Child Care Investment Increasing

ABSTRACT: This article focuses on two child care assistance programs and summarizes major provisions of these programs affecting accessibility and affordability of state subsidized child care for low-to-moderate income families. State and federal funding and strategies for financing the projected growth in child care expenditures also are discussed in this paper.

Introduction

State subsidized child care assistance programs enable low and moderate-income families to participate in employment, educational and training programs. The Department of Children, Families and Learning (“DCFL”) administers two major cash assistance child care programs: Basic Sliding Fee (BSF) child care and Aid For Families with Dependent Children (AFDC)/Temporary Assistance for the Needy Families (TANF) child care. Effective July 1, 1997, the AFDC/TANF program transitions from being an entitlement program to a fully funded program, called the Minnesota Family Investment Program (MFIP-S) in which the state will reimburse counties for the total number of families provided cash assistance for child care. Unlike the MFIP-S program, the BSF program allocation is capped at a certain level that may or may not allow services to be provided to all eligible families. Counties may only be able to serve a limited number of families based on their total BSF allocation.

During the 1997 Legislative session, the Family and Early Childhood Education Finance Committee had MFIP-S and BSF child care within its purview. In the Family and Early Childhood Education Omnibus Act, (Laws 1997, Chapter 162) child care assistance general fund expenditures rose 130 percent in the FY 1998-99 biennium, compared to the FY 96-97 biennium, increasing the state’s overall investment in child care. Using FY98 net non dedicated revenue projections, it is estimated that for every $100 of tax revenue spent by the state, approximately 84 cents will be spent on child care assistance.¹

¹ For this calculation, FY 1998 expenditures for Basic Sliding Fee Child Care and TANF child care were used along with the total amount of net, non dedicated revenue projected in the Consolidated Fund Statement, Department of Finance, September 1997. State expenditures for Dependent Care Tax Credits or Child Care Grants at Post Secondary Institutions were not included in this calculation.
Background

Minnesota is eligible to receive a federal block grant for child care called the Child Care and Development Fund (CC&DF) through FY 2002. The CC&DF has three components: discretionary, mandatory, and matching funds. There are separate requirements for each component of the CC&DF that Minnesota must meet annually through FY 2002 in order to receive the available funding. These requirements are as follows:

- **CC&DF discretionary funds** require no maintenance of effort (MOE) by the state. In other words, the state does not need to appropriate any funds to receive and spend these federal dollars.

- **CC&DF mandatory funds** require no MOE as long as the state meets its TANF block grant MOE requirements.

- **CC&DF matching funds** are available to Minnesota if the following conditions are met: (1) the state must annually appropriate $19.7 million, which is equal to federal FY 95 spending on AFDC related child care, as a MOE for the CC&DF block grant through FY 02; and, (2) state expenditures above the MOE will then be matched with additional federal funds of up to $14.4 million in FY98.

Total CC&DF funding is not expected to increase or rise with inflation. Instead, the real value of the block grant will shrink over time. CC&DF funding may only increase if the state continues to appropriate sufficient state dollars to meet MOE and matching requirements. Conversely, funding may decrease if the state does not appropriate sufficient dollars.

Since the state appropriated an amount above the FY 1995 base and enough to meet all matching requirements, Minnesota will be able to draw down the maximum amount of federal funding available (approximately $52 million) in FY 1998. CC&DF funds may be used for MFIP-S child care, BSF child care, child care development and child care administrative expenditures. Minnesota is not the only state to try to maximize the total federal funds available. There are approximately 20 states nationwide also planning to appropriate state dollars beyond the amount they are required to spend to access “new” federal funds. The amount of matching funds that will be available to Minnesota may increase if other states do not access the full amount of funding available to them. Minnesota may receive an

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increase in the amount of matching funds available to them because federal law governing this block grant includes a reallocation provision for any money not disbursed within the original funding cycle.

