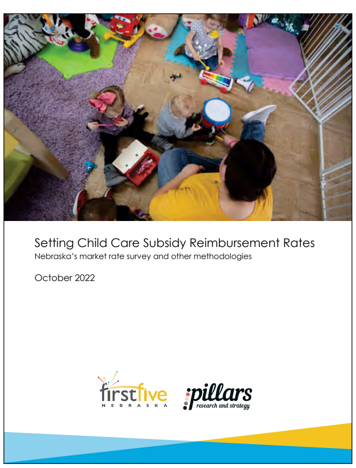
LR378: Child Care Subsidy Reimbursement Rates

POLICY BRIEF | OCTOBER 2022

Developed in collaboration with Pillars Research and Strategy

Nebraska's process for setting child care subsidy reimbursement rates directly influences the viability of our state's early childhood programs and the working families who depend upon them.

We must ensure our process for setting reimbursement rates reflects the changing economic realities faced by child care providers and this critically important industry as a whole.



Access the full report, *Setting Child Care Subsidy Reimbursement Rates*, at FirstFiveNebraska.org

Key Points

- Like other states, Nebraska uses a market rate survey to determine how much a child care provider will be reimbursed for serving children who qualify for the child care subsidy. Reimbursement rates are affected by children's age, program type, program quality and location.
- The market rate system for setting subsidy reimbursements does not reflect the true cost of delivering quality child care, even for families who pay for child care services privately. Because state statute prevents providers from claiming subsidy reimbursements above what they can realistically charge for private pay, it severely undercuts the financial viability of child care programs.
- There are alternative methods for setting subsidy reimbursements that combine market rate data with other factors that can make participation in the child care subsidy program more feasible for Nebraska's providers.

Introduction

The child care industry boosts economic growth, supporting $99.3 billion in U.S. output annually. Access to care promotes productivity, increases revenue, attracts diverse talent pools, reduces turnover and creates employment opportunities. We also know that high-quality child care is a strategic long-term investment, supporting strong child development and a powerful workforce of the future.

In Nebraska, insufficient child care options resulted in significant losses to household income, business revenue and Nebraska tax revenues. Altogether, these totalled nearly $745 million in direct losses annually prior to the global pandemic. Child care subsidies help low-income parents access child care, allowing them to participate in the workforce, pursue an education, earn higher wages and provide stability to support healthy child development. The child care industry plays a key role in propping up Nebraska's economy. The state has an opportunity to ensure the industry is stronger than ever.

Background

The Child Care and Development Block Grant is a federal program that provides funding to states for child care subsidies for low-income families. States use this pot of money—called the Child Care and Development Fund (CCDF)—to subsidize child care for eligible families. States determine provider reimbursement rates and have broad latitude in doing so. Federal legislation encourages states to set reimbursement rates high enough that child care providers are willing to accept CCDF subsidies so that, ideally, eligible children have equal access to care as children whose families pay privately.

LB1011

Nebraska's child care reimbursement rates increased from the 60th to the 75th percentile with passage of LB1011 in 2022. The increase is paid for through the Federal Child Care and Development Block Grant (CCDBG), supplemented by Temporary Assistance for Needy Families (TANF) program funds, if necessary.

To determine provider reimbursement rates, states must use a statistically valid and reliable methodology. The majority of states, including Nebraska, use a market rate survey.

A market rate survey (MRS) is a study of the distribution of prices child care providers charge families for services. Prices are ranked from highest to lowest and grouped in percentiles. Each percentile level indicates the percent of providers who charge that specific rate or less. If a provider's price is at the 60th percentile, for example, then they charge more for their services than 60% of providers and less than 40%.

The Administration for Children and Families (ACF) does not require that lead agencies use a specific percentile threshold to set their rates, so there is a wide range of reimbursement rate percentiles across states, territories and tribes. ACF recommends, however, that lead agencies set their reimbursement rates at the 75th percentile; ACF considers this as providing equal access.

Because the price of child care varies based on setting, age of child and other factors, MRS research typically takes these into account in the analysis and states utilize this information to set reimbursement rates that reflect those differences. Nebraska differentiates child care reimbursement rates across four factors: age, location, accreditation/quality rating and setting type. See Table A for additional information.

