Child Care

Current Program

Over the past decade, recognition of child care as a critical public policy issue has dramatically increased. The public's attention is fueled by several factors, including the unprecedented numbers of mothers in the workforce; the high cost of care; a shortage of providers in many communities; and an increased awareness of the importance of early childhood development.

State and federally funded child care has become an essential work support for low-income families, as well as an important tool for promoting child development and learning. The passage of welfare reform legislation in 1996 ended the entitlement to cash assistance, placed a time limit on assistance, and emphasized the transition from welfare to work. This landmark legislation also was the impetus for a dramatic increase in federal and state child care funding, since a focus on clients making the transition to work required that states provide work supports such as child care. More recently, there has been a national focus on the importance of quality child care to early childhood development and education. Child care is no longer considered merely a work support, but rather an opportunity to make a positive impact on the growth and development of children.

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As child care funding has increased, the role of state child care agencies has changed and expanded. Child care agencies are clearly critical to the success of both welfare-to-work and school readiness programs. These agencies also play an important role in coordinating the myriad publicly funded child care programs, including Head Start and state-funded pre-kindergarten. In many states, the responsibility for regulating and licensing child care providers and ensuring the health and safety of the children in care also falls to the state child care agency. In addition, state child care agencies are a primary driver of quality improvement, supporting a vast array of quality initiatives such as consumer education campaigns, teacher training and education, and tiered reimbursement. Finally, child care agencies have a significant impact on the child care industry and state economies. Economic analyses of child care subsidies demonstrate that they create a substantial number of jobs and contribute to the state's economic well-being. Public child care dollars help subsidize local child care businesses and therefore create jobs and provide the necessary infrastructure to attract other businesses to the state.

Much of the recent growth in federal and state child care spending resulted from passage of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA, P.L. 104-193), which created a new welfare program, Temporary Assistance for Needy Families (TANF).

PRWORA replaced federal welfare and child care entitlement programs with block grants to states that provide a set amount of funding and allow state flexibility to design programs. The legislation consolidated major federal child care programs into the Child Care and Development Fund (CCDF) and increased federal funding for child care by approximately $4 billion over six years.

CCDF is the primary source of federal and state funding for child care, providing $4.8 billion in federal funding and $2 billion in state funding in fiscal year 2004 and serving an average of 1.8 million children each month. CCDF is composed of four funding components: discretionary funds, mandatory funds, matching funds, and state maintenance-of-effort (MOE) funds. Discretionary funding, also known as the Child Care and Development Block Grant (CCDBG), was $2.1 billion in FY 2004. A portion of the CCDBG discretionary funds are "set-asides," required to be used for certain child care activities, usually related to quality. For FY 2004, the quality set-asides were $19 million for child care resource and referral services and school-age child care activities; $100 million for infant and toddler quality improvement; and $172 million for general child care quality improvement activities.

Mandatory funds are provided as an entitlement to states and do not require congressional appropriation. Approximately $1.2 billion in mandatory funds was distributed to states in FY 2004. Matching funds were a new source of child care funding included in the welfare reform law and were funded at $1.5 billion last year. Matching funds are also entitlement funds and do not require annual appropriations. To gain access to matching funds, states must meet a child care MOE level equal to the state matching dollars expended in FY 1994 for Aid to Families with Dependent Children (AFDC)–related child care programs. After the MOE is satisfied, states match the federal funds at the Federal Medical Assistance Percentage (FMAP). In FY 2003, states spent $2 billion to meet MOE and matching requirements.

In addition to CCDF, TANF and the Social Services Block Grant (SSBG) are significant sources of child care funding. States have the option of transferring up to 30 percent of their TANF funding into their CCDF grant or spending TANF dollars directly on child care services for TANF-eligible families. In FY 2003, states transferred $1.8 billion of TANF funds into CCDF and spent $1.7 billion of funds directly on child care services. SSBG may also be used to fund child care services, as well as a broad range of other social services. In 2002, states spent $99 million in SSBG funds on child care.

