November 18, 1997

MEMORANDUM FOR DISTRIBUTION

FROM: ELENA KAGAN
DEPUTY ASSISTANT TO THE PRESIDENT
FOR DOMESTIC POLICY

RE: DEPUTIES MEETING ON CHILD CARE INITIATIVE

As you know, the President announced that he will unveil a child care initiative in his 1998 State of the Union Address. The Domestic Policy Council has been leading a policy development process, with significant input from various federal agencies and White House offices, to develop policy options on child care for the President's consideration.

The purpose of today's Deputies-level meeting is to discuss various policy options for the child care initiative that have been developed over the past months. At the meeting, representatives from the Departments of the Treasury, Health and Human Services, and Education will make brief presentations of several proposals, with the balance of the meeting reserved for discussion.

Attached for your review please find several documents: 1) an overview paper which outlines current federal investment in child care, proposes goals for a new child care initiative, and summarizes the policy options for discussion at the Deputies meeting, and 2) the policy proposals developed by various agencies (which are summarized in the overview paper).

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CHILD CARE INITIATIVE

Overview of Current Federal Investment in Child Care

The Federal government invests in child care in a variety of ways. The two principal mechanisms designed to help parents pay for child care are the Child and Dependent Care Tax Credit (CDCTC) and the Child Care and Development Block Grant (CCDBG):

- **Child and Dependent Care Tax Credit (CDCTC).** The CDCTC provides tax relief to taxpayers who pay for the care of a child under 13 or a disabled dependent or spouse in order to work. The non-refundable credit is equal to a percentage of the taxpayer's employment-related expenditures for child or dependent care, with the amount of the credit rate depending on the taxpayer's adjusted gross income. The Federal government spent approximately $2.6 billion on the CDCTC in 1997.

- **Child Care and Development Block Grant (CCDBG).** The CCDBG is the primary Federal subsidy program devoted to child care, enabling low-income parents and parents receiving Temporary Assistance for Needy Families (TANF) to work or participate in the educational or training programs they need in order to work. Welfare reform increased federal funding for child care by approximately $4 billion over five years (FY 1997 - FY 2002), and it consolidated four child care subsidy programs into the CCDBG. The funds are distributed primarily by formula to the States to operate direct child care subsidy programs and improve the quality and availability of care. The Federal government spent 1 $2.9 billion in direct child care subsidies in FY 1997, serving a little more than one million children.

In addition, the $500 per-child tax credit in the Balanced Budget Act can provide significant additional support to help parents meet child care costs.

In addition to these programs, the federal government runs a food program for child and adult day care centers through the USDA and invests in after-school programs for school-age children. The Child and Adult Care Food Program (CACFP) provided meals to approximately 2.5 million children in approximately 35,000 child care centers (including after-school centers) in 1997. The General Accounting Office identified the CACFP as one of the most effective vehicles for reaching family child care providers and enhancing care in home-based settings. After-school programs are supported through a variety of initiatives, including the Department of Education's 21st Century Learning Centers, funded at $40 million for FY 1998, which will provide after-school program opportunities in public schools for a million children.

Goals of New Child Care Initiative

The goals for the Child Care Initiative will drive decisions on how to invest limited additional resources. Agency representatives generally have argued for a child care initiative addressing each of the following goals:

1. Helping more parents afford child care
2. Assuring safety and quality in child care
3. Making child care more available

These goals and their prioritization of course remain open for discussion and debate. A child care initiative could decide to focus on one or two of these goals, rather than all three.

Policy Options

The remainder of this memo outlines policy options relating to the goals of affordability, safety and quality, and availability. Some of the options address more than one of these goals, but are placed in a single category for organizational purposes.

I. AFFORDABILITY

In order to help more parents afford child care, the Administration could: 1) expand the Child Care and Development Block Grant and/or 2) modify the Child and Dependent Care Tax Credit. The pros and cons of building on one or both of these mechanisms are discussed in the attached papers prepared by the Departments of the Treasury and HHS. Information on the way the two mechanisms assist low-income families appears below, followed by policy options relating to each.

	CCDBG	**CDCTC**
Current Federal funding level	$2.9 billion (FY 1997)	$2.6 billion (FY 1998)
Eligibility criteria	Families (TANF and non-TANF) with children under 13 who need child care and earn less than 85% of state median income	Taxpayers who pay for at least 50% of the care of a child under 13 and/or a disabled dependent or spouse in order to work.
% of overall dollars in program going to families with AGI below 200% of poverty	100%	19%

	CCDBG	CDCTC
% of families with AGI below 200% of poverty and children under 13 who receive assistance under program	12% (of potentially eligible families)	13%
Amount of federal assistance	$2,200 (average, annual federal subsidy per-child)	1 $497 (average tax relief per family with AGI below 200% of poverty)

1. Extent of State Flexibility
2. If want targeting, what kind of targeting do you want.

1. **Increase Federal Investment in the Child Care and Development Block Grant**

There are three options for additional investment in the Child Care and Development Block Grant:

OPTION ONE: Increasing CCDBG funding based on current formula.

e.g. State elig. level must go up by X each year.

HHS recommends

OPTION TWO: Increasing CCDBG funding and working with states to set specified benchmarks or performance standards for use of additional funding (e.g. to expand eligibility, make co-payments more affordable, improve reimbursement rates).

Asking states to meet certain reqs. Don't separate new stream from old.

OPTION THREE: Increasing CCDBG funding and requiring that funds are targeted to reach families of a specified income level or to pay child care costs for children of a specified age level.

Target additional funding - Problems: State gaming
Cumbersome to do age bec. subsidy goes to families -- not individual kids

Gruber: If you are doing legis, maybe we shld Δ copayments

For each of these options, using HHS estimates, for every $100 million of annual additional investment in the CCDBG, the child care costs of at least an additional 35,000 children from families with incomes below 200% of poverty will be subsidized:

Lew: Fund. Q about child care initiative → what is our goal - Narrow goal that we can meet. Or broaden people who get it but don't solve problem as a whole.

Increased Investment in CCDBG	Number of Additional Children Reached
$100 million/year or more than $500 million/5 years	Approximately 35,000/year
$300 million/year or more than $1.5 billion/5 years	Approximately 105,000/year
$500 million/year or more than $2.5 billion/5 years	Approximately 175,000/year

FY 98 Cost = $3800 per slot, $2,200 of which is Federal.

Kitty: States already have a lot of $ for TANF population.

Mandatory 0-5 Program. Signature Clinton Admin. initiative. Focus on ~~[illegible]~~ spending shld be on early learning.

Lew: Could target at specific age group.

Sperling: Just gave $500 tax credit | $20B. Doing block grant is not memorable. 2 yrs before (0-3)

Lew: If we do affordability, then do tax cut. But not sure we can afford to do any of this.

Gene: $10 B over 5 on tax side.

Increased Investment in CCDBG	Number of Additional Children Reached
$700 million/year or more than $3.5 billion/5 years	Approximately 250,000/year
$1 billion/year or more than $5 billion/5 years	Approximately 350,000/year

2. Modify the Child and Dependent Care Tax Credit

The Child and Dependent Care Tax Credit is currently a non-refundable credit that may be claimed by taxpayers who pay for the care of a qualifying individual (children under 13 years old and/or disabled dependents or spouses) in order to work. The credit is equal to a percentage of the taxpayer's employment-related expenditures for child or dependent care. The amount of the credit rate depends on the taxpayer's adjusted gross income (AGI). The credit rate is phased down from 30% (for taxpayers with AGI of $10,000 or less) to 20% (for taxpayers with adjusted gross income above $28,000). The maximum amounts of qualifying expenses for which credits may be claimed are $2,400 for one qualifying individual and $4,800 for two or more qualifying individuals. Thus, the maximum credit ranges from $480 to $720 for a taxpayer with one qualifying individual and $960 to $1,440 for a taxpayer with two or more qualifying individuals.

Four options are proposed for discussion:

10 - 28,000 ↓ 18 - 45,000

OPTION ONE: Beginning in 1999, taxpayers would become eligible for the 30 percent credit rate if their income is $18,000 or less. The credit rate would be phased down from 30% to 20% for AGI between $18,000 and $45,000. In subsequent years, the starting point for the phase down range would be indexed for inflation, as would the maximum amounts of qualifying child and dependent care expenses that could be claimed.

IMPACT AND COST: The Department of the Treasury estimates that this option would affect 2.1 million taxpayers with AGI below $45,000, providing an average tax cut increase of $74. It would cost approximately $2.4 billion over five years (see Treasury paper for fuller discussion).

Broaden these. Richer.

1. Assuming do something, do ref. or just adjustment?
2. Assuming want to do afford., which do -- subsidy or tax.

OPTION TWO: Beginning in 1999, taxpayers would become eligible for a 50% credit rate if their income is $18,000 or less. The credit rate would be phased-down from 50% to 20% for AGI between $18,000 and $47,000. In subsequent years, the starting point for the phase down range would be indexed for inflation, as would the maximum amounts of qualifying child and dependent care expenses that can be claimed.

Blank: ~~Treas~~ Prefers refundable tax credit to subsidy

Gene: No refundability. Broaden proposals, not refundability.
$35 - 50,000 range. Very little mand. spending available. So won't be able to do big subsidy program.

IMPACT AND COST: The Department of the Treasury estimates that this option would affect 2.2 million taxpayers with AGI below $47,000, providing an average tax cut increase of $233. It would cost approximately $4.6 billion over five years (see Treasury paper for fuller discussion).

OPTION THREE: The CDCTC would be made refundable in 1999, thus allowing individuals who do not have an income tax liability to claim the credit.

below

IMPACT AND COST: The Department of the Treasury estimates that this option would affect 1.3 million families, mostly with AGI ~~between~~ 160-200% of poverty, providing an annual tax cut increase or refund of $407. It would cost approximately $6.9 billion over five years (see Treasury paper for fuller discussion).

OPTION FOUR: In addition to making the CDCTC refundable, the phase-down would be adjusted as described in Option One.

IMPACT AND COST: The Department of the Treasury estimates that this option would affect 3.4 million families, providing an average tax cut increase or refund of $347. It would cost would cost approximately $11 billion over five years (see Treasury paper for fuller discussion).

II. SAFETY AND QUALITY

Four proposals to ensure safety and quality in child care will be presented for discussion: increasing federal funds targeted to quality improvements, either by increasing funding for the CCDBG (with its set-aside for quality improvements) or by establishing a separate quality fund; increasing federal investment in education and training for child care providers; and establishing a new fund for activities related to consumer education, technology development and utilization, and data and research.

1. Increase Federal Funds Targeted to Quality Improvements

Olivia: Our approach is like Kerry.

OPTION ONE: Increase federal funding in the CCDBG and thereby increase required 4% set-aside for quality improvements.

IMPACT AND COST: For every $100 million of annual. additional investment in the CCDBG, States would receive an additional $4 million in flexible funding for quality improvements:

Elena
1. If do qual. fund, targeting?
- age?
- what qual. improvements do you want? Do you tell states what to do? spend on enforcement?
2. How much $?

