SENATE FISCAL AGENCY
ISSUE PAPER

**CHILD CARE AND DEVELOPMENT FUND:
AN OVERVIEW OF THE MICHIGAN PROGRAM AND
THE EXPENDITURE OF FEDERAL AND STATE RESOURCES**

by

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INTRODUCTION

The passage of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), Public Law 104-193, significantly altered child care policy in the United States. The impetus behind the overhaul in child care policy is reflected in PRWORA's emphasis on moving welfare recipients into the workforce. To achieve this goal, lawmakers acknowledged that families had to be provided with adequate child care. In an effort to meet this need, PRWORA repealed the legal authority for three existing child care programs and combined their funds with additional Federal funds to create the Child Care and Development Fund (CCDF), otherwise known as the Child Care and Development Block Grant (CCDBG). This paper examines Michigan's child care program as it relates to the expenditure of Federal and State resources.

MICHIGAN'S TOTAL CHILD CARE PAYMENTS[1]

Since the inception of the CCDF, Michigan's child care expenditures and caseloads have grown dramatically. As indicated in Table 1, between fiscal year (FY) 1997-98 and projected FY 2001-02, Michigan's annual child care payments to providers increased by 144%, from approximately $318.6 million to $458.5 million. Similarly, costs per case and costs per child rose throughout the same period. In FY 1997-98, Michigan spent approximately $463 per case per month, or $261 per child per month. By FY 2001-02, child care payments had reached a projected average of $596 per case per month, or $313 per child per month. Child care caseloads, however, have not followed the same pattern. The number of child care cases, as well as the number of children served, rose until FY 1998-99 when they reached their peak of 66,811 cases or 125,77 children, and since have been steadily falling.

Table 1

Total Child Care Payments, Monthly Caseload Data and Monthly Caseload Costs Fiscal Years 1997-98 – 2001-02*

	FY 1997-98	FY 1998-99	FY 1999-2000	FY 2000-01	FY 2001-02
Total Annual Payments (in millions)	$318.6	$392.7	$418.5	$413.8	$458.5
Average Monthly Number of Cases	56,976	65,247	66,811	65,007	63,864
Average Monthly Number of Children Served	100,904	119,389	125,777	124,061	121,384
Monthly Cost per Case	$463	$498	$519	$529	$596
Monthly Cost per Child	$261	$273	$276	$277	$313

Source: Michigan Family Independence Agency CH-370 reports
*indicates projection based on Family Independence Agency CH-370 reports 10/01 - 07/02

One potential explanation for increased child care costs lies in Michigan's rising employment

[1]Payment data come from Family Independence Agency CH-370 reports.

participation requirements for Family Independence Program (FIP) recipients. Through July 1998, a single-parent FIP client in Michigan was required to work 20 hours per week and one parent in two-parent FIP families was required to work 35 hours per week. After July 1998, single parents were required to work 25 hours a week to remain eligible for FIP. In August 1999, the number of required work hours increased to 30 per week, and in April 2002 the work requirement reached its peak of 40 hours per week for both single-parent families and one parent in two-parent families. The mandated increases in hours of work meant that families also needed more hours of child care, resulting in increased costs.

Increased costs also may be due in part to the Family Independence Agency's (FIA's) Child Development and Care Internet billing system, which was implemented in January 2002. The Internet billing system allows providers to place their billings for FIA reimbursement on the Internet, allowing for more accuracy and giving providers the ability to update and change their billing hours with ease. Because cumbersome paperwork is eliminated, representatives at the FIA speculate that providers actually might be billing the State more accurately for their time, resulting in increased costs.

The Federal government, through both the CCDF block grant and the Temporary Assistance to Needy Families (TANF) block grant, serves as Michigan's primary fund source for child care payments. In order to receive Federal money, Michigan must follow the CCDF's rules and regulations regarding child care programs.

