of Policy and Management has maintained a policy that each state agency contracting with nonprofits must execute at least 95 percent of contracts no fewer than 15 days prior to the commencement of services: “The late execution of contracts imposes costs on nonprofit providers and is not an acceptable business practice for either the State or its providers.” See Benjamin Barnes, Secretary, Office of Policy and Management, February 11, 2011, [Memorandum](#) re: Health and Human Services Purchase of Service Contracting Reforms.

⁹⁵ See, e.g., “Region Balanced Scorecard, [Strategic Indicators November 2013 Report](#),” Florida Department of Children and Families. Although not made publicly available, Florida agencies are also required [on a daily basis] to report their prompt payment compliance and assessed interest penalties to the Vendor Ombudsman within the Department of Financial Services. See Florida Chief Financial Officer [Memorandum No. 01](#) (2013-2014), August 6, 2013.

11. Independent Government Office to Protect Charities from Contracting Abuses

States should create an independent office to ensure accountability so state and local governments are honoring the terms of their written agreements and not changing them unilaterally mid-stream. Alternatively, State Attorneys General, invoking their authority and responsibilities under the doctrine of *parens patriae* to protect charitable assets and the public trust, should accept complaints filed by charitable nonprofits, investigate, and intervene to stop state and local governments from unilaterally changing contract terms mid-stream that have the effect of increasing costs on charitable nonprofits.

On the surface, it might appear that charitable nonprofits have no remedy to oppose unilateral, mid-stream contract changes by governments other than refusing to comply or going to court. Refusal to comply jeopardizes the entire contract and the people the nonprofit is serving. Litigation imposes tremendous costs, creates hostility, and diverts nonprofit employees from their mission. Without a counterbalance for accountability, such as a neutral place for nonprofits to express concerns, resolve contract disputes before damage is done, and seek relief, there is no visible deterrent stopping a government employee from making unilateral changes that impose additional costs on charitable nonprofits.

One solution would be to create an official Ombudsman, Inspector General, or whistleblower center to investigate and resolve contract disputes. As a matter of public integrity, each jurisdiction should consider establishing such an independent office as a sign of good faith and a reminder to its own employees. As a matter of sound public policy, each state should establish such an office with statewide authority to review all contract disputes between charitable nonprofits and governments at the state and local levels. Having a centralized office will enable tracking of commonly occurring problems to inform focused training, as well as tracking of sources of reoccurring problems such as a particular government unit or employee.⁹⁶

In the alternative, State Attorneys General should make charitable nonprofits aware of their existing – although to date unused – powers to intervene in some disputes. State Attorneys General, under the common law doctrine of *parens patriae*, have the authority to intervene both to protect charitable assets and protect the public trust. Attorneys General already invoke that authority regularly in antitrust, consumer, and environmental contexts, as well as for oversight of charitable assets. For example, when consumers believe that a business has treated them unfairly by changing the terms of an agreement, they can turn to the state Attorney General's Office to file a complaint. In addition to providing an avenue for recourse, this process allows the Attorney General to see patterns of abuse, such as how many complaints against a given company or a pattern of complaints within a given industry. The Attorney General then has a variety of powers at his or her disposal to protect the public.

The public is disserved when charitable assets – assets dedicated to the public good – are wasted, whether as the result of insider wrongdoing or governmental overreach and arbitrary action. Invoking the legal doctrine of *parens patriae*, Attorneys General have protected the assets of charitable organizations, usually from insiders. But the concept is the same: if the Attorney General is to step forward in the name of the public to protect charitable assets from being taken or wasted, it should be done across the board. As true guardians of charitable assets, Attorneys General must protect against harm and wasteful diversion of assets perpetrated by any and all, including those within government.