Additional Annual Investment in CCDBG	Increase in Quality Set-Aside Per Year (4% of increase)
$100 million	$4 million
$300 million	$12 million
$500 million	$20 million
$700 million	$28 million
$1 billion	$40 million

Need (1) tangible results; and (2) show that these $s result in these changes.

OPTION TWO: Establish a fund distributed to the States according to the CCDBG formula to provide grants to communities to improve safety, quality, and learning for young children in child care (see HHS paper for fuller discussion). This fund would differ from the 4% set-aside for quality in the CCDBG because it would be designated for use by communities, rather than by States, and because it would be targeted for ~~to~~ infants and toddlers.

States wld have to come to you with benchmarks e.g. stds, access for families w/ babies

IMPACT AND COST: This fund would build on the North Carolina model of community grants known as "Smart Start." HHS recommends a funding level of $800 million per year or $4 billion over 5 years to reach 1,000 communities; still needed is a range of cost options and further impact analyses.

2. **Increase Federal Investment in Provider Education and Training**

OPTION: Build on the Child Care Provider Scholarship Fund announced by the President at the White House Conference on Child Care, in which states provide scholarship funds to students working toward a state or national credential, certificate or Associate, B.A. or B.S. degree. Child care workers, who must commit to remaining in the field for at least one year for each year of assistance received, will earn increased compensation or bonuses when they complete their course work, provided by some combination of the scholarship fund and the worker's employer.

IMPACT AND COST: For every $50 million of annual federal investment in the Child Care Provider Scholarship Fund (matched with one State or Community dollar for every four federal dollars), up to 50,000 child care providers will receive scholarship assistance.

Federal Investment in Child Care Provider Fund	Number of Scholarships Available
$50 million/year or $250 million/5 years	50,000/year
$100 million/year or $500 million/5 years	100,000/year
$150 million/year or $750 million/5 years	150,000/year
$200 million/year or $1 billion/5 years	200,000/year

3. **Increase Federal Investment in Consumer Education, Research, and Technology**

The CCDBG currently contains a 4% set-aside for quality activities, under which consumer education is an allowable, but not a required expense. HHS reports that although some States are investing some of their quality set-aside in consumer education efforts, these efforts are limited and scattershot. Further, HHS reports that no funds are presently targeted to child care data and research.

OPTION: Establish a new fund for activities related to consumer education, technology development and utilization, and data and research. Funds would support research and demonstration projects, a National Center on Child Care Statistics, a national child care hotline, and a consumer education campaign to help parents select safe and healthy care for their children (see HHS paper for fuller discussion).

> **IMPACT AND COST**: HHS recommends federal investment of $50 million per year; still needed is a range of cost options and further impact analyses.

III. AVAILABILITY

Two options to make child care more available will be presented for consideration: 1) investing in school-age care opportunities, and 2) providing incentives to businesses to create and/or run child care programs.

1. **Invest in School-Age Care Opportunities**

Three options will be presented for consideration:

OPTION ONE: Expand the existing 21st Century Community Learning Centers program to provide start-up funds to school-community partnerships to establish before- and after-school programs for school-age children at public schools. This expanded program would target additional funding to high-need communities (using eligibility requirements for the President's Title V Teacher Recruitment proposal), further concentrate on providing enriching after-school programming for children, and require an increased local match to ensure that programs become self-sustaining after receiving start-up funding (see Department of Education paper for fuller discussion).

IMPACT AND COST: The Department of Education recommends annual federal funding of up to $400 million. Using the Department of Education assumption of a one-to-one local match and an average per-child cost of an after-school program as $800/year, the Department estimates that this level of funding would enable the program to serve up to 1 million children. Using these estimates, other levels of federal investment would yield:

Federal Investment	Approximate Number of Children Served
$100 million	250,000
$400 million	1 million
$680 million	1.7 million (which would double the current level of participation in after-school programs)
$800 million	2 million

OPTION TWO: Establish a fund to support after-school program opportunities to be distributed to the States according to the CCDBG formula, with matching and benchmark-setting requirements. Funds would go through States directly to communities, with 50% targeted to areas with high concentrations of poverty. These funds would enable communities to create new programs and link already-existing community resources such as schools, libraries, parks, and recreation centers to build the supply of school-age care and improve quality. The proposal is modeled after the Making the Most of Out of School Time (MOST) projects (see HHS paper for fuller discussion).

IMPACT AND COST: HHS recommends an annual investment of $300 million; still needed is per-child cost and a range of investment options and further impact analyses.

OPTION THREE: Increase federal funding in the CCDBG and thereby increase CCDBG dollars targeted to support after-school opportunities. HHS estimates that approximately one-third of children currently served by the CCDBG are school-age.

IMPACT AND COST: HHS estimates a general increase in the CCDBG will proportionately increase school-age slots by approximately 30%.

2. **Provide Tax Incentive to Businesses**

OPTION: Senator Kohl has introduced legislation to provide a tax credit to businesses that incur costs related to providing child care services to their employees. Qualifying expenses would include those a business incurs to build or expand a child care facility, operate an existing facility, train child care workers, reserve slots at a child care facility for employees, or provide child care resource and referral services to employees. The credit would cover 50% of qualified costs incurred, but could not exceed $150,000 per year.

IMPACT AND COST: The Department of the Treasury advises that low-wage workers are generally less likely to receive employer-provided fringe benefits than middle- and higher-wage workers and that the proposed credit is therefore likely to benefit disproportionately middle- and higher-wage workers. The Joint Committee on Taxation has estimated the Kohl proposal to cost $2.6 billion over five years.

HHS submission

Affordability

Federal child care assistance in FY 1997 provides $2.9 billion in direct subsidies, serving a little more than one million children. However, even with this substantial investment, only 10% of eligible children receive assistance. Due to the high demand for assistance, States often set eligibility levels below the allowable income level established in the Federal statute. For example, although a State can allow families up to 85% of State Median Income to receive assistance, many States cut off eligibility at 130% of the Federal poverty level. Therefore, many working families are not eligible for direct assistance and are also unable to take advantage of the Dependent Care Tax Credit.

OPTION 1: Increase CCDBG funding without benchmarking or targeting.

Interaction with Current Program: The proposal is simply an increase in the CCDBG.

Cost Estimate: The Secretary has recommended a $700 million increase in the CCDBG to expand the number of children served with subsidies. These funds would be matched at the FMAP (which averages around 56%).

Impact Analysis: An increase of $700 million in CCDBG would provide at least 250,000 child care slots in FY 99.

Pros:
- Gives States the flexibility to spend the funds as best fits its needs.
- Enables the States to serve more working families with subsidy through the CCDBG.

Cons:
- May not be targeted enough to reach the working poor population in need of child care assistance.

OPTION 2: Increase the Child Care and Development Block Grant (CCDBG) funding and require States to set benchmarks to make care more affordable and accessible for low-income working families.

Interaction with Current Program: New funding will be provided through the CCDBG, although in order to access additional dollars, each State would have to set benchmarks, based on the State's individual situation. The benchmarks would describe how States will expand eligibility to serve more working families, make copayments more affordable, and improve reimbursement rates. For instance, if a State currently sets eligibility at 130% of the Federal poverty level, they may expand eligibility to 135% of poverty.

Cost Estimate: See Option 1 above.

Impact Analysis: An increase of $700 million in CCDBG would provide at least 250,000 child care slots in FY 99. Requiring States to set benchmarks will ensure that funds are targeted to low-income working families.

Pros:

- Retains State flexibility to use funds for the particular child care needs of their populations.
- Targets low-income working families without adding regulatory or administrative burden on the States.
- Focuses on results by requiring States to set and report on benchmarks.

Cons:

- May have to provide technical assistance to States in order for them to set appropriate and enforceable benchmarks.
- May not be sufficiently targeted to assure that funds reach specific age groups or specified income levels. However, all funds would still reach low income families that are eligible for CCDBG.

OPTION 3: Increase CCDBG funding, but require that the funds be targeted.

OPTION 3A: Target the CCDBG increase to reach families of a certain income level.

Interaction with current program: Funding would be provided through the CCDBG. Every State would be required; regardless of its individual situation, to assure that the additional money goes to families at a specified income level.

Cost Estimate: See Option 1 above.

Impact Analysis: This option would assure that additional funds are targeted to working poor families, rather than those families who are moving from welfare to work.

Pros:

- Provides a mechanism to target funds to more working poor families.

Cons:

- Limits the flexibility that States have under CCDBG to assess their own needs and allocate funds accordingly.
- Restricts States' ability to use the funds to move families from welfare to work.
- Recreates the type of administrative complications that the reforms in the Personal Responsibility Act were designed to eliminate.
- May not achieve its goal due to a substitution effect. For example, States may move the working families whom they already serve under this targeted funding and use the existing funding on other families, leading to no net increase in the number of working families served.

OPTION 3B: Target the CCDBG increase to reach children of a certain age.

Interaction with Current Program: Funding would be provided through the CCDBG. Every State would be required, regardless of its individual situation, to assure that the additional money goes to children in a specified age group.

Cost Estimate: See Option 1 above.

Impact Analysis: This option provides a mechanism to reach a specific targeted population based on the age of the children in the family. For instance, only a third of the children currently served are school age. Therefore, a general increase in CCDBG will proportionately only increase school age slots by over 30%. Targeting could increase the number and proportion of school age children affected.

Pros:

- Provides a mechanism to attempt to target funds to children in a certain age group.

Cons:

- May not achieve its goal due to a substitution effect. For example, States may move the children of a targeted age whom they already serve under this targeted funding and use the existing funding on other children, leading to no net increase in the number of children served from the specified age group.
- May restrict States' ability to serve all children in families with children of different ages (one child may be eligible while a "non-target" age child may not be eligible for the subsidy).
- Takes away the flexibility that States have under CCDBG to assess their own needs and allocate funds accordingly.
- Restricts States' ability to use the funds to move families from welfare to work, by constraining States' priorities.
- Recreates the type of administrative complications that the reforms in the Personal Responsibility Act were designed to eliminate.

Treasury Submission

Modifying the Child and Dependent Care Tax Credit

Current Law

A taxpayer may be eligible for a nonrefundable tax credit if he or she pays for the care of a qualifying individual in order to work. Qualifying individuals include children under the age of 13 and disabled dependents or spouses. The credit is equal to a percentage of the taxpayer's employment-related expenditures for child or dependent care.

The amount of the credit rate depends on the taxpayer's adjusted gross income. The credit rate is phased-down from 30 percent (for taxpayers with adjusted gross income of $10,000 or less) to 20 percent (for taxpayers with adjusted gross income above $28,000). The maximum amounts of qualifying expenses for which credits can be claimed are limited to $2,400 for one qualifying individual and $4,800 for two or more qualifying individuals. Thus, the maximum credit ranges from $480 to $720 for a taxpayer with one qualifying individual and $960 to $1,440 for a taxpayer with two or more qualifying individuals.