FEDERAL CHILD CARE POLICY

The Child Care and Development Fund has five stated goals:

1. To allow each state maximum flexibility in developing child care programs and policies that best suit the needs of children and parents within the state;
2. To promote parental choice to empower working parents to make their own decisions on the child care that best suits their family's needs;
3. To encourage states to provide consumer education information to help parents make informed choices about child care;
4. To assist states in providing child care to parents trying to achieve independence from public assistance; and
5. To assist states in implementing the health, safety, licensing, and registration standards established in state regulations.

Under CCDF regulations, states are granted enormous flexibility to design child care programs. States have the option to decide their own income eligibility thresholds, up to the Federal maximum of 85% of the state median income (SMI); provider reimbursement rates; parental copayment requirements; education and outreach activities; and whether to offer subsidies in the form of vouchers or provider contracts. In order to qualify for CCDF funds, a child normally must also be under age 13, and the child's parent(s) must be working or participating in an employment and training activity. The CCDF also may be used to subsidize care for children at risk of abuse or neglect or who need child care as a protective service. The Child Care and Development Fund requirements further specify that those payment rates for which assistance is provided must be sufficient to ensure equal access for eligible families as compared with children whose parents are not eligible for assistance.

Child Care and Development Fund money is allocated by the Federal government to the states via three separate funding streams:

1. A mandatory fund;
2. A matching fund; and
3. A discretionary fund.

Both the mandatory and discretionary funds are 100% Federal funds, with no state match required. Mandatory funds are allocated by formula as an entitlement to states, and discretionary funds are determined annually during the Federal appropriations process. States receive matching funds, if they obligate all of their mandatory funds by the end of the fiscal year, spend state-only dollars in an amount equal to the CCDF maintenance of effort (MOE) thresholds, and obligate the Federal and state share of the matching funds within two fiscal years. The state is required to provide funds for CCDF matching funds at the current year Federal Medical Assistance Payment rate. Only state expenditures above the CCDF MOE may be claimed for a Federal match. States' CCDF MOE is based on the greater of FY 1993-94 or FY 1994-95 expenditures. Additionally, states are required to spend at least 4% of CCDF Federal funds and State matching funds to improve the quality and availability of child care. States are prohibited from spending more than 5% of CCDF funds for administrative activities.

In addition to relying on CCDF funds to support child care programs, states may use their TANF dollars. The rationale for allowing TANF dollars to be used to fund child care programs stems from the belief that as cash assistance caseloads began to shrink, states would have to increase their investments in work supports, such as child care. Thus, a state may transfer up to 30% of its current year TANF block grant to the CCDF and up to 10% of its current year TANF block grant to the Title XX of the Social Security Act or Social Services Block Grant (SSBG), provided that the combined total amount of the transfer does not exceed 30% of the state's allocation. For example, if a state elects to transfer 10% of its TANF funds to the SSBG, not more than 20% may be transferred to the CCDF. Once TANF dollars are transferred to the CCDF, they are subject to the CCDF regulations.

A state also may spend TANF funds directly for child care. States do not have to follow CCDF guidelines if they are spending TANF funds directly, although they may choose to do so. When spending TANF directly, it is important to understand the implications of TANF rules in regard to whether the spending will be considered "TANF assistance". Child care spending for a family in which an individual is employed is considered "non-assistance". Child care for a family in which no individual is employed is considered "assistance", unless the child care can be treated as a nonrecurrent, short-term benefit. If a family's subsidy is deemed "assistance", the 60-month Federal TANF time limit, child support enforcement, and data collection requirements apply. Thus, spending TANF dollars directly on day care puts more accountability constraints on recipients who are receiving child care subsidies as "assistance".

Choosing to transfer TANF dollars to the CCDF, spend TANF dollars directly for child care, or do some combination of the two has no monetary impact on state child care revenues or expenditures. Many states find that transferring TANF funds to the CCDF has the advantage of expanding access and improving the quality of child care. For example, 4% of CCDF funds must be directed toward quality improvement; thus, transferring TANF funds to the CCDF automatically raises the amount of money that must be spent on quality improvement. Choosing to spend TANF dollars directly on child care also has advantages, however. Spending TANF funds directly gives access to additional funds for child care after maximizing the ability to transfer to the CCDF. Spending TANF directly also may be more convenient for financing some specific initiatives that are more easily funded with TANF funds than with CCDF funds.