Some might say that an Attorney General would have a conflict and could not do this work. But if citizens complain that a state body or local government has violated the Open Meetings or Public Records Laws, the Attorney General's Office can investigate and take action. Each Attorney General Office has procedures for dealing with potential conflicts, such as when citizens complain that a state board or official represented by the Attorney General has breached its duty in some way. Similarly here, the Attorney General can step in to protect the state's own interests of ensuring that individual state or local government employees, officers, and agencies are honoring rather than

⁹⁶ Florida's Legislature has created such a program in the Department of Financial Services, not to monitor for improper contract changes mid-stream but to monitor each agency's compliance with prompt payments. It specifically provides that employees found responsible for persistent failure to make timely payments to contractors may be subject to dismissal. See Florida Statutes, Tax and Finance §215.422. Florida also offers a [Vendor Ombudsman](#), "whose duties include acting as an advocate for vendors who may be experiencing problems in obtaining timely payment(s) from a state agency."

breaching the government's signed and legal binding written agreements. If the government can freely breach its agreements by imposing costly new terms, then public trust in government and faith in the value of all written agreements will evaporate.

The knowledge that an Ombudsman, Inspector General, or the Attorney General might intervene should serve as a deterrent to stop the current one-sided, mid-stream changes to written agreements and lead government employees and officials who want to change contract terms to do so via renegotiations and formal contract amendments that provide for paying the costs of any new expenses. Indeed, such an independent authority may stop – through deterrence or remedial action – the other unfair practices, such as late payments and late contracting, that also waste charitable assets.

12. Standardized Language for Contracts and Grants

State and local governments should standardize contract and grant language across multiple agencies to secure the savings attainable through reduced negotiating costs, standardized attachments and forms. Reporting requirements should be standardized as well for consistency across government agencies, while also ensuring compliance with federal guidelines (where governing) and general accounting principles.

The benefits of having standard language for a contract or grant cannot be overstated. In addition to creating consistency in the definitions that can be used when negotiating and enforcing contracts and grants, uniform terms can eliminate some of the mid-stream changes that get made after agreements are signed.

Typically, each government agency creates its own application forms and identifies what specific information is to be provided. Anyone who has completed a few applications knows that aside from program specific details, the core information they must supply is consistent from one application to the next. Yet there can be wide variances when preparing an application in terms of the different forms, format, phrasing, and order in which to provide the information. Standardized formats and forms would make applications easier to complete, plus be easier for governments to review and compare. This also prepares for more consistent reporting and monitoring after an award is approved. Similarly, budget formats should be in accordance with Generally Accepted Accounting Principles (GAAP) and follow the Unified Chart of Accounts rather than different government agencies asking for uniquely different formats.

Excellent examples of standard contracts are readily available. The Connecticut POS Standard Contract contains all core provisions in a 30-page document.⁹⁷ New York State released its new standard contract in 2012 after consultation with charitable nonprofit contractors.⁹⁸ The New York standard contract will be used by all state agencies contracting with nonprofits to provide services.

Even the process for developing common language for all written agreements can promote consistency that eliminates mid-stream changes. Plus, a sound process can help reduce redundancy in forms and processes as government officials evaluate which legal provisions are required by law, which are essential for maintaining public accountability and fiscal oversight, and which are unnecessary. To this end, a recent Illinois law calls for the creation of a common service taxonomy for human services providers to include, but not be limited to, a common list of terms to define services, processes, and client populations.⁹⁹ It is essential that during the process of developing standard language, attention must be devoted to standardizing what can and cannot be included within allowable costs across

⁹⁷ See Connecticut [POS Standard Contract](#). See also general background materials regarding [Standard Contract](#) on the Connecticut Office of Policy and Management website.

⁹⁸ See New York's [Grants Reform](#) website.

⁹⁹ See Illinois Public Act [097-0210](#) (July 2011).

all agreements, rather than being established separately through each funding opportunity or agency.¹⁰⁰ Coordinated actions will eliminate costs associated with preparing separate reports according to multiple sets of guidelines, enhance transparency, and promote greater compliance.

One respondent to the Pulse Poll explained the value of standardization quite succinctly.