Employees may exclude from their taxable income (and their earnings for social security tax purposes) amounts their employers provide as child and dependent care benefits, including cafeteria plan contributions. The exclusion is limited to $5,000 of child care expenses per year and does not vary with the number of qualifying dependents. The amount of the expenses eligible for the child and dependent care credit is reduced dollar for dollar by the amount of excludable expenses.

Options to Increase the Credit Amounts and/or to Extend Eligibility

Option 1: Beginning in 1999, taxpayers would become eligible for the 30 percent credit rate if their income is $18,000 or less. The credit rate would be phased-down from 30 percent to 20 percent for AGI between $18,000 and $45,000. In subsequent years, the starting point for the phase-down range is indexed for inflation, as are the maximum amounts of qualifying child and dependent care expenses that can be claimed for the credit or the employer exclusion.

Option 2: Beginning in 1999, taxpayers would become eligible for a 50 percent credit rate if their income is $18,000 or less. The credit rate would be phased-down from 50 percent to 20 percent for AGI between $18,000 and $47,000. In subsequent years, the starting point for the phase-down range is indexed for inflation, as are the maximum amounts of qualifying child and dependent care expenses that can be claimed for the credit or the employer exclusion.

Option 3: The child and dependent care tax credit would be made refundable in 1999, thus allowing individuals who do not have an income tax liability to claim the credit.

Option 4: In addition to making the child and dependent care tax credit refundable, the phase-down range would be adjusted as described under option 1.

Impact Analysis and Cost

Cost and Number of Families Affected by Various Options									
	Cost in Fiscal Year (millions)							Number of Taxpayers with Cut (1999)	Average Tax Cut (1999)
	1999	2000	2001	2002	2003	1999-2003	1999-2007		
Option 1	39	192	204	239	238	673	2,446	2.1 million	$74
Option 2	132	613	543	550	555	1,838	4,638	2.2 million	$223
Option 3	150	698	636	683	747	2,167	6,880	1.3 million	$409
Option 4	215	1,014	965	1,068	1,205	3,261	11,078	3.4 million	$234

Options 1 and 2: Increase Amount of Child and Dependent Care Tax Credit

Pros

- The child and dependent care tax credit parameters have not been adjusted for inflation since 1982. Options 1 and 2 essentially adjust the child and dependent care credit for inflation since 1982.

  -- In 1982, nearly 6 percent of taxpayers who benefited from the child and dependent care tax credit were eligible for the maximum credit rate of 30 percent.

  -- But in 1999, very few taxpayers will qualify for the 30 percent rate because the income threshold ($10,000) has not been increased since 1982 Options 1 and 2 increase the threshold from $10,000 to $18,000, the level it would be in 1999 if the parameters had been indexed in 1982.

- Through the tax system, assistance can be provided directly to parents for their child care needs with low administrative costs.

- Working parents can receive the credit by filing a tax return and avoid the hassles and stigma associated with applying for assistance through welfare offices.

Cons

- The child and dependent care tax credit is not well targeted to those with low income.

-- Under current law, about 1 percent of the child and dependent care tax credit is received by families with money income in the bottom quintile and children under 13. About 32 percent of the credit is received by those with income in the top quintile.

-- Taxpayers, who also claim the $500 child credit, will not benefit from an increase in the child and dependent care tax credit unless their income is at least between 130 and 160 percent of poverty.

- The IRS cannot easily verify child care expenditures. In 1988, about one-third of the child and dependent care tax credit amounts were overclaimed on tax returns. While compliance efforts since 1988 may have reduced this error rate, these initiatives have not significantly improved IRS's ability to verify expenditures.

<u>Options 3 and 4: Expand Eligibility for the Credit by Making it Refundable</u>

<u>Pros</u>

- Low-income taxpayers will not benefit from an expansion of the child and dependent care tax credit unless the credit is made refundable.

<u>Cons</u>

- Many beneficiaries of a refundable child and dependent care tax credit already are able to use the EITC to fully offset their income and payroll taxes. Hence, critics of refundability will be quick to label a new refundable child and dependent care tax credit as "welfare" and vigorously fight the proposal.

- In the past, efforts to create new refundable credits (including recent experience with the child credit) have led to increased scrutiny of the EITC and its compliance problems. Unfortunately, the EITC will remain vulnerable to such attacks until the most recent set of compliance initiatives can be fully implemented, and studies show an improvement in compliance.

- The child and dependent care tax credit will generally not be available to most taxpayers until the end of the year. But low-income parents, particularly those who are just entering the workforce, need assistance in "real-time."

HHS Submission

The Supply and Quality of Care for Young Children

Currently, activities to improve safety, health, and learning in child care are funded by States under the required 4 percent minimum set-aside for such activities in the Child Care and Development Block Grant (CCDBG). States fund a variety of quality activities including training, licensing improvements, and resource and referral services. Since there is a tremendous need for direct assistance, most States spend only the minimum set-aside on quality activities.

OPTION 1: Increase CCDBG funding thereby increasing the amount of money that is allocated to quality via the 4% minimum set-aside.

Interaction with the Current Program: This proposal is simply an increase in the CCDBG.

Cost Estimate:
The funds for quality activities would increase by 4% of the total CCDBG increase. The Secretary proposes a $700 million subsidy increase.

Impact Analysis: A CCDBG increase would result in the States having more money to direct toward quality activities. The Secretary's proposal would result in $28 million more for quality. However, the net increase in quality funds would be offset by the fact that the increased subsidies would result in more children in child care in need of quality enhancements.

Pros:
- Improves affordability
- Potentially increases supply
- Devotes more funding to State-identified quality and supply issues.

Cons:
- Is not primarily a quality strategy; 96% of the new funds do not target quality at all, but 100% of the funds are applied to one of the three goals of quality, affordability, and supply.
- Does not target young children, especially infants and toddlers, who have the most critical health and safety concerns in child care.
- Does not allow the Administration to use its funds to leverage additional public and private resources to increase the total investments in quality.
- Does not pomote decision making at the community level.

OPTION 2: Establish a fund distributed to the States according to the Child Care and Development Block Grant formula to provide grants to communities to improve safety, health, and learning for young children in child care. The funds would specifically target young children, with a focus on infants and toddlers who are the most vulnerable children in care. States would be required to match the Federal money and would have to set benchmarks to measure their outcomes. At least 85% of funds would go directly to communities and 50% would be targeted to areas with high concentrations of poverty. This model is based on the Smart Start program in North Carolina which has allowed many counties to improve the supply and quality of care for young children. With these funds communities might choose to establish family child care networks, promote accreditation, help providers meet health and safety standards, and promote health and parent education in child care.

Interaction with the Current Program: The vast majority of the CCDBG funding currently goes toward affordability, most often in the form of vouchers. The quality money is extremely limited and typically goes to general activities funded by the States. Little or no money is administered for these purposes directly by communities. The new funding would not replace the quality set-aside, but would give communities a role in building local supply.

Cost Estimate:
The Secretary has recommended a $800 million dollar increase in the CCDBG to increase the health, safety and learning environment of child care programs.

Impact Analysis:
The proposal recognizes that the real issue in child care is whether *each community* has an adequate supply of quality care. These funds would improve the safety, health and learning of young children in child care by allowing up to 1000 communities to craft solutions that meet their specific needs.

North Carolina's Smart Start program demonstrates the impact that the community grants would have. One Smart Start county has expanded supply by 3,578 spaces in licensed programs. In another, every child care center and 50 percent of the family child care programs are participating Smart Start programs to improve the quality of care, which affects 1,234 young children in the county. In North Carolina's most populous county, 7000 children were enrolled in programs that received enhancements through the county's Smart Start grant. In other North Carolina communities, 1400 children received health and developmental screenings as a result of the Smart Start grants.

Pros:
- Gives flexibility to communities to tailor funds to their specific needs.
- Focuses on results by requiring communities to meet

benchmarks and report on outcomes.

- Targets young children, especially infants and toddlers, who are the most vulnerable children in care.
- Allows communities to build supply and fill gaps in their system of care.

- Meets the President's challenge to find a way to replicate successful child care models across the country.
- Uses Federal money to leverage State and local public and private sector funds.

Cons:

- Limits State flexibility to determine the use of funds.
- Targets only one age group.

HHS Submission

Child Care Provider Education and Training

Child care provider training is one of a number of allowable activities under the Child Care and Development Block Grant set-aside for quality activities, but only a small portion of the set-aside is spent for that purpose. The funds that do go to training are often spread very thin and cover only basic workshops which don't lead to credentials or degrees.

OPTION 1: Establish the Child Care Provider Scholarship Fund announced by the President at the White House Conference. States will administer scholarship funds to providers for either pre-service on in-service coursework as part of a degree or credential program. The provider and the sponsoring child care program must also bear a portion of the cost. The provider, who will receive increased compensation after the coursework is complete, must commit to remaining in the field for at least one year for each year of assistance received.

Interaction with the Current Program: These funds are targeted specifically to providers who are enrolled in a degree or certificate program, unlike current expenditures for training. In addition, these scholarships are tied to an increase in compensation.

Cost Estimate:
The Secretary's proposal recommends an investment of $150 million in scholarship funds to provide training and support.

Impact Analysis:
The scholarships will reach approximately 150,000 providers and increase the quality and supply of child care for about 1.5 million children.

Pros:
- Targets training of providers, which is a proven effective approach to build warm and responsive interactions between the provider and the child. These interactions, while often the most difficult aspect of quality to measure, have been found in recent studies to be one of the most powerful predictors of children's healthy development in child care.
- Requires an investment from several stakeholders including the provider and the sponsoring child care program.
- Impacts potentially scores of children with each scholarship, because each provider reaches many children.

Cons:
- Cannot guarantee that the recipient will stay in the field beyond the one year commitment. However, child care workers have an average turnover of over 30%, but programs like T.E.A.C.H. in North Carolina have shown that education reduces turnover. In North Carolina, staff turnover is only 10% for people who participate in the program, compared to 42% overall.

HHS Subsmission

National Leadership for Consumer Education, Research, and Technology

The Child Care and Development Block Grant (CCDBG) currently contains a 4% set-aside for quality activities, under which consumer education is an allowable cost. However, quality set-aside funds only meet a small portion of the need for consumer education. In addition, the law provides a small set-aside for technical assistance, which amounts to about $8 million per year.

OPTION 1: Establish a new fund for activities related to consumer education, technology development and utilization, and data and research to help redefine the future of child care in America. The fund would support a national child care hotline and a consumer education campaign to help parents select safe and healthy care for their children, a project to increase the use of distance learning technologies for rural and home-based providers, and a National Center on Child Care Statistics, along with research and demonstration projects.

Interaction with the Current Program: These funds will go to initiatives which will lead the field of child care into the twenty first century. Although some States are investing some of their quality set-aside in consumer education, these limited efforts are scattered around the country and provide inadequate coverage even within States. No funds are targeted to child care data and research on a national level. A few States and academic institutions are undertaking research, which primarily consists of studies with small sample sizes. Currently there is no framework to provide leadership to coordinate consumer education, technology development and utilization, and research of a national scope. The fund for consumer education, research and technology will fill that gap.