**Making MFIP-S Child Care “Accessible and Affordable”**

MFIP-S child care state expenditures will be driven up by the new work requirements created by welfare reform or the federal Personal Responsibility and Work Opportunity Reconciliation Act (P.L. 104-193). Welfare recipients will be required to go to work to continue to receive assistance. MFIP-S child care needs to be accessible and affordable to families to enable them to work. During the 1997 session, several provisions were changed which govern child care assistance. State appropriations also increased significantly during the 1997 session. Table 1 shows how state and federal MFIP-S expenditures are expected to increase in the FY 1998-99 biennium compared to the 1996-97 biennium.

<table>
<thead>
<tr>
<th>Table 1. MFIP-S Child Care Appropriations</th>
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<tr>
<td>Source</td>
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<tr>
<td>State</td>
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<tr>
<td>Federal</td>
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<tr>
<td>TOTAL</td>
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**Eligibility**

Families eligible for MFIP-S child care, in general, include AFDC, MFIP, MFIP-R, MFIP-S recipients who are employed, searching for employment or participating in activities from an approved employment plan. Beginning July 1, 1998, all employed families without an employment plan will be required to work at least an average of 20 hours per week. MFIP-S families with one or more children under age one, however, are exempt from MFIP-S work requirements.

There are no time limit requirements attached to MFIP-S child care in statute. MFIP-S families receiving TANF block grant benefits, however, are only eligible to receive these benefits for up to five years. This provision indirectly limits the number of years that MFIP-S families may receive MFIP-S child care.

**Copayment**

No copayment is required for TANF child care participants with incomes below 75 percent of the federal poverty level. Between 75 percent and 100 percent of the federal poverty level, TANF recipients will be required to pay a monthly copayment of $5 starting January 1, 1998. TANF recipients with incomes above 100 percent of poverty level will make copayments, based on income and family size, as identified in the state child care BSF schedule.

**Estimated Number of Families Served**

DCFL estimates that an average of approximately 11,700 families will be served per quarter in FY98, or approximately 4,000 more families than last year, at an average annual cost of $4,725 per family.

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3 Bulletin, Minnesota Department of Children, Families and Learning, June 19, 1997, p.6

4 DCFL collects child care data on a quarterly basis and collects data on the number of families participating in the program as opposed to the number of children participating in the program. For analytical purposes, there are approximately 1.3 (continued...)
4 (...continued)

children per family.
Allocation of State and Federal MFIP-S to Counties

MFIP-S child care funding is not distributed to counties based on a formula. Instead, counties receive retrospective payments from the state as reimbursement for MFIP-S expenditures.

Discussion

MFIP-S child care is primarily financed with state general fund appropriations and federal CC&DF funds. In FY 1998-99, state general fund expenditures for MFIP-S child care will increase by more than 130 percent. By the FY 2000-01 biennium, MFIP-S expenditures are projected to increase another 74 percent. One possible way to finance some of the projected growth in MFIP-S child care expenditures, aside from another general fund appropriation, is to access TANF block grant funds or require private sector participation in financing child care.

States are allowed to transfer up to 30 percent of the TANF block grant to CC&DF. Approximately 12 states, including Florida, Wisconsin, Oregon and North Carolina are transferring some, if not all, of the amount allowable in their TANF block grant to CC&DF for child care expenditures. Currently, Minnesota is not using any of its TANF block grant allocation for child care.

Minnesota’s TANF block grant is $297 million in FY98 and $288 million in FY99. The TANF block grant is currently being spent on Minnesota Family Investment Plan (MFIP) cash grants, work grants, MFIP-S and county and state level administration. Of this block grant, approximately $43 million or 14 percent of the total block grant has not been spent in FY98. A similar portion of the FY99 block grant has also not been allocated. These unspent funds may be transferred to MFIP-S child care to help finance the projected growth in child care expenditures over the next few years.

Another option is to strongly encourage private sector financial participation in child care. Financial and non-financial incentives need to be created so that the private sector may subsidize a portion of the total cost of child care for its employees living near the federal poverty level. The State of Colorado established a Business Commission...
on Child Care Finance in 1995 to propose solutions to their child care crisis. To date, this commission has focused on creating tax incentives and changing zoning requirements to expand the supply of child care.