Another complimentary federal funding source for child care and early learning is Head Start and Early Head Start. These programs provide comprehensive development, education, health, and nutrition services for low-income children and social services for their families and focus on improving school readiness. Head Start funding is awarded directly to local grantees, not to states. Historically, Head Start has been predominately a part-day, part-year program. In recent years, due to recognition of the overlap in families served, greater efforts have been advanced by states, the U.S. Department of Health and Human Services (HHS), and in reauthorization legislation to blend funding and increase collaboration between state child care programs and Head Start. The intent is to extend services to full day and full year so that families in need of such complete child care services will not be required to move their children between Head Start and other child care providers. In FY 2004 Head Start funding was $6.8 billion and served approximately 900,000 children.

In 1998, Congress created the 21st Century Community Learning Centers (21st CCLC), which provide after-school learning opportunities for children in a school setting. Grants from this program are awarded to state education departments, which manage statewide competitions and award grants to local organizations. The program funding has steadily grown since its inception, and in FY 2004 funding reached just under $1 billion. While this program is viewed by some as after-school child care, the range of programs that are funded across the country is varied and may not always address child care needs.

Federal law permits states to use CCDF funds to provide child care for families whose income does not exceed 85 percent of the state median income (SMI). However, states may impose lower income eligibility limits. In their FY 2004–2005 state plans, states reported eligibility limits ranging from 28 percent to 85 percent of SMI. The average eligibility level in 2003 was 59 percent of SMI, down from 62 percent in 2001. In their FY 2004–2005 plans, 26 states reported lower income eligibility levels than in their FY 2002–2003 state plans.

In addition to establishing income eligibility limits, federal law requires that children served by CCDF must be under age 13 and live with parents working or participating in education or training or require protective services. States must give priority to children with special needs or in “very low-income” families. States also must use 70 percent of CCDF funds for families receiving TANF or at risk of requiring TANF assistance.

The majority of CCDF child care assistance is provided through vouchers or certificates that families may use to purchase child care from any legally operating provider. The provider may provide services in a center, a family child care home, or in the child’s home. In addition to offering vouchers, 26 states contract directly with providers to offer child care to families eligible for CCDF assistance.

States use biennial Market Rate Surveys (MRS) to establish subsidy reimbursement rates. In their FY 2004–2005 plans, only 23 states set rates at or above the 75th percentile of MRS. More than half of states have established higher rates for providers that meet certain quality standards, provide care for children with special needs, or provide care during non-traditional hours.

In addition to funding direct services, states may use up to 5 percent of CCDF funds on administrative expenses and are required to use at least 4 percent of funding on improving quality and access to child care. However, many spend less than 5 percent on administration, and the majority of states spend more than 4 percent on quality. In FY 2004–2005 state plans, the average quality expenditure was 7 percent of CCDF funds.

Both the TANF and CCDF block grants expired at the end of FY 2002 and have been extended to date through a series of short-term extensions. In the 108th Congress, TANF and CCDF reauthorization legislation was introduced, but never passed. Similar bills are expected in the 109th Congress. TANF proposals would increase mandatory work hours from 20 to 40 for mothers with children under age 6 and from 30 to 40 hours for all other TANF clients. In addition, the percentage of TANF clients placed in work activities would grow from 50 to 70 over five years. States expressed concerns that the increase in work requirements would place a serious burden on child care programs and argued that additional resources were necessary. House-passed legislation would authorize $1 billion increase over five years in child care mandatory funding and $1 billion in discretionary funds. The Senate approved a $7 billion increase in mandatory matching funds over 5 years, waiving the state match for these funds for the first three years. CCDF reauthorization measures introduced in Congress would also raise the quality set-aside from 4 to 6 percent; impose new data reporting requirements; increase the TANF transfer from 30 to 50 percent; and set new outcome goals directed at early childhood development and education.

Challenges

As CCDF awaits reauthorization, some key challenges, as well as opportunities for improvement, face the program. Child care funding must be enhanced to help meet the demand for child care in states. Adequate child care funding is vital to helping families successfully make the transition from TANF to work, helping other low-income families maintain employment, and enhancing early childhood development and learning. In addition, the flexibility of CCDF funding must be maintained. The block grant structure of CCDF has allowed states to create programs that are tailored to their state's families and providers and to create statewide infrastructures that benefit all child care consumers. State success in administering child care programs depends on flexibility in the types of services and activities (including quality initiatives) funded and flexibility in using CCDF for licensing and other regulatory activities. Reauthorization also presents an opportunity to streamline child care funding by modifying obligation and liquidation schedules and consolidating all set-aside funding.