Various government grant-makers ... use the eGrant system and require similar information, but require it at different times and in different formats. It would be a great time-saver, especially for non-profits that rely largely on volunteers, if agencies developed common application and evaluation forms. (DE)

Excluding specific differences in programmatic requirements, standardizing contract requirements across government agencies eliminates the need for government to have repeated individual contract approvals, as well as removes redundancies and conflicts that frequently occur when each agency creates its own contract documents. It also establishes consistent expectations in the requirements, eliminating the need for a substantial portion of mid-stream changes. The new OMB Uniform Guidance is attempting to standardize and make consistent the funding agreements, application, and reporting requirements by limiting the use of forms to only those approved by OMB. The OMB must approve variations from the permitted forms, established requirements, or requests for additional information and have indicated their intent to limit approval of these kinds of changes.

13. Ongoing Provider Input

Governments should institutionalize methods to regularly obtain input from nonprofits about how contracting and grant processes, as well as program design and implementation, can be improved. Barriers to open and public exchanges of ideas and solutions should be eliminated.

State ethics and contracting laws appropriately prohibit individuals and organizations from improperly attempting to influence the drafting of Requests for Proposals (RFPs) and similar documents in ways that would provide them with unfair advantages. These restrictions, however, can have the unintended consequence of walling off government program and contracting officers from the work that will be performed on behalf of government, thus limiting their understanding of the real-world impact of the written agreements they are drafting.

The Maryland Legislature remedied this problem in 2012 by allowing state agencies to receive input and comments from provider groups on RFPs in their draft stage.¹⁰¹ It is anticipated that the new approach will improve the quality of the RFPs and reduce the number of amendments that have bedeviled contractors in the state for years. If the government has a more informed view of service delivery requirements and restraints in advance, there will be less need to try to change the terms of the agreements after they are signed, as well as reduce issues with prompt contracting.

Experience finds that, when opening up the application process to encourage informed insights through pre-RFP meetings with providers, it is important to ensure fairness for all potential bidders. There are established procedures to facilitate these important discussions prior to the crafting of a RFP without resulting in any nonprofit receiving an unfair advantage. Typically, efforts should not be attempted with individual nonprofits, but instead with group meetings in open settings.

¹⁰⁰ While necessary, it must be acknowledged, as the federal Office of Management and Budget has done, that full standardization of cost determinations cannot be achieved for all programs and for all types of charitable nonprofits. See, e.g., OMB Uniform Guidance §200.414(b): “Because of the diverse characteristics and accounting practices of nonprofit organizations, it is not possible to specify the types of cost which may be classified as indirect (F&A) cost in all situations. Identification with a Federal award rather than the nature of the goods and services involved is the determining factor in distinguishing direct from indirect (F&A) costs of Federal awards. However, typical examples of indirect (F&A) cost for many nonprofit organizations may include depreciation on buildings and equipment, the costs of operating and maintaining facilities, and general administration and general expenses, such as the salaries and expenses of executive officers, personnel administration, and accounting.”

¹⁰¹ Maryland Laws, [Chapter 707](#) (enacted May 22, 2012).

Simplifying Complex Application and Reporting Requirements

When almost three-quarters of all nonprofits with government contracts/grants reporting problems due to complicated application and reporting requirements, something is obviously broken. Here are a few ways to address some common problems.

14. Document Vaults

States and local governments should significantly reduce redundancy in the application process by creating an electronic repository or “document vault” to house in a central location all commonly required documents relevant to bids for government contracts and grants, and to which each contracting agency would have access.

Virtually every time a nonprofit responds to a government Request for Proposal (RFP) or Request for Qualifications (RFQ) it must provide multiple hard copies of approximately twenty different documents, including its IRS Letter of Determination, its Articles of Incorporation, its Form 1023 Application for Tax Exempt Status, its Bylaws, its licensing and credentialing document(s), its recent Form 990 informational tax returns, its list of board members, its most recent audit(s), its organizational charts, its personnel policies, and more. Each government agency and each RFP and RFQ will require different documents arranged in different order. Submitting documents out of order can disqualify a proposal, meaning nonprofits must devote extra time for every proposal to triple-check that the submission package meets the unique requirements for that application.