In theory, if reimbursement rates are higher than what 75% of providers charge, then Nebraska families enrolled in the subsidy program should be able to access that same 75% of providers for their children's care. But that is not the reality.

Table A: 2022 Child Care Subsidy Rate Differentiating Factors

Child Age	Location	Accreditation/Quality Rating	Setting Type
Infant	Lancaster, Dakota, Douglas and Sarpy counties	Accredited provider/Step 3 on Step Up to Quality	Licensed Family Child Care Homes I and II
Toddler	All other counties	Step 4 on Step Up to Quality	License-Exempt Family Child Care Homes
Preschool		Step 5 on Step Up to Quality	License-Exempt In-Home Providers
School Age			Licensed Child Care Centers

Challenges with current provider reimbursement rates

▶ **A Broken Market**: Market rates reflect the amount providers charge, not the costs they incur, and not all providers can charge the amount required to cover the cost of quality care. Many families struggle to afford care, so providers set their rates based on what families in their area can afford. As a result, providers face difficult tradeoffs: operate at a deficit; cut costs, often through lower staff compensation and/or program quality; enroll fewer children who are eligible for CCDF subsidies or stop serving eligible children entirely; or close their program. Basing reimbursement rates on what providers charge embeds the broken market into the subsidy system.

- **Private Pay Ceiling**: Based on Nebraska Statute, the Nebraska Department of Health and Human Services (NDHHS) cannot pay providers a reimbursement rate higher than the amount providers charge their private pay families. The private pay amount creates a ceiling, capping the maximum amount a provider can receive in subsidy reimbursement. This approach exacerbates child care providers' financial issues, particularly those in low-income neighborhoods. Even when reimbursement rates defined through an MRS reflect or are close to the cost of care, it doesn't necessarily mean providers receive that amount. If a provider is located in a low-income neighborhood, they are limited to charging lower prices.

Because of the private pay ceiling, provider reimbursement rates are restricted by the amount families in their market can afford. So if providers are in a market that won't support prices that cover the cost of care, they receive lower reimbursement rates and, therefore, less CCDF funding overall. As a result, lower-income neighborhoods receive fewer resources than higher-income neighborhoods, despite incurring comparable costs. Further, CCDF reimbursement payments include restrictions not present in private pay—such as limits on the number of allowed absences and invoicing after services—that create additional financial stability for providers who accept private pay families.

Cost Estimations

Discussions about cost estimations use several different terms to relay information about cost. *Cost of care* reflects the total expenditures providers make to deliver services. *Cost of quality* or *true cost of care* refers to the cost of operating a high-quality program with staff and resources to meet quality standards.

Alternatives to Market Rate Approach

At the federal and state level, there is increasing awareness of the challenges with the market rate approach. This awareness spurred efforts to replace or supplement the market rate survey with methods based on cost rather than price, specifically cost-estimation models.

Cost-estimation models incorporate data on provider expenses to estimate the cost of a fully funded, high-quality program operating with a stable budget and staffed by effective educators. Reimbursement rates based on actual costs can shift the child care landscape in a state by enabling providers to operate more sustainable business models, lowering their risk of closing and making it more financially appealing to operate child care programs. Altogether, moving past the private pay ceiling and adopting an approach based on provider costs can stabilize and strengthen child care programs, increase the supply and quality of care and allow Nebraska's economy to thrive.

State Profiles

Rate-setting processes differ across states and demonstrate a variety of ways states are supporting children, providers and families. The comparison states profiled on Table B (next page) are Arkansas, Iowa, New Mexico, South Dakota and Virginia. These states offer a balanced portfolio of approaches to setting rates, illustrating similarities to Nebraska's process, methodologies that are discussed in this study and examples of how Nebraska's approach might evolve moving forward.