MICHIGAN'S CHILD CARE POLICY

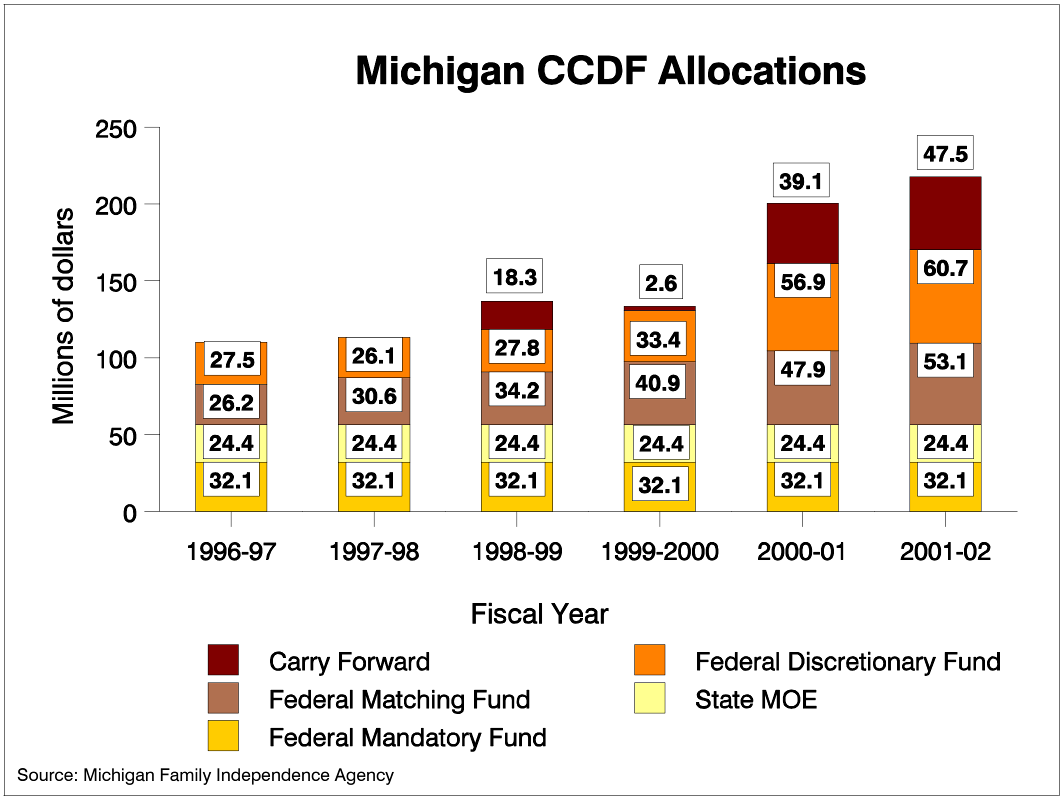
As mentioned above, each state must design its own plan to allocate the CCDF grant. Michigan set its maximum income eligibility requirement at approximately 185% of the Federal Poverty Income Guideline, or $31,038 for a family of four in FY 2001-02. Eligible families must require child care because of employment, approved education, or an approved family preservation activity for a health or social condition for which treatment is being received.

In order to meet the Federal CCDF rule that mandates equal access to child care for low-income families, Michigan has formulated a provider rate reimbursement scale by region. In order to determine reimbursement rates, the State completed a market rate survey in April 1999 and set payment rates at the 75th percentile of the local market rate. Capping payment rates at the 75th percentile means that the maximum rate paid by the State will not exceed the price charged by at least 75% of the providers in a particular category of care and region.