The government side of the RFP equation is even more paper intensive. Once the application from each nonprofit organization is received, multiple copies are printed and distributed to several state employees for review, each having his or her own files to maintain. Next, if the application is selected for funding, more copies are made to distribute to those who will be negotiating, reviewing, and ultimately approving an actual written agreement, in addition to those government employees who will be managing and monitoring it. And even the paperwork of those not selected must be maintained in file cabinets for a certain number of years in case there is a bid protest or to comply with public records laws. On top of all this paperwork is the human side: having enough state employees to receive, maintain, retrieve, archive, and then review documents when requested.

The money- and space-saving solution to this growing problem is a document vault – an online electronic repository where nonprofits can upload all of their core required documents for any government employee to access as appropriate. Several governmental entities have already started the process of implementing document vaults as a way to save money for both government and nonprofits by streamlining some of the contracting processes. Working with the charitable nonprofits in their states, each has developed a system that best meets its own needs. What is particularly impressive is that most have done so with little or no additional implementation costs.

For example, Connecticut utilized its existing online procurement system (BizNet) to create an online portal to house standard contract and grant documents for nonprofits. This has reduced the burdens associated with Purchase of Services (“POS”) contracting processes. As of July 1, 2012, all nonprofits with POS contracts in Connecticut are required to register on BizNet as contractors and store the documents required when applying for contracts in this online system. Currently, six different health and human services agencies are able to access this information electronically, removing the need for staff to handle all of the previous paper.

New York City created and hosts a secure, web-based contracting system, the HHS Accelerator, to support the nonprofit sector by improving contracting procedures and reduce costs.¹⁰² The Accelerator contains a document vault that allows nonprofits to maintain standard documents. It also includes a pre-qualification process for potential nonprofit contractors and provides notifications of funding availability and the ability to respond to those notices. Any nonprofit may sign up and include its documents in the document vault, and can even give others, such as foundations, access to those documents. As noted earlier, New York State has launched a Grants Gateway that could ultimately incorporate a document vault component as envisioned here.

¹⁰² New York City [HHS Accelerator](#).

Illinois created the Management Improvement Initiative Committee (MIIC) in 2011 to improve government-nonprofit contracting practices and procedures.¹⁰³ As part of its efforts, the state utilized existing software and IT staff to develop a document vault, known as the Centralized Repository Vault (CRV), to house a standard list of documents from nonprofits contracting with six different human services agencies. The Illinois CRV, in its first three months of operation, saved the state \$40,000 in printing costs alone. Currently, more than 1,600 nonprofits have signed up and are using the system, with a compliance rate of 93 percent. One Illinois official estimates that simply by not having to manage the 6,500 paper documents now in electronic form the state is easily saving more than \$100,000 annually.

While each jurisdiction developing a documents vault has created its own model based on specific needs and available resources, there are commonalities beyond the development of the actual technology to consider that undoubtedly have contributed to success. In all of these cases, there was strong support from both the executive leadership and the legislature. This is particularly important if the system will be used across multiple state agencies, which is essential to streamlining and starting to standardize contracting processes and procedures. Additionally, the document vaults were developed with ongoing input from the nonprofit community, ensuring a more user-friendly system while building collaborative relationships between government and charitable nonprofits. Together, these key elements create an environment poised for success.

Document vaults give states and municipalities the opportunity to free up staff time to attend to the real work needed to be done and save thousands of dollars in printing and paper costs. These electronic repositories also enable nonprofit contractors and grantees to devote more personnel to direct service activities while reducing wasteful printing, paper, and postage costs. As a result, taxpayer dollars are used much more efficiently and for their real purpose of helping residents.

15. Standardized Monitoring and Reporting

Governments should reduce redundant monitoring by standardizing and integrating reporting procedures across multiple government agencies. In particular, governments should standardize administrative requirements, consolidate and standardize forms and reporting processes, and develop and use common language, and apply them consistently across services and agencies, with particular emphasis placed on fiscal and general administration documents.