Cost Estimate: The various components of this effort total $50 million.

Impact Analysis: The Secretary's proposal provides sufficient funds for a consumer education initiative, which will reach millions of households with information for parents on how to find and select safe, healthy care. The quality of care for thousands of children, particularly rural children, will be enhanced by the training of providers, made possible by distance learning technologies. The National Center for Child Care Statistics and competitive research and demonstration projects will help policymakers, community leaders, and program developers find solutions to the lack of safe, healthy, affordable, and accessible care.

Pros:
- Targets funds directly to consumer education to assist parents in choosing care that will protect the health and safety of their children.
- Will potentially build the supply of quality care by

creating demand for quality care

- Provides funds specifically for data and research to help policy makers and community leaders better understand how to build the supply of affordable, quality care.

Cons:

- Does not directly increase the supply of care
- Does not directly make care more affordable

Education Submission

Expanding School-Age Care Through 21st Century Community Learning Centers

Description of Policy Option

The Department of Education proposes to expand the existing 21st Century Community Learning Centers program to provide start-up funds to school-community partnerships to establish before- and after-school programs for school-age children at public schools. The proposal responds to surveys showing strong parental support for keeping schools open during non-school hours and complements existing and proposed funding from HHS by enabling communities with under-utilized school facilities to apply for 21st Century funding and enabling other communities to apply for funding from HHS. The expanded 21st Century funding would provide up to 1 million school children per year with safe, drug-free, low-cost, and accessible programming combining learning, enrichment and recreational activities.

Description of Current Programs and Interaction of Proposal with Current Programs

This proposal would expand the existing 21st Century Community Learning Centers program that was sponsored by Senator Jeffords in 1994. The program has won strong bipartisan support in Congress, which increased its funding from $1 million in FY97 to $40 million in FY98 with particularly strong support from Rep. Nita Lowey. The program was designed to expand the use of school facilities during non-school hours.

In expanding the current program, the Department proposes to better target funding to high-need communities, further focus it on enriching after-school programming for children, and require an increasing local match to make sure programs become self-sustaining after receiving start-up funding. As now, schools would be required to partner with community, business, or educational organizations and programming could be provided by these partners in the schools.

Schools can currently use Title I, Safe and Drug-Free Schools and other federal funding for after-school programming, but these dollars are already committed and stretched thin. An expanded 21st Century Schools program would enable high-need schools to start before- and after-school programs linked to other federally funded activities, further benefit from federal school-based nutrition programs, and provide a catalyst for the schools to partner with community organizations and businesses.

The Education Department has also generated interest from a private foundation to supplement the 21st Century Community Learning Centers by developing training, technical assistance and networking capacity among participating sites. This private funding would further help the education and child care communities work effectively together in providing after-school care.

Impact Analysis

A $400 million per year 21st Century program would reach up to 1 million school children per year. While the current law limits eligibility to "inner city and rural" schools, the Department proposes to retarget the program to *high-need* urban, rural, and suburban communities using the same eligibility as used for the President's Title V Teacher Recruitment proposal. Thus, 4,300 high-need communities serving approximately a third of the nation's school children and 60 percent of the nation's poor children would be eligible for funding.

Pros of Expanding 21st Century Community Learning Centers

- Increases the supply of after-school programs in a cost-effective manner by establishing or expanding programs at underutilized school buildings.
- Compliments HHS funding by allowing communities to choose between school-based and non-school based options.
- Responds to surveys showing strong parental and educator support for school-based after-school programs. Parents often prefer school-based programs because they do not require transportation from school to the after-school program and they trust their school officials to care for their children and provide appropriate activities.
- Enables linkages between after-school activities and school-day activities and learning.
- Provides start-up funding not requiring on-going funding after five years.
- 21st Century Schools has a proven record of support in this Congress.
- Does not require the creation of a new federal program.

Cons of Expanding 21st Century Community Learning Centers

- Some schools operate in an isolated manner and do not broadly engage parents or community organizations in their programs. However, schools are increasingly interested in partnering with community organizations and this funding would provide a catalyst for them to do so. Schools would be *required* to partner with outside organizations.
- Some are concerned that any school-based after-school program could lead to a divisive debate over vouchers. However, 21st Century Schools has won bipartisan support in this Congress and did not engender a debate over vouchers because it is premised on taking advantage of underutilized school facilities.

Cost of Proposal

The Department of Education proposes to expand 21st Century funding from $40 million to $400 million per year, serving up to 1 million children per year, assuming a one-to-one local match and an average cost of $800 per child. Each program would set its hours to meet the community's needs but would operate for the equivalent of 3-4 hours each school day.

HHS submission

The Supply and Quality of School-Age Care

Experts estimate that nearly 5 million school-age children spend time without adult supervision during a typical week. However, only about 1.7 million children in kindergarten through grade 8 were enrolled in formal before- and after-school 49,500 programs in 1991, according to the National Study of Before and After School Programs. School-age children are currently served by the Child Care and Development Block Grant (CCDBG) subsidy program. Approximately one-third of the subsidies go to school-age children (i.e. approximately $1 billion).

OPTION 1: Establish a fund distributed to the States according to the CCDBG formula to provide grants to increase the supply and quality of school-age care. States would be required to match the Federal money and to set benchmarks to measure their progress. At least 85% of funds would go directly to communities, with 50% targeted to areas with high concentrations of poverty. The new money would allow communities to create new programs and link already-existing community resources such as schools, libraries, parks, and recreation centers to build the supply of school-age care and improve quality.

Interaction with the Current Program: Money would be targeted to school-age children, unlike the CCDBG funds. Rather than funding slots through the subsidy program, the new money would build supply and quality through partnerships in communities. Decisions would be made at the community level, rather than the State level, to allow communities to fill their own local needs.

Cost Estimate: The Secretary has recommended a $300 million dollar increase in the CCDBG to improve the supply and quality of care school-age children.

Impact Analysis:
An increase in funding for this program would affect school-age children from a variety of economic backgrounds by allowing them to have safe and productive ways to spend their before and after-school time. The funds would provide up to 500 community grants to expand current promising programs and create new, comprehensive services. The proposal is modeled after the Making the Most of Out of School Time (M.O.S.T.) projects, underway in three American cities. The following are examples of what the Seattle M.O.S.T. project accomplished in its first two years: provided training for 560 school-age caregivers, served 250 low-income children in free summer programs, served an additional 500 low-income children by establishing three new programs and expanding seven existing ones, and created a database of school-age programs that was used by 2000 families in a nine-month period.

Pros:
- Targets school-age care, which is lacking in many communities.

- Builds on existing community resources to maximize the impact of the investment.
- Prevents children's exposure to violence and substance abuse during the hours that studies show they are most likely to experience those risks.
- Enhances academic performance through academic enrichment and homework supervision and support.
- Allows communities to fill the gaps that they identify in their school-age care systems.
- Uses a community approach to reach a broader range of families than CCDBG subsidy.
- Meets the President's challenge to find a way to replicate successful child care models across the country.

Cons:

- Limits State flexibility.
- Targets only one age group.

Treasury Submission

Child Care Infrastructure Act of 1997 (S.82)

Description of Proposal

Senator Kohl has introduced a bill (S. 82) that would provide a tax credit to businesses that incur costs related to providing child care services to their employees. Qualifying expenses would include those a business incurs to build or expand a child care facility, operate an existing facility, train child care workers, reserve slots at a child care facility for employees, or provide child care resource and referral services to employees. The credit would be for 50 percent of qualified costs incurred, but not to exceed $150,000 per year.

Current Law and Interaction

The costs of child and dependent care services provided by an employer are currently deductible compensation. An employer that builds a structure for use as a child care facility would normally depreciate the associated capital costs. Under the proposal, many taxpayers will see it to their advantage to take the tax credit for expenses that they would otherwise have deducted or depreciated.

Impact Analysis

In general, low-wage workers are less likely to receive employer-provided fringe benefits than middle- and higher-wage workers. Therefore, the proposed credit is likely to disproportionately benefit middle- and higher-wage workers.

Pros

- The proposal could increase the availability of child care services by giving businesses an incentive to provide those services to their employees.
- The proposal addresses concerns about the quality of child care by requiring that qualifying expenditures be taken with regard to a licensed child care facility and by allowing training and continuing education costs for child care employees to qualify for the proposed credit.

Cons

- The proposal will not necessarily increase the number of quality child care placements or improve the quality of existing facilities. Instead, it will provide a subsidy to businesses that take the credit for expenses that they would have made -- and deducted or depreciated -- in the absence of the credit.
- Because the proposed credit is likely to disproportionately benefit middle- and higher-wage workers, it is not the most efficient use of scarce Federal resources to support child care.
- A tax credit for employers will not benefit the nearly 30 percent of the labor force whose employers are non-taxable (governments, non-profit organizations, etc.).

Cost of Proposal

JCT has estimated the proposal to cost $2.6 billion over five years.

Draft for Discussion Purposes Only
December 2, 1997

OPTIONS FOR CHILD CARE INITIATIVE

I. **Tax System**. Options for investing in child care through the tax system include:

A. *Child and Dependent Care Tax Credit.* Modify the Child and Dependent Care Tax Credit (CDCTC) by raising the top rate and moving the phase-out range. One option considered would raise the top rate from 30 percent (current law) to 50 percent and move the phase-out range from $10,000-$28,000 (current law) to $30,000-$59,000, indexed for inflation thereafter. Presently, the CDCTC phases down from a high of 30 percent at $10,000 or less of income to 20 percent at more than $28,000 of income (a phase out rate of one percentage point per $2,000 of income). Under this option, the credit would phase-out at a rate of one percentage point per $1,000 of income, from a high of 50 percent at $30,000 or less of income to 20 percent at more than $59,000. This option would cost $5.2 billion through the year 2003; less expensive options, using different rates and phase-out ranges, are also available. The credit could also be made refundable.

But offsets have been rejected before.

Need distrib. / analysis of who is helped.

B. *Tax Credits to Corporate Sector.* Provide a tax credit to businesses that incur costs related to providing child care services to their employees. Qualifying expenses could include those a business incurs to build or expand a child care facility, operate an existing facility, train child care workers, reserve slots at a child care facility for employees, or provide child care resource and referral services to employees. Under one option, the credit could cover 50% of qualified costs incurred, but could not exceed $150,000 per year. This option has been estimated by the Joint Committee on Taxation to cost $2.6 billion over five years.

But we like Senator Kohl.