Since the inception of CCDF, states have worked to improve the quality of child care and to increase collaborations with other federal and state programs that fund child care. Continued federal support for national and local quality research and for a diverse array of state quality goals and activities are essential to assuring that child care is developmentally appropriate and provides an environment for growth and learning. Coordination between CCDF and other child care programs, such as Head Start, helps make sure that families are receiving the services that best fit their needs in the least burdensome manner possible. Continued efforts to promote program collaboration must strive to reduce administrative complexities, while respecting parental choice.

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A major potential challenge for state child care programs is Internal Revenue Service (IRS) policy that would require states to act as the employer of informal child care providers when the state provides a child care subsidy to that provider. Some regional IRS offices are interpreting IRS code to hold states responsible for paying and withholding taxes; they reason that since state funding pays for the child care services, this fact makes the state the provider's employer. National policy requiring states to pay employer taxes for informal providers paid with CCDF or TANF funds would have a substantial negative impact on child care programs; it would increase the costs of individual subsidies and reduce benefits and services, and could possibly limit parental choice and access to care.

Finally, program integrity poses potential challenges and opportunities for states. Federal implementation of the Improper Payments Information Act of 2002 (IPIA, P.L. 107-300) offers an opportunity to focus on improving program integrity. States support program integrity initiatives that respect state diversity, are cost-effective, provide additional funding for improved technology, focus on prevention of fraud, and do not create any additional burdens on child care consumers. Implementation of a national error rate, however, would create a new administrative burden and expense. It would not be able to accurately capture the extent and nature of states' improper payments due to the extent of state differences in program design.

Recommendations

Proposal

Increase CCDF funding and maintain TANF funding level and TANF transfer authority.

During the 108th Congress, the Senate approved an amendment to increase child care mandatory funding by $7 billion over five years, with no state match required for the first three years. APHSA continues to support such an increase. In addition, new funding dedicated to information technology is needed. With new data reporting requirements, there is a growing need to gather data from state child care systems. Additional requirements should be accompanied by additional federal funding.

The current TANF funding level and authority to transfer up to 30 percent of TANF funding to CCDBG must be maintained. TANF funding is critical for child care. The majority of states use TANF for child care; therefore, any cut to TANF or transfer authority would result in decreased child care funding.

Explanation

Current federal child care funding is inadequate to meet the needs of all families eligible for CCDF assistance. States have the option to provide child care assistance for all families with incomes up to 85 percent of SMI, but the majority of states have set the income limits much lower due to a lack of funding. In recent years, state budget deficits, as well as increasing demand for care, have forced states to reduce eligibility or postpone quality and early learning initiatives. Subsidized child care is critical to keeping former TANF beneficiaries employed and helping current beneficiaries find sustainable employment. Even as state welfare caseloads have fallen, the need for child care continues to grow. In addition, any increases in TANF workload participation requirements will necessitate an increase in child care funding.

In addition to increased funding for direct services, new funding dedicated to information technology must be provided. Chronic child care funding shortages have resulted in limited investment in data systems and other technology in recent years. Improved data capability is an important tool for both improving child care quality and reducing fraud and improper payments. It is also necessary for meeting federal data reporting requirements. Other technology improvements, such as automated payment and attendance tracking systems and websites with licensing and quality information, can help improve quality, increase consumer awareness and satisfaction, and reduce fraud.

Proposal

CCDF obligation and liquidation schedules and set-asides should be streamlined.

Obligation and liquidation schedules for mandatory, discretionary, and matching funds should be examined for ways to streamline the rules. If schedules across the three parts of CCDF are merged, states should at minimum have two years to obligate and two years to liquidate CCDF funds as well as TANF transfer funds.

Existing quality set-aside funding should be consolidated and funding rules attached to the existing requirements should be streamlined. In addition, broad statutory language should be added to clarify that set-aside funding should be used to fund infant and toddler programs, resource and referral activities, and other child care quality initiatives states deem appropriate.