Michigan's sliding fee scale for family contributions to the cost of child care also helps ensure that low-income families have equal access to child care. Michigan's copayment rates vary according to the income and the size of the family. For example, for a family of four that earns $2,000 per month, the State will pay 95% of child care costs. For a family of four that earns $2,500 per month, the State will pay 40% of the family's child care costs. According to the State Plan for Michigan Child Care and Development Fund Services, Michigan's child care program currently serves all eligible applicants with priority given to very low-income families and children with special needs. Michigan does not give priority status to families that have recently left the Family Independence Program, but rather uses income as a determinant regardless of FIP status. Michigan adopted this policy so that families would not have an incentive to apply for cash assistance in order to receive child care subsidies.

Michigan carries out its child care program using Child Care and Development Fund dollars, as well as TANF dollars. Michigan's CCDF allocation has grown every year since the block grant's inception. As shown in Figure 1, in FY 1996-97, Michigan received $58.9 million in Federal CCDF allocations. By FY 2001-02, that number had increased to $145.9 million. Annually, Michigan receives $32.1 million in Federal mandatory funds and meets its maintenance of effort requirement of $24.4 million. Over the period between FY 1996-97 and FY 2001-02, Federal matching funds have more than doubled from $26.2 million to $53.1 million.

Figure 1

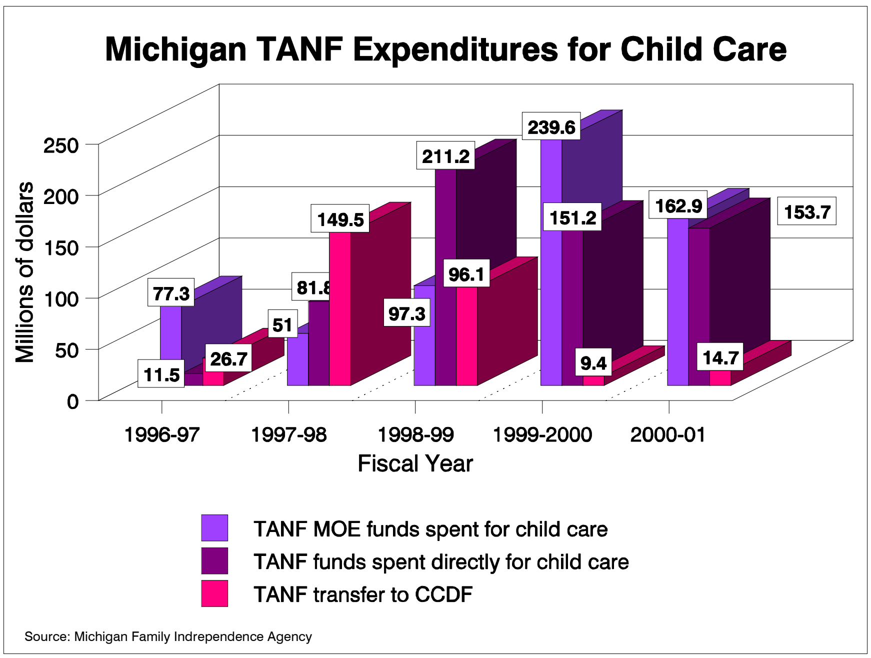


Federal discretionary funds allocated to Michigan also have grown dramatically in the last six years, from $27.5 million in FY 1996-97 to $60.7 million in FY 2001-02. Beginning in FY 1998-99, Michigan legislators earmarked a portion of the discretionary fund for child care resource and referral and school-age child care activities. In FY 1999-2000, legislators earmarked additional discretionary funds for quality improvement activities and infant and toddler care. Despite setting aside these funds for specific programs, Michigan still had $52.1 million in discretionary funds available after the earmarks in FY 2001-02. The increase in discretionary funds not only has provided more child care revenue for Michigan, but along with TANF dollars, also has allowed the State to initiate innovative programs, such as the Infant/Toddler Incentive program that encourages more child care providers to care for infants and toddlers by increasing the provider reimbursement rate for children under 30 months old.