II. **Child Care and Development Block Grant**. Options for increasing federal investment in the Child Care and Development Block Grant (CCDBG) include:

A. *Distribute additional funding to States by current CCDBG formula without restriction.*

B. *Require that states set benchmarks to access additional funding.* To access additional funding, states would be required to set benchmarks, concerning, for example, eligibility and priority (i.e. targeting) levels, copayments, and reimbursement rates. While states would have considerable flexibility in setting the benchmarks, continued additional funding would be contingent on progress toward meeting the benchmarks. (1) Figure out way to make clear that not prescriptive but describe what we want as an end result -- i.e. helping working families

A possible recommendation is to increase the investment by $4 billion over five years, which would provide subsidies for approximately 280,000 children per year. Less money would mean proportionately fewer additional children subsidized.

Goal: Want states to spend on working families -- reach up income scale - talk to States & hill about tactics of this.

Tie to measure against guidelines -- do in outyears or at end of year.

(2) HHS - how to talk about what we've already done.

III. **Quality/Early Learning**. Options for increasing federal investment in the quality of child care and early learning include:

A. *Child Care Provider Training.* Increase federal investment in the training of child care providers. Options include:

1. *Child Care Provider Scholarship Fund.* Announced by the President, the Child Care Provider Scholarship Fund will enable states to provide scholarship funds to students working toward a child care credential. Eligible child care workers must commit to remaining in the field for at least one year for each year of assistance received and will earn increased compensation or bonuses when they complete their course work. The President announced an investment of $250 million over five years.

2. *Expand the Child Care Apprenticeship Training Program.* Expand the Child Care Apprenticeship Program to fund the training of child care workers toward a degree equivalent to the Child Development Associate degree, with on the job observation and practice. The Department of Labor has asked for an appropriation of $10 million for FY 1999.

B. *Consumer Education and Research.* Establish a new fund to support consumer education, technology development and utilization, data and research. Uses for the new funding would include research and demonstration projects, a National Center on Child Care Statistics, a national child care hotline, and a consumer education campaign to help parents select safe and healthy care.

C. *Standards Enforcement and Licensing Support.* Establish a fund for states to improve and enforce state child care health and safety standards. Activities supported would include increasing unannounced visits to licensed child care centers and family day care homes, and improving state licensing of child care settings.

D. *Early Childhood Education.* Increase investment in early childhood education and learning activities. Options for the funding mechanism include:

Describe this better -- use Smart Start and military models. Work w/ NEC & HHS come up w/ proposal or crystallize differences.

1. *Early Childhood Education Fund.* Establish a grant program to support specific activities to improve safety, quality, and learning for young children in child care. The fund would support, among other things, health and safety improvements and parental involvement in child care. Options for the funding mechanism include:

a) *Combined local/state funding for early childhood education activities.* 50 percent of the fund would be passed through states to local collaboratives and 50 percent would be state discretionary dollars. The local funds could be allocated by states by formula or through a competitive grant process, but states would be required to use child poverty as one of the major factors in distributing the dollars. States would have considerable flexibility with their 50 percent of the funds, but would be required to set benchmarks concerning child care standards in the areas of education, health and/or safety. The fund would require a modest (e.g. 20 percent) cash match for

Q: w/in package of these things, does the general quality fund make sense? Is it too loose?

- Shld we do Early Learning at all as part of child care?
- How do you ensure that this fund gets the result you want to get?

Do you want more focused investments in quality or more generalized fund? Grant w/ allowable uses.

the state funds. There would be no match for the local funds.

b) *Funding for Local Collaboratives through States.* Funding would entirely pass through states to local collaboratives through a state-administered competitive grant program, with a modest (e.g. 20 percent) state match. States would have considerable flexibility in administering the grant program, but would be required to use child poverty as one of the major factors in distributing the dollars.

How does this differ from Head Start?

c) *Funding for Local Collaboratives through Federal Competitive Grant Program.* Funding would pass directly from the Federal government to local collaboratives through a federally-administered competitive grant program. The feasibility of this mechanism would depend on the level of funding for the program.

2. *Head Start / Early Head Start.* Increase the Early Head Start (children 0-3) set-aside (5 percent under current law), while increasing overall funding in Head Start to ensure that boosting the set-aside does not reduce the resources available for children 3-5. Early Head Start funds activities other than child care, such as parent training in child development, home visits, and family support services. One option would be to double the set-aside to enable more than 50,000 additional children to receive Early Head Start services in 2002 (relative to current law).

<u>Possible recommendations for funding the above package of initiatives fall within the range of $1.5 to $4 billion over five years</u>.

IV. **<u>School-Age Opportunities</u>**.

A. *Increasing Federal Investment in School-Age Programs.* Options for the funding mechanism include:

1. *Invest in a Two-Pronged School-Age Initiative.* Both expand the existing 21st Century Community Learning Centers program for public-school based programs and establish a new fund for community-based agencies to increase supply of school-age opportunities. The 21st Century Community Learning Program provides start-up funds to school-community partnerships to establish before- and after-school programs for school-age children at public schools. The expansion would support school-based programs in targeted high-need communities, further concentrate on providing enriching after-school programming for children, and require an increased local match to ensure that programs become self-sustaining after receiving start-up funding. Creating a fund for community use would support non-school-based programs; funds would pass through the states (by CCDBG formula with matching and benchmark-setting requirements) to communities, with 50% targeted to areas with high concentrations of poverty.

2. *Expand and Modify the 21st Century Community Learning Centers program.* Expand the existing 21st Century Community Learning Centers program and modify it so that non-school-based efforts are eligible for support.

Require coordination - push the envelope of what we can do w/in current law.

HHS - do we want to kick up to next level

3. *Expand the existing 21st Century Community Learning Centers program.*

B. *Coordination of Federal Efforts.* Set up a multi-agency task force to focus on youths during after-school hours in three to five pilot sites. The task force would gather and organize this information by the purpose for which it may be used, rather than by the agency administering it, to be of better use to communities seeking to determine what assistance is available.

Possible recommendations for funding the initiatives above fall within the range of $.5 to ~~$1.5~~ $3.5 billion over five years.

300
+400
700

V. Stay-at-Home Parents.

A. *Leave Options for Working Parents.*

Focus just on newborns?

1. *Expand the reach of the Family and Medical Leave Act* (FMLA) to cover businesses with 25 or more employees. This could also be done incrementally. Presently, FMLA covers employees of businesses with 50 or more employees.

2. *Expand the period of time for FMLA* from 12 weeks (current law) to 24 weeks.
Help 400,000 families.

3. *Provide paid parental leave coverage* for a limited amount of time for working parents below a set income level. For example, a new paid leave plan could provide 6 weeks of paid leave to all new parents who have been in the workforce either part-time or full-time for one year and whose family income is below $50,000, at a cost of $1 billion per year. This plan would use the unemployment insurance system to provide the leave payments, but would be paid for by the federal government. $200/wk for 6 wks

B. *Demonstration Project to Support Stay-at-Home Parents.* Establish a demonstration project for innovative approaches by states to enable parents to stay at home during their children's first years of life and supporting them in their role as their children's first teacher, such as through home visitation.

C. *Tax Credits.* Options include:

Political [illegible] risk of opening bal. budget

1. *Expand the child tax credit for families with children of a certain age.* For example, families with children 0 to 3 years of age could receive an additional $250, at a cost of roughly $6.5 billion over 5 years, or families with children 0 to 1 year of age could receive an additional $500, at a cost of roughly $4.67 billion over 5 years.

2. *Modify the Child and Dependent Care Tax Credit* (CDCTC) to cover certain kinds of expenses for those parents who stay at home to raise a child.
Predicated on having documentable expenses. Stay at homes don't have this.

Look at Jeffords proposal.

The Supply and Quality of Care for Young Children

Currently, activities to improve safety, health, and learning in child care are funded by States under the required 4 percent minimum set-aside for such activities in the Child Care and Development Block Grant (CCDBG). States fund a variety of quality activities including training, licensing improvements, and resource and referral services. Since there is a tremendous need for direct assistance, most States spend only the minimum set-aside on quality activities.

OPTION 1: Increase CCDBG funding thereby increasing the amount of money that is allocated to quality via the 4% minimum set-aside.

Interaction with the Current Program: This proposal is simply an increase in the CCDBG.

Cost Estimate:
The funds for quality activities would increase by 4% of the total CCDBG increase. The Secretary proposes a $700 million subsidy increase.

Impact Analysis: A CCDBG increase would result in the States having more money to direct toward quality activities. The Secretary's proposal would result in $28 million more for quality. However, the net increase in quality funds would be offset by the fact that the increased subsidies would result in more children in child care in need of quality enhancements.

Pros:
- Improves affordability
- Potentially increases supply
- Devotes more funding to State-identified quality and supply issues.

Cons:
- Is not primarily a quality strategy; 96% of the new funds do not target quality at all, but 100% of the funds are applied to one of the three goals of quality, affordability, and supply.
- Does not target young children, especially infants and toddlers, who have the most critical health and safety concerns in child care.
- Does not allow the Administration to use its funds to leverage additional public and private resources to increase the total investments in quality.
- Does not pomote decision making at the community level.

OPTION 2: Establish a fund distributed to the States according to the Child Care and Development Block Grant formula to provide grants to communities to improve safety, health, and learning for young children in child care. The funds would specifically target young children, with a focus on infants and toddlers who are the most vulnerable children in care. States would be required to match the Federal money and would have to set benchmarks to measure their outcomes. At least 85% of funds would go directly to communities and 50% would be targeted to areas with high concentrations of poverty. This model is based on the Smart Start program in North Carolina which has allowed many counties to improve the supply and quality of care for young children. With these funds communities might choose to establish family child care networks, promote accreditation, help providers meet health and safety standards, and promote health and parent education in child care.

Interaction with the Current Program: The vast majority of the CCDBG funding currently goes toward affordability, most often in the form of vouchers. The quality money is extremely limited and typically goes to general activities funded by the States. Little or no money is administered for these purposes directly by communities. The new funding would not replace the quality set-aside, but would give communities a role in building local supply.

Cost Estimate:
The Secretary has recommended a $800 million dollar increase in the CCDBG to increase the health, safety and learning environment of child care programs.

Impact Analysis:
The proposal recognizes that the real issue in child care is whether *each community* has an adequate supply of quality care. These funds would improve the safety, health and learning of young children in child care by allowing up to 1000 communities to craft solutions that meet their specific needs.

North Carolina's Smart Start program demonstrates the impact that the community grants would have. One Smart Start county has expanded supply by 3,578 spaces in licensed programs. In another, every child care center and 50 percent of the family child care programs are participating Smart Start programs to improve the quality of care, which affects 1,234 young children in the county. In North Carolina's most populous county, 7000 children were enrolled in programs that received enhancements through the county's Smart Start grant. In other North Carolina communities, 1400 children received health and developmental screenings as a result of the Smart Start grants.

Pros:
- Gives flexibility to communities to tailor funds to their specific needs.
- Focuses on results by requiring communities to meet

benchmarks and report on outcomes.
- Targets young children, especially infants and toddlers, who are the most vulnerable children in care.
- Allows communities to build supply and fill gaps in their system of care.

- Meets the President's challenge to find a way to replicate successful child care models across the country.
- Uses Federal money to leverage State and local public and private sector funds.