Explanation

Simplifying current funding policies would greatly reduce state administrative burdens and free resources that could be better used to improve or increase services for families. Existing liquidation and obligation schedules should be redesigned to create a more streamlined system. Currently, states have two years to obligate discretionary funds and an additional year to liquidate those obligations. Mandatory funds must be obligated in one year, but there is no deadline for liquidating funds. Federal matching funds must be obligated in one year and liquidated in two years. The variation in obligation and liquidation schedules between funding streams creates unnecessary administrative work for states. States should be granted a minimum of two years to obligate and two years to liquidate all three sources of funds.

In addition, the current multiple quality set-asides should be consolidated into one set-aside. The streamlined set-aside should require that states address quality for certain populations, such as infants and school-aged children, but should allow states the flexibility to determine the amount of funding dedicated to these populations and the types of activities funded.

Proposal

Preserve CCDF flexibility.

APHSA opposes efforts to limit states' flexibility in using CCDF funds for statewide licensing, health and safety inspections, and other regulatory activities or to direct a percentage of CCDF funds for "direct services."

Explanation

The CCDF is a block grant to states to provide child care services in a manner that best meets the needs of the state's population. Legislation and regulation must maintain the flexibility of the block grant program. The ability of states to use CCDF funding for statewide licensing, health and safety inspections, and other regulatory activities must be preserved. These activities are essential elements of state child care systems that meet the needs of subsidy recipients, as well as other child care consumers. Limiting the use of CCDF funding to licensing and regulating providers that provide care to subsidy families would create an administrative and financial burden and may result in reduced provider options for families. No additional set-asides for direct services should be created.

Proposal

Revise IRS policy to clarify that families, not governmental agencies, are the employers of informal child care providers.

The IRS should clarify that the act of reimbursing a client for amounts the client pays as wages to the client's domestic worker does not cause a governmental agency to become a "control" employer under the IRS code. Parents, not states or municipalities, are the employers of child care providers, unless the state expressly defines it otherwise.

Explanation

Some IRS regional offices have taken the position that informal child care providers may be considered state employees for the purpose of withholding of payroll taxes when the state provides a subsidy for the employment of the provider. Legislation or IRS guidance is needed to clarify that a state is not an employer with respect to payments made by a state for child care services under Title IV of the Social Security Act, regardless of whether the state pays the caregiver directly or pays the child's family. The guidance should specify that the state shall not be considered a caregiver's employer for any purposes, including withholding, reporting, or remitting federal employment taxes, unless the state agrees to act as an agent for purposes of such taxes.

Any policy that allowed informal child care providers to be considered employees of the state would have dire financial consequences for state child care and other programs.

Any policy that allowed informal child care providers to be considered employees of the state would have dire financial consequences for state child care and other programs. State payment of employer taxes for providers would add a significant new cost to child care budgets and require a reduction in the number of families served or in other activities, such as quality improvements. The costs associated with acting as an employer for in-home providers might force the state to limit the number of these providers, therefore threatening consumer choice and access to services. This IRS policy could also set a precedent for the state to be considered the employer for a wide range of other benefits, including unemployment insurance, health insurance, and retirement benefits. In addition, this policy could be used to require the state to act as the employer of other domestic service providers that are hired using federal or state funds, such as personal assistants for the disabled covered by Medicaid.

Proposal

Promote collaboration with other programs to meet child care program goals.

Head Start should fund grantees to provide full-day, full-year services.

Any efforts to coordinate CCDF-funded child care and other federal programs must maintain and respect informed parental choice in the design of these coordinated projects.

State flexibility to use CCDF and TANF funds for early learning programming must be maintained. Federal policy should recognize state investments in developmentally appropriate child care as contributing toward early learning goals.

States' ability to count pre-kindergarten expenditures toward their TANF and CCDF MOE requirements must be preserved.

Explanation

The CCDF and TANF are important sources of funding for child care, but are not the only sources of federal and state funding for child care. Head Start and Early Head Start also provide child care and other services to over 900,000 low-income children, and the 21st CCLC program funds after-school care for many children. Coordination between CCDF and other child care programs at the federal, state, and local levels can help meet the needs of child care consumers. For example, Head Start and Early Head Start grants that offer full-day, full-year services better meet the needs of families and eliminate the complexities of using multiple funding streams to provide full-time child care.