Making Basic Sliding Fee (BSF) Child Care “Accessible and Affordable”

Welfare reform will indirectly influence BSF expenditures. As more welfare families begin to work and as their incomes increase, they will be transitioning off of MFIP-S child care and into the BSF child care program. With a capped appropriation, BSF Child Care will serve families with low to moderate incomes. Table 2 shows how state and federal BSF appropriations have increased since the 1996-1997 biennium.

<table>
<thead>
<tr>
<th>Source</th>
<th>FY 96-97</th>
<th>FY 1998-99</th>
<th>Change</th>
<th>Percent Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>State</td>
<td>$40.2 million</td>
<td>$92.4 million</td>
<td>$52.2 million</td>
<td>130%</td>
</tr>
<tr>
<td>Federal</td>
<td>$33.0 million</td>
<td>$33.4 million</td>
<td>$.4 million</td>
<td>1.2%</td>
</tr>
<tr>
<td>TOTAL</td>
<td>$73.2 million</td>
<td>$125.8 million</td>
<td>$52.6 million</td>
<td>72%</td>
</tr>
</tbody>
</table>

Eligibility

Families eligible for BSF child care must not be on MFIP-S child care and must be working and have an income that does not exceed 75 percent of the state median income (or approximately 250 percent of the federal poverty level). BSF child care may also be authorized for families in support of a job search for up to 240 hours per calendar year. Students in good academic standing are also eligible for Basic Sliding Fee for the duration of the time necessary to complete their credit requirements for an associate or baccalaureate degree.

Copayment

Copayments are required and are calculated as a percent of a family’s income and adjusted for family size. Administrative rules for child care set the maximum percentage of household copayment contribution at 17.2 percent. In 1997, the Minnesota Legislature approved a provision that would require, beginning January 1998, that households between 75 percent and 100 percent of the poverty level pay a $5.00 co-payment. The Legislature also included another provision that copayments for households at or above the poverty level must not decrease due to the addition of family members after the family’s initial eligibility determination.

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Allocation of BSF funding to counties

In every calendar year, each county is guaranteed funding equal to 90 percent of the allocation received in the preceding calendar year. From January 1, 1999 to December 31, 1999 each county’s guaranteed floor must be equal the original calendar 1998 allocation or its actual earnings, which ever is less. Any remaining BSF funds are allocated according to the following formula:

- one-third of the funds are allocated in proportion to each county’s total expenditures for the BSF program reported during the most recent calendar year to the total expenditures for the BSF program for all counties during the most recent calendar year;

- one-third of the funds are allocated based on the number of children under age 13 in each county who are enrolled in general assistance medical care, medical assistance, and MinnesotaCare on December 31, and;

- one-third of the funds are allocated based on the number of children under age 13 who reside in the county.

This formula is in place to assure an equitable distribution of BSF funds to counties based on past demonstrated need. Since state funding for BSF child care assistance increased significantly during the 1998-99 biennium, a temporary formula allocation has been put in place to distribute calendar year 1998 and 1999 allocations. The temporary allocation formula is intended to distribute new funds to counties with waiting lists.

Estimated Number of Families Served

Approximately 13,100 families will be served by BSF per quarter in FY98, or 3,000 more families than last year, at an average annual cost of $4,450 per family. The annual cost per family for BSF is slightly lower than the MFIP-S program because copayments contributed by families help offset the total average cost of the program. BSF copayment contributions also generate additional funding to provide services to more eligible families.

A provision passed in the 1997 Family and Early Childhood Omnibus Act is making it easier for families who are participating in the BSF program to continue receiving care when they move to another county. Before this provision was enacted, families were at risk of losing their basic sliding fee child care if they moved to another county with a long waiting list for the program. Starting July 1, 1997, DCFL will establish a portability pool of up to 5 percent of the annual BSF appropriation to provide continuous child care for eligible families who move between counties. When an eligible family moves to another county their basic sliding fee program expenses will be covered under the unitary residency act for two months. During this time, they must apply in the new county for services. After two months, the receiving county, must either accept administrative responsibility for the family or, if they
have a waiting list, claim funding for assistance to the family through the portability pool for up to six months. This provision is expected to improve program accessibility for families in transition.