Cons:
- Limits State flexibility to determine the use of funds.
- Targets only one age group.

Child Care Provider Education and Training

Child care provider training is one of a number of allowable activities under the Child Care and Development Block Grant set-aside for quality activities, but only a small portion of the set-aside is spent for that purpose. The funds that do go to training are often spread very thin and cover only basic workshops which don't lead to credentials or degrees.

OPTION 1: Establish the Child Care Provider Scholarship Fund announced by the President at the White House Conference. States will administer scholarship funds to providers for either pre-service on in-service coursework as part of a degree or credential program. The provider and the sponsoring child care program must also bear a portion of the cost. The provider, who will receive increased compensation after the coursework is complete, must commit to remaining in the field for at least one year for each year of assistance received.

Interaction with the Current Program: These funds are targeted specifically to providers who are enrolled in a degree or certificate program, unlike current expenditures for training. In addition, these scholarships are tied to an increase in compensation.

Cost Estimate:
The Secretary's proposal recommends an investment of $150 million in scholarship funds to provide training and support.

Impact Analysis:
The scholarships will reach approximately 150,000 providers and increase the quality and supply of child care for about 1.5 million children.

Pros:
- Targets training of providers, which is a proven effective approach to build warm and responsive interactions between the provider and the child. These interactions, while often the most difficult aspect of quality to measure, have been found in recent studies to be one of the most powerful predictors of children's healthy development in child care.
- Requires an investment from several stakeholders including the provider and the sponsoring child care program.
- Impacts potentially scores of children with each scholarship, because each provider reaches many children.

Cons:
- Cannot guarantee that the recipient will stay in the field beyond the one year commitment. However, child care workers have an average turnover of over 30%, but programs like T.E.A.C.H. in North Carolina have shown that education reduces turnover. In North Carolina, staff turnover is only 10% for people who participate in the program, compared to 42% overall.

National Leadership for Consumer Education, Research, and Technology

The Child Care and Development Block Grant (CCDBG) currently contains a 4% set-aside for quality activities, under which consumer education is an allowable cost. However, quality set-aside funds only meet a small portion of the need for consumer education. In addition, the law provides a small set-aside for technical assistance, which amounts to about $8 million per year.

OPTION 1: Establish a new fund for activities related to consumer education, technology development and utilization, and data and research to help redefine the future of child care in America. The fund would support a national child care hotline and a consumer education campaign to help parents select safe and healthy care for their children, a project to increase the use of distance learning technologies for rural and home-based providers, and a National Center on Child Care Statistics, along with research and demonstration projects.

Interaction with the Current Program: These funds will go to initiatives which will lead the field of child care into the twenty first century. Although some States are investing some of their quality set-aside in consumer education, these limited efforts are scattered around the country and provide inadequate coverage even within States. No funds are targeted to child care data and research on a national level. A few States and academic institutions are undertaking research, which primarily consists of studies with small sample sizes. Currently there is no framework to provide leadership to coordinate consumer education, technology development and utilization, and research of a national scope. The fund for consumer education, research and technology will fill that gap.

Cost Estimate: The various components of this effort total $50 million.

Impact Analysis: The Secretary's proposal provides sufficient funds for a consumer education initiative, which will reach millions of households with information for parents on how to find and select safe, healthy care. The quality of care for thousands of children, particularly rural children, will be enhanced by the training of providers, made possible by distance learning technologies. The National Center for Child Care Statistics and competitive research and demonstration projects will help policymakers, community leaders, and program developers find solutions to the lack of safe, healthy, affordable, and accessible care.

Pros:
- Targets funds directly to consumer education to assist parents in choosing care that will protect the health and safety of their children.
- Will potentially build the supply of quality care by

creating demand for quality care

- Provides funds specifically for data and research to help policy makers and community leaders better understand how to build the supply of affordable, quality care.

Cons:

- Does not directly increase the supply of care
- Does not directly make care more affordable

Expanding School-Age Care Through 21st Century Community Learning Centers

Description of Policy Option

The Department of Education proposes to expand the existing 21st Century Community Learning Centers program to provide start-up funds to school-community partnerships to establish before- and after-school programs for school-age children at public schools. The proposal responds to surveys showing strong parental support for keeping schools open during non-school hours and complements existing and proposed funding from HHS by enabling communities with under-utilized school facilities to apply for 21st Century funding and enabling other communities to apply for funding from HHS. The expanded 21st Century funding would provide up to 1 million school children per year with safe, drug-free, low-cost, and accessible programming combining learning, enrichment and recreational activities.

Description of Current Programs and Interaction of Proposal with Current Programs

This proposal would expand the existing 21st Century Community Learning Centers program that was sponsored by Senator Jeffords in 1994. The program has won strong bipartisan support in Congress, which increased its funding from $1 million in FY97 to $40 million in FY98 with particularly strong support from Rep. Nita Lowey. The program was designed to expand the use of school facilities during non-school hours.

In expanding the current program, the Department proposes to better target funding to high-need communities, further focus it on enriching after-school programming for children, and require an increasing local match to make sure programs become self-sustaining after receiving start-up funding. As now, schools would be required to partner with community, business, or educational organizations and programming could be provided by these partners in the schools.

Schools can currently use Title I, Safe and Drug-Free Schools and other federal funding for after-school programming, but these dollars are already committed and stretched thin. An expanded 21st Century Schools program would enable high-need schools to start before- and after-school programs linked to other federally funded activities, further benefit from federal school-based nutrition programs, and provide a catalyst for the schools to partner with community organizations and businesses.

The Education Department has also generated interest from a private foundation to supplement the 21st Century Community Learning Centers by developing training, technical assistance and networking capacity among participating sites. This private funding would further help the education and child care communities work effectively together in providing after-school care.

Impact Analysis

A $400 million per year 21st Century program would reach up to 1 million school children per year. While the current law limits eligibility to "inner city and rural" schools, the Department proposes to retarget the program to *high-need* urban, rural, and suburban communities using the same eligibility as used for the President's Title V Teacher Recruitment proposal. Thus, 4,300 high-need communities serving approximately a third of the nation's school children and 60 percent of the nation's poor children would be eligible for funding.

Pros of Expanding 21st Century Community Learning Centers

- Increases the supply of after-school programs in a cost-effective manner by establishing or expanding programs at underutilized school buildings.
- Compliments HHS funding by allowing communities to choose between school-based and non-school based options.
- Responds to surveys showing strong parental and educator support for school-based after-school programs. Parents often prefer school-based programs because they do not require transportation from school to the after-school program and they trust their school officials to care for their children and provide appropriate activities.
- Enables linkages between after-school activities and school-day activities and learning.
- Provides start-up funding not requiring on-going funding after five years.
- 21st Century Schools has a proven record of support in this Congress.
- Does not require the creation of a new federal program.

Cons of Expanding 21st Century Community Learning Centers

- Some schools operate in an isolated manner and do not broadly engage parents or community organizations in their programs. However, schools are increasingly interested in partnering with community organizations and this funding would provide a catalyst for them to do so. Schools would be *required* to partner with outside organizations.
- Some are concerned that any school-based after-school program could lead to a divisive debate over vouchers. However, 21st Century Schools has won bipartisan support in this Congress and did not engender a debate over vouchers because it is premised on taking advantage of underutilized school facilities.

Cost of Proposal

The Department of Education proposes to expand 21st Century funding from $40 million to $400 million per year, serving up to 1 million children per year, assuming a one-to-one local match and an average cost of $800 per child. Each program would set its hours to meet the community's needs but would operate for the equivalent of 3-4 hours each school day.

The Supply and Quality of School-Age Care

Experts estimate that nearly 5 million school-age children spend time without adult supervision during a typical week. However, only about 1.7 million children in kindergarten through grade 8 were enrolled in formal before- and after-school 49,500 programs in 1991, according to the National Study of Before and After School Programs. School-age children are currently served by the Child Care and Development Block Grant (CCDBG) subsidy program. Approximately one-third of the subsidies go to school-age children (i.e. approximately $1 billion).

OPTION 1: Establish a fund distributed to the States according to the CCDBG formula to provide grants to increase the supply and quality of school-age care. States would be required to match the Federal money and to set benchmarks to measure their progress. At least 85% of funds would go directly to communities, with 50% targeted to areas with high concentrations of poverty. The new money would allow communities to create new programs and link already-existing community resources such as schools, libraries, parks, and recreation centers to build the supply of school-age care and improve quality.

Interaction with the Current Program: Money would be targeted to school-age children, unlike the CCDBG funds. Rather than funding slots through the subsidy program, the new money would build supply and quality through partnerships in communities. Decisions would be made at the community level, rather than the State level, to allow communities to fill their own local needs.

Cost Estimate: The Secretary has recommended a $300 million dollar increase in the CCDBG to improve the supply and quality of care school-age children.

Impact Analysis:
An increase in funding for this program would affect school-age children from a variety of economic backgrounds by allowing them to have safe and productive ways to spend their before and after-school time. The funds would provide up to 500 community grants to expand current promising programs and create new, comprehensive services. The proposal is modeled after the Making the Most of Out of School Time (M.O.S.T.) projects, underway in three American cities. The following are examples of what the Seattle M.O.S.T. project accomplished in its first two years: provided training for 560 school-age caregivers, served 250 low-income children in free summer programs, served an additional 500 low-income children by establishing three new programs and expanding seven existing ones, and created a database of school-age programs that was used by 2000 families in a nine-month period.

Pros:
- Targets school-age care, which is lacking in many communities.

- Builds on existing community resources to maximize the impact of the investment.
- Prevents children's exposure to violence and substance abuse during the hours that studies show they are most likely to experience those risks.
- Enhances academic performance through academic enrichment and homework supervision and support.
- Allows communities to fill the gaps that they identify in their school-age care systems.
- Uses a community approach to reach a broader range of families than CCDBG subsidy.
- Meets the President's challenge to find a way to replicate successful child care models across the country.

Cons:

- Limits State flexibility.
- Targets only one age group.

Child Care Infrastructure Act of 1997 (S.82)

Description of Proposal

Senator Kohl has introduced a bill (S. 82) that would provide a tax credit to businesses that incur costs related to providing child care services to their employees. Qualifying expenses would include those a business incurs to build or expand a child care facility, operate an existing facility, train child care workers, reserve slots at a child care facility for employees, or provide child care resource and referral services to employees. The credit would be for 50 percent of qualified costs incurred, but not to exceed $150,000 per year.

Current Law and Interaction

The costs of child and dependent care services provided by an employer are currently deductible compensation. An employer that builds a structure for use as a child care facility would normally depreciate the associated capital costs. Under the proposal, many taxpayers will see it to their advantage to take the tax credit for expenses that they would otherwise have deducted or depreciated.

Impact Analysis

In general, low-wage workers are less likely to receive employer-provided fringe benefits than middle- and higher-wage workers. Therefore, the proposed credit is likely to disproportionately benefit middle- and higher-wage workers.