In addition, Michigan has had carry forward funds available since FY 1998-99. Under CCDF regulations, all mandatory funds must be obligated within the fiscal year. States have two years to obligate matching funds and discretionary funds, however. Michigan's carry forward funds have been steadily growing except in FY 1999-2000. The decline in availability of carry forward funds during that year is explained by Michigan's choice not to use a $33.4 million allocation of Federal matching funds during FY 1998-99. These funds were returned to the Federal government and redistributed to other states. As a result, fewer funds were available to carry forward in FY 1999-2000. Michigan spent a total of $404.6 million of TANF funds on child care in FY 1999-2000, the highest amount between FY 1997-98 and FY 2001-02.

As noted above, Michigan chooses to use TANF dollars in addition to CCDF funds, to fund child care. Michigan uses its TANF block grant to fund child care both by transferring TANF funds to the CCDF and through spending TANF dollars directly. As depicted in Figure 2, during the five-year period between FY 1996-97 and FY 2000-01, Michigan transferred to the CCDF approximately 10.7% of its TANF money, or $296.2 million. Michigan spent approximately $609.4 million directly in TANF funds for child care, 22% of its total TANF block grant expenditures. Michigan also spent State TANF maintenance of effort funds on child care. During the five-year TANF program period between FY 1996-97 and FY 2000-01, Michigan spent approximately 25.7% of its TANF MOE obligation on child care assistance, totaling $628.2 million. The dollars spent as TANF MOE are in addition to funds spent to meet CCDF MOE requirements.

Figure 2

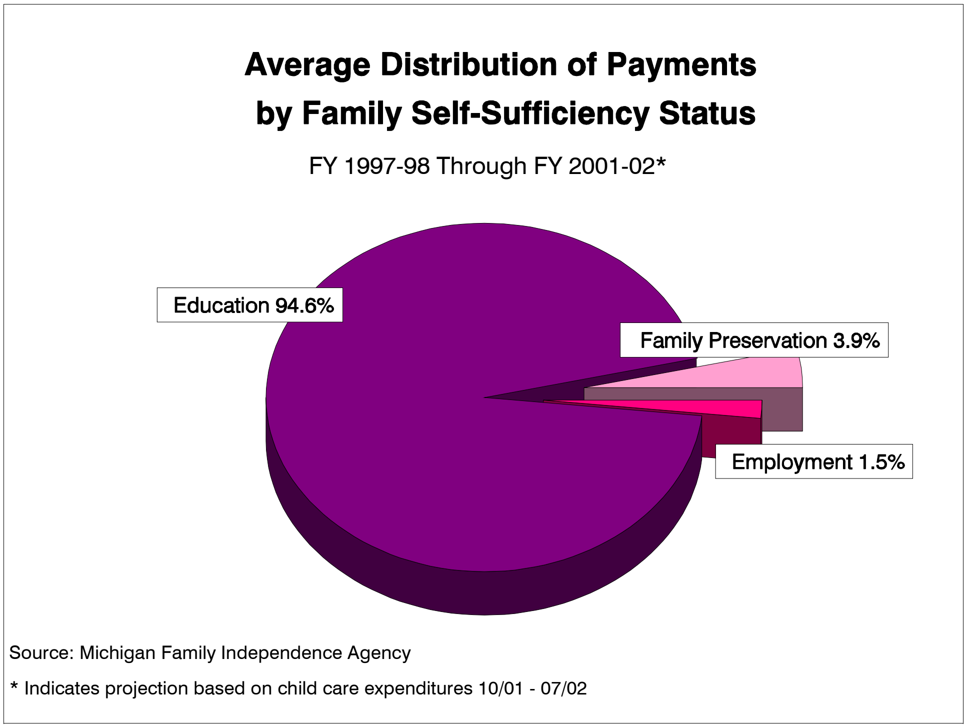


DISTRIBUTION OF MICHIGAN'S CHILD CARE PAYMENTS

As shown in Figure 3, between FY 1997-98 and projected FY 2001-02, approximately 94.6% of Michigan's child care payments--an average of $368.1 million per year--went to fund families whose self-sufficiency qualification category allowed them to receive child care subsidies because at least one parent was employed. Approximately 3.9% of payments were directed at families whose self-sufficiency qualification was a result of educational pursuits, and the remaining 1.5% of payments were spent on families that qualified under the family preservation[2] self-sufficiency eligibility category.