Monitoring generally refers to reviewing adherence to program elements, requirements, and organizational process associated with a contract or grant exclusive of the financial components. Various government agencies may establish different requirements that at times conflict with those of others or require nonprofits to keep the same information in multiple ways to comply with each agency's guidelines.

Identifying existing duplication is not the only way to find savings. The task force in Illinois found that "it is important to not only 'fix' the existing problems, but develop processes for incorporating proposed requirements into the overall structure of monitoring procedures, in order to avoid creating new redundancies."¹⁰⁴ Among many recommendations, that task force called for the creation and implementation of an inter-departmental process to cross check potential new requirements to avoid creating additional redundancies. The Illinois task force specifically urged the standardization of administrative requirements, consolidation of forms and reporting processes, and their application consistently across services, with particular emphasis placed on fiscal and general administration documents.

¹⁰³ See Illinois Public Act [097-0558](#) (2011).

¹⁰⁴ See *Illinois Task Force Report 2011*.

16. Standardization and Consolidation of Audits

Government agencies should standardize and consolidate audit requirements to avoid repeated and unnecessary audits, and to reduce interruptions in nonprofit program services. Government agencies should also share the results of audits with each other, both to enhance understanding of the work of the nonprofits, as well as to strengthen intergovernmental communications and efficiency.

Typically each government funding stream requires an audit to ensure that taxpayer dollars are used as intended. As a result, nonprofits with multiple government grants and contracts often undergo multiple audits of their financials each year, many of which are duplicative. Additionally, governments experiencing their own budget cuts are trying to keep up with their responsibilities despite fewer staff to complete as much or more work.

Use of shared/standardized audits is a significant way to reduce the costs and time for governments and nonprofits alike, without reducing accountability. It entails combining the different elements and eliminating the duplication inherent in multiple audits conducted by multiple agencies and people, into one audit of a nonprofit conducted by the state.

Illinois has assumed a leadership role in working to streamline the audit process to reduce costs and duplication. A task force report in late 2010 noted that many state audit mandates were redundant, pointing out that most nonprofit human services providers submit to an annual comprehensive independent audit, conducted by external certified public accountants as well as their Single (A-133) audit, if required. The task force recommended, among other things, that state agencies accept the nonprofit's independent CPA audit in place of specific state department audits, when the CPA audit meets federal requirements and the funding received is tested as a major program. It also called for creation of a centralized unit for fiscal control review (also known as "desk reviews") for all human service departments, and standardizing audit requirements and fiscal report formats across state agencies and divisions.¹⁰⁵ The legislature took these recommendations seriously and amended the Illinois Grant Funds Recovery Act by creating a Single Audit Commission to develop and report back to the Legislature on improving consolidated/shared audits, as well as offering recommendations on the entire grants process in Illinois.¹⁰⁶

¹⁰⁵ HB5124 Task Force Report (December 31, 2010), summarized in *Partnering for Impact* Report.

¹⁰⁶ See Illinois Public Act [098-0047](#) (2013).

Conclusion

In the old courts of equity there was a Latin legal maxim, *ubi jus ibi remedium*, which translates to “where there is a right, there must be a remedy.” Throughout this paper, we have followed the parallel principle that for every problem there must be solutions. The problems in the current government-nonprofit contracting “systems” across the country are profound, thoroughly documented, and, most importantly, solvable. The solutions discussed in this report are tested, free or relatively inexpensive, and readily available.

All that is needed are people of goodwill, a commitment to identifying the solutions most appropriate to the jurisdiction, and the motivation to take action. Whether that motivation comes from outrage, sheer frustration, the specter of financial collapse, political leadership, or a simple recognition that the *status quo* is the common enemy – it does not matter.

What matters is that people in government and nonprofits talk with each other. By way of this paper, the network of the National Council of Nonprofits extends an open invitation to all people of goodwill – officials within government, frontline nonprofit employees and volunteers, individuals relying on services, taxpayers, and politicians – to work with you to identify the problems that need solving immediately, to craft the appropriate solutions, and to take action to get them implemented.

For additional information on government-nonprofit contracting issues and solutions,
please visit our dedicated web portal at www.govtcontracting.org