Pros

- The proposal could increase the availability of child care services by giving businesses an incentive to provide those services to their employees.
- The proposal addresses concerns about the quality of child care by requiring that qualifying expenditures be taken with regard to a licensed child care facility and by allowing training and continuing education costs for child care employees to qualify for the proposed credit.

Cons

- The proposal will not necessarily increase the number of quality child care placements or improve the quality of existing facilities. Instead, it will provide a subsidy to businesses that take the credit for expenses that they would have made -- and deducted or depreciated -- in the absence of the credit.
- Because the proposed credit is likely to disproportionately benefit middle- and higher-wage workers, it is not the most efficient use of scarce Federal resources to support child care.
- A tax credit for employers will not benefit the nearly 30 percent of the labor force whose employers are non-taxable (governments, non-profit organizations, etc.).

Cost of Proposal

JCT has estimated the proposal to cost $2.6 billion over five years.

Affordability

Federal child care assistance in FY 1997 provides $2.9 billion in direct subsidies, serving a little more than one million children. However, even with this substantial investment, only 10% of eligible children receive assistance. Due to the high demand for assistance, States often set eligibility levels below the allowable income level established in the Federal statute. For example, although a State can allow families up to 85% of State Median Income to receive assistance, many States cut off eligibility at 130% of the Federal poverty level. Therefore, many working families are not eligible for direct assistance and are also unable to take advantage of the Dependent Care Tax Credit.

OPTION 1: Increase CCDBG funding without benchmarking or targeting.

Interaction with Current Program: The proposal is simply an increase in the CCDBG.

Cost Estimate: The Secretary has recommended a $700 million increase in the CCDBG to expand the number of children served with subsidies. These funds would be matched at the FMAP (which averages around 56%).

Impact Analysis: An increase of $700 million in CCDBG would provide at least 250,000 child care slots in FY 99.

Pros:
- Gives States the flexibility to spend the funds as best fits its needs.
- Enables the States to serve more working families with subsidy through the CCDBG.

Cons:
- May not be targeted enough to reach the working poor population in need of child care assistance.

OPTION 2: Increase the Child Care and Development Block Grant (CCDBG) funding and require States to set benchmarks to make care more affordable and accessible for low-income working families.

Interaction with Current Program: New funding will be provided through the CCDBG, although in order to access additional dollars, each State would have to set benchmarks, based on the State's individual situation. The benchmarks would describe how States will expand eligibility to serve more working families, make copayments more affordable, and improve reimbursement rates. For instance, if a State currently sets eligibility at 130% of the Federal poverty level, they may expand eligibility to 135% of poverty.

Cost Estimate: See Option 1 above.

Impact Analysis: An increase of $700 million in CCDBG would provide at least 250,000 child care slots in FY 99. Requiring States to set benchmarks will ensure that funds are targeted to low-income working families.

Pros:

- Retains State flexibility to use funds for the particular child care needs of their populations.
- Targets low-income working families without adding regulatory or administrative burden on the States.
- Focuses on results by requiring States to set and report on benchmarks.

Cons:

- May have to provide technical assistance to States in order for them to set appropriate and enforceable benchmarks.
- May not be sufficiently targeted to assure that funds reach specific age groups or specified income levels. However, all funds would still reach low income families that are eligible for CCDBG.

OPTION 3: Increase CCDBG funding, but require that the funds be targeted.

OPTION 3A: Target the CCDBG increase to reach families of a certain income level.

Interaction with current program: Funding would be provided through the CCDBG. Every State would be required; regardless of its individual situation, to assure that the additional money goes to families at a specified income level.

Cost Estimate: See Option 1 above.

Impact Analysis: This option would assure that additional funds are targeted to working poor families, rather than those families who are moving from welfare to work.

Pros:
- Provides a mechanism to target funds to more working poor families.

Cons:
- Limits the flexibility that States have under CCDBG to assess their own needs and allocate funds accordingly.
- Restricts States' ability to use the funds to move families from welfare to work.
- Recreates the type of administrative complications that the reforms in the Personal Responsibility Act were designed to eliminate.
- May not achieve its goal due to a substitution effect. For example, States may move the working families whom they already serve under this targeted funding and use the existing funding on other families, leading to no net increase in the number of working families served.

OPTION 3B: Target the CCDBG increase to reach children of a certain age.

Interaction with Current Program: Funding would be provided through the CCDBG. Every State would be required, regardless of its individual situation, to assure that the additional money goes to children in a specified age group.

Cost Estimate: See Option 1 above.

Impact Analysis: This option provides a mechanism to reach a specific targeted population based on the age of the children in the family. For instance, only a third of the children currently served are school age. Therefore, a general increase in CCDBG will proportionately only increase school age slots by over 30%. Targeting could increase the number and proportion of school age children affected.

Pros:
- Provides a mechanism to attempt to target funds to children in a certain age group.

Cons:

- May not achieve its goal due to a substitution effect. For example, States may move the children of a targeted age whom they already serve under this targeted funding and use the existing funding on other children, leading to no net increase in the number of children served from the specified age group.
- May restrict States' ability to serve all children in families with children of different ages (one child may be eligible while a "non-target" age child may not be eligible for the subsidy).
- Takes away the flexibility that States have under CCDBG to assess their own needs and allocate funds accordingly.
- Restricts States' ability to use the funds to move families from welfare to work, by constraining States' priorities.
- Recreates the type of administrative complications that the reforms in the Personal Responsibility Act were designed to eliminate.

Modifying the Child and Dependent Care Tax Credit

Current Law

A taxpayer may be eligible for a nonrefundable tax credit if he or she pays for the care of a qualifying individual in order to work. Qualifying individuals include children under the age of 13 and disabled dependents or spouses. The credit is equal to a percentage of the taxpayer's employment-related expenditures for child or dependent care.

The amount of the credit rate depends on the taxpayer's adjusted gross income. The credit rate is phased-down from 30 percent (for taxpayers with adjusted gross income of $10,000 or less) to 20 percent (for taxpayers with adjusted gross income above $28,000). The maximum amounts of qualifying expenses for which credits can be claimed are limited to $2,400 for one qualifying individual and $4,800 for two or more qualifying individuals. Thus, the maximum credit ranges from $480 to $720 for a taxpayer with one qualifying individual and $960 to $1,440 for a taxpayer with two or more qualifying individuals.

Employees may exclude from their taxable income (and their earnings for social security tax purposes) amounts their employers provide as child and dependent care benefits, including cafeteria plan contributions. The exclusion is limited to $5,000 of child care expenses per year and does not vary with the number of qualifying dependents. The amount of the expenses eligible for the child and dependent care credit is reduced dollar for dollar by the amount of excludable expenses.

Options to Increase the Credit Amounts and/or to Extend Eligibility

Option 1: Beginning in 1999, taxpayers would become eligible for the 30 percent credit rate if their income is $18,000 or less. The credit rate would be phased-down from 30 percent to 20 percent for AGI between $18,000 and $45,000. In subsequent years, the starting point for the phase-down range is indexed for inflation, as are the maximum amounts of qualifying child and dependent care expenses that can be claimed for the credit or the employer exclusion.

Option 2: Beginning in 1999, taxpayers would become eligible for a 50 percent credit rate if their income is $18,000 or less. The credit rate would be phased-down from 50 percent to 20 percent for AGI between $18,000 and $47,000. In subsequent years, the starting point for the phase-down range is indexed for inflation, as are the maximum amounts of qualifying child and dependent care expenses that can be claimed for the credit or the employer exclusion.

Option 3: The child and dependent care tax credit would be made refundable in 1999, thus allowing individuals who do not have an income tax liability to claim the credit.

Option 4: In addition to making the child and dependent care tax credit refundable, the phase-down range would be adjusted as described under option 1.

Impact Analysis and Cost

Cost and Number of Families Affected by Various Options									
	Cost in Fiscal Year (millions)							Number of Taxpayers with Cut (1999)	Average Tax Cut (1999)
	1999	2000	2001	2002	2003	1999-2003	1999-2007		
Option 1	39	192	204	239	238	673	2,446	2.1 million	$74
Option 2	132	613	543	550	555	1,838	4,638	2.2 million	$223
Option 3	150	698	636	683	747	2,167	6,880	1.3 million	$409
Option 4	215	1,014	965	1,068	1,205	3,261	11,078	3.4 million	$234

Options 1 and 2: Increase Amount of Child and Dependent Care Tax Credit

Pros

- The child and dependent care tax credit parameters have not been adjusted for inflation since 1982. Options 1 and 2 essentially adjust the child and dependent care credit for inflation since 1982.

  -- In 1982, nearly 6 percent of taxpayers who benefited from the child and dependent care tax credit were eligible for the maximum credit rate of 30 percent.

  -- But in 1999, very few taxpayers will qualify for the 30 percent rate because the income threshold ($10,000) has not been increased since 1982 Options 1 and 2 increase the threshold from $10,000 to $18,000, the level it would be in 1999 if the parameters had been indexed in 1982.

- Through the tax system, assistance can be provided directly to parents for their child care needs with low administrative costs.

- Working parents can receive the credit by filing a tax return and avoid the hassles and stigma associated with applying for assistance through welfare offices.

Cons

- The child and dependent care tax credit is not well targeted to those with low income.

- -- Under current law, about 1 percent of the child and dependent care tax credit is received by families with money income in the bottom quintile and children under 13. About 32 percent of the credit is received by those with income in the top quintile.

- -- Taxpayers, who also claim the $500 child credit, will not benefit from an increase in the child and dependent care tax credit unless their income is at least between 130 and 160 percent of poverty.

- The IRS cannot easily verify child care expenditures. In 1988, about one-third of the child and dependent care tax credit amounts were overclaimed on tax returns. While compliance efforts since 1988 may have reduced this error rate, these initiatives have not significantly improved IRS's ability to verify expenditures.

<u>Options 3 and 4: Expand Eligibility for the Credit by Making it Refundable</u>

<u>Pros</u>

- Low-income taxpayers will not benefit from an expansion of the child and dependent care tax credit unless the credit is made refundable.

<u>Cons</u>

- Many beneficiaries of a refundable child and dependent care tax credit already are able to use the EITC to fully offset their income and payroll taxes. Hence, critics of refundability will be quick to label a new refundable child and dependent care tax credit as "welfare" and vigorously fight the proposal.

- In the past, efforts to create new refundable credits (including recent experience with the child credit) have led to increased scrutiny of the EITC and its compliance problems. Unfortunately, the EITC will remain vulnerable to such attacks until the most recent set of compliance initiatives can be fully implemented, and studies show an improvement in compliance.

- The child and dependent care tax credit will generally not be available to most taxpayers until the end of the year. But low-income parents, particularly those who are just entering the workforce, need assistance in "real-time."