[2]The family preservation eligibility category includes protective services, preventative services, and foster care.

Figure 3



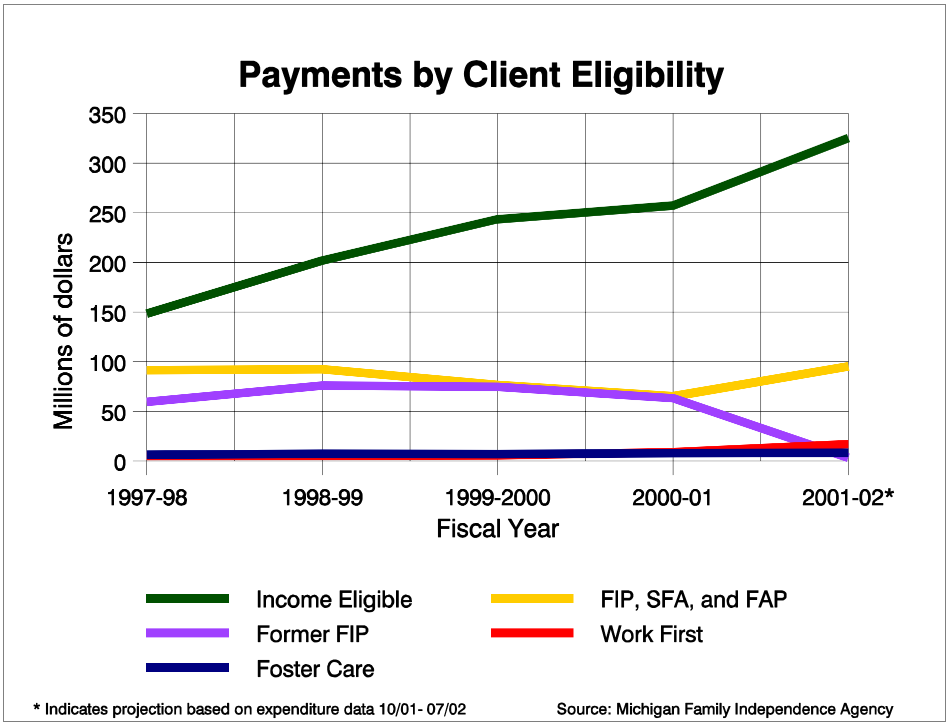
The three broad self-sufficiency categories by which families may qualify to receive child care subsidies are further broken down into specific eligibility groupings. For example, a family that qualifies for child care subsidies under the "employment" category, may be eligible for aid as a result of their income, Work First participation, or FIP status. Between FY 1997-98 and projected FY 2001-02, an average of 58.8% of Michigan's child care payments went to subsidize families that qualified to receive day care subsidies because they were classified as "income eligible", meaning their monthly income was less than Michigan's maximum income eligibility of $33,845. Another 21.1% of child care payments were directed toward FIP, State Family Assistance (SFA), and Food Assistance Program (FAP) (formerly Food Stamp) recipients. Former FIP recipients accounted for the third largest payments group between FY 1997-98 and FY 2001-02 with 13.9% of payments going to support those families. Work First recipients, ineligible grantees[3], foster families, migrant families, families pursuing higher education under a plan approved by the Michigan Works Agency, and families involved with protective or preventative services account for the remainder of those eligible for child care subsidies.