**Discussion**

Some counties participating in the BSF program, mostly in the metro area, must develop a waiting list because demand for services exceeds the amount of funding available. To reduce these waiting lists without allocating more general fund dollars, the state could consider several options.

First, limiting eligibility to 65 percent of state median income or 200 percent of the federal poverty level. The income eligibility limit under current law is 75 percent of state median income. The savings earned from reducing the income eligibility for BSF could be used to serve more families with greater financial need and less resources.

Second, limit the number of years that families will be eligible for BSF. In 1996, the average time on BSF assistance was almost three years. Under current law, there is no eligibility time limit and this gives families no incentive to transition off the program. Instead, families may remain in the program for several years which is problematic because the BSF program is a capped appropriation. Since few families leave the BSF program, an additional appropriation would be needed to expand services to newly eligible families.

Another option to consider is Wrap Around Child Care. Some counties and community action agencies have become more creative and have tried to stretch their state general fund dollars. Wrap Around child care consists of a half day of BSF child care and a half day of Head Start. Unlike BSF child care, Head Start is administered by Community Action Agencies and offers a comprehensive program to meet the social, emotional, health, and psychological needs of low-income children and their parents. Both Head Start and BSF receive federal funds. The total average annual cost of BSF is $4,450 and for full day Head Start it is $8,537 in 1998. If BSF funds are limited and if Head Start funds are available, Wrap Around Child Care is a good way to maximize the resources of each program.

**Other Child Care Subsidy Programs**

**Child Care Diversion**

Up to $500,000 is available to DCFL to establish a one year grant program for assistance to AFDC/TANF/MFIP-S participants and their expenses related to the costs of education, training or transportation. At this time, DCFL does not have an estimate of the projected numbers of families who might be served by this program.

**At-Home Care**

Up to 7 percent of the BSF annual allocation, which equals $2.9 million in FY98, is available to DCFL to establish an At-Home Child Care program for families with infants eligible for the BSF program and not receiving MFIP-S. This program will provide cash assistance to parents staying home with their infants under 12 months of age. Parents providing child care will be paid an amount equivalent to 75 percent of the family child care market rate, minus any required copayment. The implementation date of At-Home Care is July 1, 1998. During the first year of implementation, an estimated 700 families will make use of this program.

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Cherie Kotilnek, Child Care Assistance, Department of Children, Families, and Learning, 1997.
Dependent Care Tax Credits

Minnesota allows low to moderate income families to claim a child and dependent care tax credits against personal income taxes owed to the state. Unlike the federal credit, the Minnesota credit is refundable, meaning that taxpayers who owe no state income tax may claim the credit as a refund. Families with an income at or below $30,150 are eligible for this program if they: (1) paid someone to care for their child under age 13 (or a disabled dependent) so the taxpayer can work or seek work; or, (2) operated a licensed family day care home while caring for their own child under 7 years of age; or, (3) regardless of child care expenses, had a newborn infant during the tax year. The maximum amount a family may claim as a credit for one child is $720 and $1,440 for two or more children. For tax year 1996, the dependent care tax credit was claimed by 36,270 filers. The average dependent care tax credit in 1996 was $327 per filer for a total cost of approximately $11.8 million.

Dependent Care Pre-Tax Accounts

Minnesota (by conforming to federal tax law), allows parents to direct up to $5,000 of their pre-tax wages to an employer-sponsored account, which is used to pay for dependent child care expenses for their child under age 13. No income limits apply. These accounts are advantageous to employees whose child care costs are paid from income that is exempt from federal and state income and payroll (Social Security and Medicare) taxes. The employer benefits by saving the cost of the “employer match” (7.65 percent) to the federal payroll taxes. The worker or family decides each year how much to have withheld for child care expenses and submits bills to the account administrator at work, who pays the care provider. Nationally, roughly half of private and government employers with more than 100 workers offer this benefit, but less than 15 percent of smaller employers do so. The annual state tax expenditure for pre-tax dependent care accounts is variously estimated to be between $5 million and $8 million per year.