firstfive NEBRASKA
FirstFiveNebraska.org
info@FirstFiveNebraska.org

pillars research and strategy
PillarsResearch.org
ashley@PillarsResearch.org

Table B: State Profiles

	Primary Methodology	Process for Setting Reimbursement Rates	Reimbursement Percentiles/Rate	Narrow Cost Analysis	Subsidy Participation
Arkansas	Hybrid methodology. Arkansas conducts the MRS and cost model. The state is in the process of working on the next MRS and cost model.	Reimbursement rates are set by the Arkansas Division of Child Care and Early Childhood Education.	Current rates are set at the 75th percentile.	Cost model was used to estimate the costs of care at each quality level, minimum wage increases from 2019-21 and health, safety, quality and staffing requirements.	52% of licensed providers
Iowa	Market rate survey. Market rate data are collected from the statewide Child Care Resource and Referral database and updated annually. The most recent MRS was completed in 2020; currently planning for the 2023 MRS and narrow cost analysis.	The Iowa Department of Human Services prepares data, shares information and answers questions about the market rates and percentiles. Reimbursement rates are then set by the state legislature.	Legislation passed in 2021 increased reimbursement rates to at least the 50th percentile of the 2020 MRS. Currently, base reimbursement rates range from the 50th percentile to the 60th percentile.	Conducted cost survey in 2020 for narrow cost analysis, however, data was not available in time to be incorporated into rates. The cost survey/study uses cost data supplied by providers.	82.5% of providers (licensed and licensed-exempt)
Nebraska	Market rate survey. Current rates are based on the 2021 MRS. The 2023 MRS is currently under review by the Nebraska Department of Health and Human Services (NDHHS).	Under the guidance of the state legislature, NDHHS adjusts the reimbursement rates every other odd-numbered year.	Nebraska Revised Statute §43-536 requires NDHHS to set reimbursement rates between the 60th and 75th percentiles. Recent legislation raised rates to the 75th percentile through June 2023.	Extenuating environmental circumstances led Nebraska to request a waiver for completing a narrow cost analysis for the 2019-2021 and 2022-24 CCDF plans.	36% of family child care homes and 77% of child care centers. Approximately 48% of all licensed homes and centers participate in the program.
New Mexico	Alternative methodology. The methodology uses two approaches: a cost study and cost-estimation model. The methodology was conducted in 2021 and New Mexico is about to begin the process again.	New Mexico Early Childhood Education and Care Department (ECECD) sets rates based on the ACF-approved alternative methodology, through the State's official regulatory adoption process. ECECD first publishes the proposed rates for public consideration. They are then adopted and/or amended. ECECD obtains Governor approval prior to proposing the rates.	New Mexico sets its rates based on the estimated cost of care. For center-based care, the base rate covers 82% - 110% of the estimated cost of care. For family child care, the base rate covers 82% - 102% of the estimated cost of care. The rates also vary by age group and Quality Rating and Improvement System (QRIS) level.	Using the cost model, the Lead Agency ran scenarios to estimate the costs of health, safety, quality and staffing requirements, as well as the cost of quality care at each quality level on its QRIS.	71% of centers, 83% of family child care homes and 91% of group homes participate in the child care subsidy program.
South Dakota	Market rate survey. The most recent MRS was conducted in 2022.	Reimbursement rates are set after internal analysis within the South Dakota Department of Social Services.	Current rates are set at the 75th percentile.	Cost study. Reimbursement rates were evaluated against the cost of care data by age group and provider type; results were used to inform the current percentile.	49% of regulated providers
Virginia	Alternative methodology. Historically, Virginia used the MRS to set reimbursement rates. In 2022, Virginia conducted an alternative methodology for the first time. The cost-estimation model allowed the state to run multiple scenarios to understand the impact different factors have on providers.	The Virginia Department of Education worked closely with the Finance Committee and regulatory coordinators to set reimbursement rates.	The proposed cost-based rates went into effect October 1, 2022. Rates are set regionally based on the percentage of estimated costs. For centers, rates are set at approximately 75% of the estimated cost of care. For family child care, rates are average 80% of the estimated cost of care. Rates vary by age group across both settings.	The cost model was used to conduct the narrow cost analysis and accounts for the cost of meeting basic health and safety standards and quality care.	40% of providers participate in the child care subsidy program. More than half of all licensed centers, one-third of licensed family child care homes, one-quarter of voluntarily registered family child care homes and 14% of religious-exempt centers participate in the child care subsidy program.