As shown in Figure 4, the number of families receiving child care subsidies as a result of their FIP, SFA, or FAP status declined between FY 1998-99 and FY 2000-01, reflecting similar declines in those programs' caseloads. As the economy faltered in FY 2001-02 and FIP, SFA, and FAP caseloads began to climb again, so too did the numbers of those receiving child care

[3]Ineligible grantees are relative caregivers who are not official foster care home providers, but still require some assistance to provide for the children in their care.

subsidies as a result of their enrollment in cash grant programs. At the same time, the number of low-income families receiving "income eligible" subsidies increased from an average of 27,894 child care cases per month in FY 1997-98 to a projected 46,174 cases per month in FY 2001-02 and is expected to continue growing. The "income eligible" category of child care subsidy recipients experienced especially dramatic increases between FY 2000-01 and FY 2001-02 mostly because the "Former FIP" category is being phased out.

Figure 4

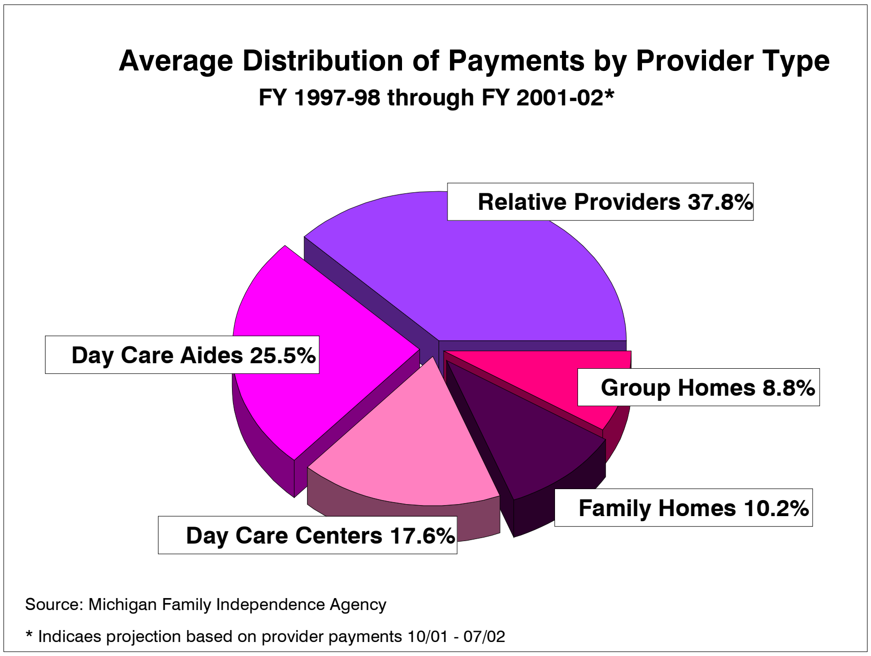


Michigan recognizes five categories of child care providers from which those families that are eligible to receive child care subsidies may choose:

1. Child day care centers, licensed by the Department of Consumer and Industry Services (DCIS);
2. Family homes, registered by the DCIS to care for up to six children;
3. Group homes, licensed by the DCIS to provide care for up to 12 children;
4. Relative homes, which require relative providers to meet enrollment requirements, including a background check, in order to receive payment; and
5. Day care aides, which are defined as relative or nonrelative caretakers providing care in the child's home. Day care aides must meet enrollment requirements to receive payment.

Relative homes provide child care for the greatest number of Michigan children, and the number of families relying on relative providers has increased continually. As shown in Figure 5, between FY 1997-98 and projected FY 2001-02, approximately 37.8% of Michigan's child care payments were paid to relative homes, amounting to an average of $151.4 million annually. Day care aides receive approximately 25.5% of Michigan's payments, and day care centers, family homes, and group homes receive the remainder. In total, between FY 1997-98 and projected FY 2001-02, relative homes provided care for an average of 40,871 children per month. Day care aides cared for 35,940 children per month, and day care centers, family homes, and group homes, cared for 19,238, 12,113, and 10,140 children per month, respectively.