Choosing between tax benefits. Generally, where an employee can choose between these tax programs, taxpayers with gross incomes over $25,000 per year and those with income in the dependent care credit phase-out range are better off using a pre-tax account. Taxpayers with incomes less than $20,000 usually receive greater tax benefits from the refundable state dependent care credit, according to House Research analysis published in 1996. Some taxpayers can use both tax benefits. The dependent care credit, however, only applies to qualifying expenses over and above the amounts paid for child care from a pre-tax account.

Child Care Grants at Public/Private Post Secondary Institutions

Public and private post-secondary institutions participating in the state financial aid program may access grants for child care. Undergraduate students with children under age 12 may apply for this grant if they are in good academic standing, enrolled at least half time and are not participating in MFIP-S or BSF child care. The maximum annual per child grant is $2,000. A student may be eligible for this grant program for up to four years of enrollment. The total FY 1998-99 appropriation is $9.48 million.

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9 . . . of household income in 1996. The income eligibility ceiling is indexed for inflation and adjusted annually.
10 Source: Data from the Department of Revenue, Research Department, August 1997.
11 Source: Dependent Care Pre-Tax Accounts, House Research Department Information Brief, revised July 1996.
Infant Care Pilot Project at State Colleges

The Higher Education Omnibus Act (Laws of 1997, Chapter 183, Article 1, Section, Subd. 3) allocated $150,000 in FY 1998 to expand child care offerings to include infant care at one community college, one technical college, and one consolidated technical college. A campus will be selected for this pilot based on the following criteria: (1) it has an exemplary child care program, (2) there is demand for infant care on campus, and (3) it has the physical and financial capacity to sustain an infant care program after the pilot has expired. An evaluation of the performance of these pilot projects and recommendations on expanding infant care to other campuses will be reported to the Legislature by the Board of Trustees of the Minnesota State Colleges and Universities System during the FY 2000-01 biennial budget request.

Conclusion

State subsidized child care is available in several different forms to support families participating in employment and/or education. In the future, the state may need to review with the relationship between MFIP-S and BSF child care as welfare reform becomes fully implemented. Currently, MFIP-S is a fully funded program and BSF child care is a capped allocation.

These fiscal structures may be problematic because as the number of families participating in MFIP-S child care increase, expenditures for MFIP-S will also increase. Eventually MFIP-S families’ income will rise and will need to transition off of MFIP-S child care and onto BSF child care. Since BSF is capped allocation, these families transitioning off MFIP-S may not be able to access BSF child care. In the event that such a scenario comes true, the state would need develop ways to make these programs’ fiscal structures more complementary so that these programs will be equipped to handle major changes in enrollment from year to year without having to delegate families to child care assistance waiting lists.

During the 1997 session, a reserve account was created (Laws of 1997, Chapter 162, Article 4, Section 24) for any unexpended BSF, MFIP-S and other child care funds. Any unexpended funds during the biennium are to be deposited into the reserve account and these funds may be reallocated by the Commissioner. This reserve account may be a one vehicle for shifting funds between MFIP-S child care and BSF child care if there are changes in enrollment from year to year.

In addition to assuring that MFIP-S child care and BSF child care are made accessible and affordable to families, another key aspect of child care assistance that has not been discussed in this article is quality. The supply of quality child care is influenced by such variables as reimbursement rates, provider training programs and resource and referral programs. These issues and others will need to be addressed during the 1998 session to ensure that the state maximizes its increased investment in child care in both the short and long run.

For more information about state funding for child care, contact: Cynthia Coronado at 296-5384.
M. J. Hedstrom (296-1237) contributed to the tax section and publication of this paper.