Any efforts to increase collaboration between CCDF and other child care programs must be designed to maintain informed parental choice.

Child care can be an important tool for promoting early learning and school readiness. Federal policies should recognize that quality child care that is developmentally appropriate is an invaluable contribution toward increasing early learning. Any efforts to improve caregiver-child interactions or other fundamental aspects of quality child care are also efforts to enhance early learning. States should have flexibility to use CCDF funds to work toward early learning goals in the manner that best fits the needs of the state.

In addition to providing child care through CCDF vouchers, 40 states funded public pre-kindergarten programs as of 2002. During the 2001–2002 school year, states served 740,000 children at a cost of $2.54 billion. These public preschool programs provide a vital source of child care for low-income families, as well as contribute significantly to school readiness. States' ability to count pre-kindergarten expenditures as part of their CCDF and TANF MOE effort should be preserved.

Proposal

The federal government should expand efforts to improve quality.

The federal government should maintain support for research related to child care quality and the impact of child care programs on workforce participation, economic development, and early learning.

States should maintain broad flexibility to design and implement strategies and activities to achieve CCDF program goals. Specific quality mechanisms and activities should not be federally mandated.

Federal policy should promote quality activities and research across the spectrum of child care settings and providers.

Explanation

Child care is both a critical work support and an opportunity to provide appropriate developmental and educational experiences that enhance the development and well-being of children. States have invested in a wide array of initiatives that address varied aspects of quality, including staff recruitment and retention, facilities improvement, and staff education and training. Types of quality activities include tiered reimbursement, training classes and curriculums, grants for professional development, and consumer education. Because ensuring quality child care is an important function of state child care programs, the majority of states currently spend more than the required 4 percent. States use the set-aside funding and additional CCDF and state funding to provide quality initiatives that best meet the needs of the providers and families in their state. States' flexibility to set their own quality goals and implement selected quality activities must be preserved.

In addition to state expenditures on increasing the quality of direct services, it is vital that the federal government continue to support child care research on quality and the impact of child care programs on workforce participation, economic development, and early learning. National and local studies supported by the federal government increase states' ability to make informed decisions about quality expenditures and goals and provide an important body of knowledge for the child care system as a whole.

States and the federal government must make a commitment to improving the quality of child care across the spectrum of providers. Families should have access to quality child care whether they choose to enroll their child in a day care center or a family child care home, hire an in-home provider, or use a family member to provide care.

PROPOSAL

States support practices that can ensure program integrity yet respect the nature of a block grant and the flexibility states are afforded in the funding of diverse initiatives. Implementation of the IPIA should not result in the establishment of a national child care error rate or other costly mandates.

Any federal initiatives to address program integrity must:

- Maintain state authority to design program integrity strategies;
- Ensure that any new systems or processes established to prevent and measure improper payments do not create an undue burden on families and providers;
- Allow states to focus on the detection of large-scale fraud and abuse, rather than small, unintentional improper payments;
- Focus on prevention, rather than detection;
- Provide additional, dedicated funds for the information technology systems required to establish efficient program integrity systems;
- Ensure that the cost of improper payment initiatives do not exceed the benefits of the initiatives; and
- Allow states to retain 100 percent of any funds recovered.

EXPLANATION

The IPIA requires federal agencies to report an annual national estimate of improper payments in certain federal programs and activities and the actions being taken to reduce these payments. While states support activities and policies aimed at improving program integrity, it is necessary that these activities respect the diversity and flexibility that are inherent in block grant programs such as CCDF. The definition of an improper payment and the methods for measuring errors are state specific and cannot be accurately captured in a national error rate.

Any federal initiatives designed to address program integrity must respect state diversity in program design, regulations, and technology. New initiatives should be accompanied by additional federal funding for technology and should allow states to retain recovered funds as an incentive for strong improper payment systems. States should be allowed to focus on prevention activities and on large-scale fraud, rather than small, unintentional improper payments. This will help ensure that program integrity activities are cost effective. Finally, it is critical that any efforts to prevent or measure improper payments do not unduly burden families or providers.