Figure 5



Not only do relative homes provide care to the largest number of children in the State, but they also provide the most hours of care. As shown in Table 2, for example, relatives provided 8.1 million hours of child care, more care than child day care centers, family homes, group homes, or day care aides. The greater number of hours of care leads to higher cost per child rates, averaging $306 per child per month between FY 1997-98 and projected FY 2001-02 for relative providers. Over the same period, day care aides proved to be the least costly form of care per child, averaging just $235 per child per month as well as providing fewer hours of care than their relative counterparts.

Table 2

Hours, Costs and Cost per Hour of Child Care by Provider December 2001			
Type of Provider	**Hours of Care**	**Costs**	**Cost per Hour**
Day Care Centers	2,961,331	$6,919,858	$2.34
Family Homes	1,592,659	$3,240,626	$2.03
Group Homes	1,796,529	$3,729,777	$2.08
Relative Providers	8,080,547	$14,927,532	$1.85
Day Care Aides	6,663,241	$9,504,662	$1.43

Source: Michigan Family Independence Agency

FEDERAL REAUTHORIZATION

Like PRWORA, the Child Care Development Fund will need to be reauthorized before September 30, 2002. As the reauthorization date nears, a number of key U.S. Senate, House, and Administration bills and proposals have been put forth. The following outlines the significant provisions of the pending Federal legislation.

Good Start, Grow Smart, the Bush Administration's proposed FY 2002-03 Early Education Initiative, maintains CCDF funding at its current level of $4.8 billion per year, and increases the percentage of state CCDF matching funds that may be applied from state expenditures from 20% to 30%. Under the Bush plan, eligibility requirements, provider payment rate provisions, and quality standards remain the same. *Good Start, Grow Smart* does require states to identify a set of quality criteria and guidelines in alignment with Federal K-12 education standards.

The proposed Personal Responsibility, Work and Family Promotion Act of 2002, the final House version of H.R. 4737, increases the CCDF matching fund by $1 billion over five years, and authorizes the appropriation of up to $3 billion in additional discretionary funds in the next five years. The House bill also increases the minimum 4% quality set-aside to 6% and eliminates the Federal maximum eligibility level of 85% of state median income, replacing it with a provision that allows states to set income levels.

Three bills regarding child care also are currently being debated by U.S. Senate committees: the Children First Act of 2002 (S. 2070); Access to High Quality Child Care Act (S. 2117); and Early Care and Education Act (S. 2566). The Children First Act would authorize an increase of $11.25 billion in matching funds over the next five years. The Access to High Quality Child Care Act would change current CCDF discretionary funding authorization to "such sums necessary for each of the fiscal years 2003 to 2007". Finally, the Early Care and Education Act would create a new authorization separate from CCDF for $1 billion of discretionary funding for 2003 and "such sums as may be necessary" for fiscal years 2003-

04 through 2007-08.

Each of these proposals will result in increased CCDF allocations, which will inevitably benefit Michigan. Funding increases are especially welcome considering that Michigan has steadily been spending more than its annual TANF block grant, because in addition to the State's basic block grant, a balance of carry forward funds has been available. Since it is unsure whether the State will have TANF funds available beyond its basic grant in the future, Michigan may have a difficult time supporting the level of TANF spending on child care that it has done in the past. In an effort to address this concern, Michigan is reorganizing spending, cutting back and eliminating some programs, and changing funding sources. In FY 2002-03, for example, Michigan plans to use more CCDF funds and transfer more State General Fund money to the Day Care Services line than it had in any previous fiscal year for the explicit purpose of saving TANF funds. These concerns about a shortage of TANF funds arise even as child care costs continue to escalate and show no sign of leveling. Any Federal increases in CCDF allocations would therefore go a long way in helping Michigan maintain the child care services it has been providing to low-income residents.

SUMMARY

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 has successfully moved large numbers of former welfare recipients into the workforce. With this shift has come an increased need for child care among low-income families. As the number of families needing child care continues to grow and the cost of child care continues to rise, both national and state legislatures will have to devise creative, high-quality and cost-effective ways to care for children while their parents work to achieve self-sufficiency.