THE SECRETARY OF HEALTH AND HUMAN SERVICES
WASHINGTON, D.C. 20201

NOV 18 1997

MEMORANDUM FOR THE PRESIDENT AND THE FIRST LADY

On the morning of the first-ever White House Conference on Child Care, you reminded the Nation that no parent should ever have to choose between work and family or between earning a decent wage and caring for a child. The growing number of women with children in the labor force is one of the biggest social changes of the 20th century; coming to terms with that change is one of our biggest challenges of the 21st century. As Secretary Rubin pointed out at the Child Care Conference, our new economy cannot continue into the 21st century unless we as a Nation can ensure safe and affordable child care. As we know from both the common sense experience of parents and a range of emerging research, our children cannot grow and thrive unless those child care settings protect their health and safety and provide an environment in which they can learn.

Together, you have lead an extraordinary national dialogue on child care. Over the past five years your Administration has taken important steps to increase funding for child care, particularly for families transitioning from welfare to work. Yet, as your White House Conference demonstrated, we still have a long way to go.

We need a bold new 21st Century Child Care Initiative to draw on the energy the Child Care Conference unleashed from all Americans -- federal, state and local leaders; employers; the faith community; child care providers; and families themselves, both rich and poor. This initiative must build on what we know about what children need to be safe and healthy, about what works in communities, and about what parents and employers need to assure a strong and effective labor force.

We cannot settle for addressing just one of these needs or just one part of the problem, because the stakes are too high for us as a Nation. We cannot meet the 21st century challenge of a thriving economy and growing children if we settle only for making child care more affordable for struggling families while leaving children's safety at risk -- or if we settle only for improving some children's care while leaving the cost of child care out of range for far too many working families. A piecemeal approach will undercut both our short-run and long-run success by failing to respond to the deeply felt needs of parents; by playing different families off against each other, rather than building a shared commitment to America's future; and by failing to provide the real leadership that communities, states, employers, and families need to move forward.

Let me say more about what we know now about each of these needs:

Across the country we hear from working families that they are struggling to afford safe care for their children. Low-income working families are spending on average a quarter of their income on child care. Although some 10 million children from working families are eligible for direct child care assistance, federal subsidies serve a little more than one million children. The Dependent Care Tax Credit reaches only a fraction of these families since it is not refundable and provides only minimal support. Your new plan must address these hardworking, low-income families. They get up each day, work hard and play by the rules and yet still cannot afford quality health care or child care.

The children of these working parents too often spend their days in settings that do not promote healthy child development and may even compromise their safety. With millions of infants and toddlers now in care, children can spend years in poor care before they enter school, directly affecting school readiness. The recent National Institute of Child Health and Human Development study clearly demonstrated that high quality care for very young children is consistently related to high levels of cognitive and language development.

Once children enter school, we do not take advantage of the valuable learning time after school and throughout the summer months. Learning does not stop at 3:00 p.m., and it is certainly not seasonal. We no longer need our children to tend our fields during the summer. Furthermore, numerous studies now indicate that the lack of care and attention put our youth at risk for greater alcohol, tobacco, drug use, teen pregnancy, and involvement in crime.

Despite these needs, very few communities have resources to create solutions to the quality, affordability, and availability issues that you outlined at the White House Conference. The vast majority of assistance goes directly to parents to pay for care. A very small amount, about four percent of direct subsidy, goes to quality activities, which are usually planned at the state level. Some communities, like those that Governor Hunt described in North Carolina, are combining a variety of resources to stimulate innovation and capitalize on the commitment of their neighborhood schools, employers, and parents. As you pointed out at the Conference, we need to take the models that are working in one community and give other communities an opportunity to adapt them to meet their specific needs.

Given what we know about child care both from emerging research and from what parents have told us, I have recommended to OMB and White House Staff a series of investments to seriously address the health, safety, and developmental needs of our youngest children and our school-age children, for whom care is most often of poor quality and in short supply.

In your State of the Union address and fiscal year 1999 budget submission, I strongly urge you to put forward a comprehensive plan that would include six critical child care investment strategies to help families and communities.

For families:

- o Increase the number of children from low-income working families that receive child care assistance by 250,000 in 1999 by expanding direct assistance by 700 million dollars. This would be an important first step toward the goal of doubling the number of children now receiving direct child care assistance.

- o Reach millions of working families by modifying the Dependent Care Tax Credit (DCTC) in two ways, making it refundable and expanding the credit to provide greater assistance to low-income working families. At a minimum we should update the DCTC; it has not been indexed for inflation since 1982. The time for change in this critical family support is long overdue.

For communities:

- o Enable up to 1,000 communities to craft innovative solutions to protect the health and safety of infants and toddlers in care. This will demonstrate your commitment to school readiness in 1999, the tenth anniversary of the education goals. Investment: 800 million dollars.

- o Enable up to 500 communities to find local solutions to school-age child care needs. Link such an effort with an expansion of your Schools of the 21st Century program to ensure that we maximize the use of schools as part of this overall community mobilization effort. A particular emphasis needs to be put on after school alternatives for adolescents. Investment: 300 million dollars.

- o Provide training and education to at least 150,000 providers, affecting the care of about 1.5 million children. This would build on the National Child Care Provider Scholarship Fund that you announced at the White House Conference. Investment: 150 million dollars.

- Put in place a system of consumer education and supports for research and data collection as well as the use of technology for training providers. This effort would include a national consumer education campaign, a training strategy to reach home providers and caregivers in rural communities and a National Center on Child Care Statistics that will finally give us the critical information we need to plan future policy direction in this area. Investment: 50 million dollars.

Together, you have set the stage for an unprecedented national discussion and investment in child care and after school programs. The American people know we have a child care system that does not work effectively for families or for children.

Building on the momentum that you began with the White House Conferences, your FY 1999 budget and the State of the Union should present a concrete and powerful strategy to build a 21st century child care system.

I believe that with your inspiring leadership, we can add another building block to your effort to redefine the future of working families in America. This will be another historic legacy of your Presidency.

Donna E. Shalala

Integrated package

Child Care Initiative

$10B Tax

$2½-5B Spending

Elmira – do as part of tobacco settlement – connect to hospitals, HMOs → who provides home visitors

Spending Options

I. Subsidy (Child Care and Development Block Grant)

II. Quality Fund acceptable menu of things to use it for

III. Targeted Investment for Quality/Availability

A. Scholarships/Apprenticeships
B. Consumer Education, Research, and Technology
C. Enforcement – Advocate for stds – "voluntary" – don't give $ unless stds meet a certain level
D. Early Learning/Head Start
E. School-Age Care

"Educare" home visitation

more $ into
- Early HS
- Quality reforms

Tax Options

I. Child and Dependent Care Tax Credit (CDCTC)

A. Refundable?
* B. Funding Level?

* II. Tax Credits for Businesses that Build/Operate Child Care Centers (Sen. Kohl Proposal)

→ Go farther – build a <u>market</u> for child care
Look at Hunt

Stay-at-Home Parents Strategies

* I. Family and Medical Leave (FMLA) Expansion
- Dropping employee limit
- ~~Add~~ Double length of time

II. 3/4 Subsidy

* III. Child and Dependent Care Tax Credit (CDCTC) Modification

Reforming UI so it wld pay for leave

Phasing in phase out of marriage penalty

DPC PRINCIPALS MEETING
November 24, 1997
Roosevelt Room
6:00 p.m.

Secretary Cohen
Secretary Rubin
Attorney General Reno
Secretary Glickman
Secretary Herman
Secretary Shalala
Secretary Cuomo
Secretary Riley
Frank Raines
Janet Yellen
Gene Sperling
Ron Klain
Erskine Bowles
Cabinet Affairs
Ann Lewis
Melanne Verveer
John Hilley
Mickey Ibarra
Rahm Emanuel
Audrey Tayse-Haynes
Bruce Reed
Maria Echaveste

Child Care Proposal

We are developing a child care proposal that will help working families afford child care, make targeted investments to improve the safety and quality of child care, particularly for infants and toddlers, and provide safe, constructive activities for school-age children.

To help working families afford child care, the proposal: (1) increases funding for federal child care subsidies through the Child Care and Development Block Grant; and (2) changes the Child and Dependent Care Tax Credit by raising the percentage of child care expenses for which a taxpayer may take a credit and by increasing the income levels of taxpayers who may claim it. [ELENA: I DIDN'T KNOW IF YOU WANTED THIS MUCH DETAIL, BUT IF YOU DO HERE IT IS -- (Currently, the credit rate is phased down from 30% for taxpayers with adjusted gross income of $10,000 or less to 20% for taxpayers with AGI above $28,000. We are considering a series of options, including raising the credit rate from 50% for taxpayers with AGI of $30,000 to 20% for those with AGI above $59,000.)]

We are also considering targeted investments to improve the safety and quality of care. First, the proposal adds funding to the scholarship program for child care providers, which you announced at the child care conference and which has received strong support. Second, it includes a new program that will ensure safety and healthy early learning and development for children in the critical first years. Third, the proposal provides resources for states to improve their enforcement of health and safety standards, and fourth, it funds parent education, research and technology.

Finally, the proposal coordinates existing programs and increases the availability of safe, constructive activities for youth during after-school hours.

Child Care Initiative
Spending Options

I. Subsidy (Child Care and Development Block Grant)

II. Quality Fund - Safety and Learning for Infants and Toddlers

III. Targeted Investment for Quality/Availability

A. Scholarships/Apprenticeships
B. Consumer Education, Research, and Technology
C. Enforcement
D. Early Learning/Head Start
E. School-Age Care

Emily - states want more $ in block grant; scholarships; enforcements
No school age.

USDA -- makes big quality improvements.

Treas. - Do Schol. but not too much more too quickly

TO DO

Call Joan

Treas. - richer tax options

CCDBG - how does benchmark work?

Schol. - how relates to apprenticeship program

After-school - HHS/Educ/Justice/Ag -- NEC/DPC/OMB coordinate proposals -- how do you know you are buying something new?

Early Learning - Kerry/Bond Challenge Grants v. HHS proposal

Stay at Home Parents

1. Tax
2. FMLA
3. After school
4. Quality
- QIF v. Gene
- Schol. / Apprent.

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TO: Jennifer Klein
Nicole Rabner

FROM: Amy Finkelstein

SUBJECT: CEA Talking Points for Child Care Meeting

DATE: November 13, 1997

Attached are some issues that CEA thinks should be considered in assessing the relative merits of increasing the CCDBG and making the CDCTC refundable. Becky Blank will bring up these points in the Deputies' meeting next week. If you are circulating materials in advance to the participants, she would like these included in the circulation.

Thanks.

EXECUTIVE OFFICE OF THE PRESIDENT
COUNCIL OF ECONOMIC ADVISERS
WASHINGTON, D.C. 20502

Talking Points:
The Choice Between Increases in Direct Subsidies and Making the CDCTC Refundable

There is a large unmet need for child care subsidies among low income families (i.e. below 200 percent of poverty) in which the mother works. Two options for increasing federal funding to this group are an increase in the amount of funding for the Child Care and Development Block Grant (CCDBG) and making the Child and Dependent Care Tax Credit (CDCTC) refundable. Currently, the CCDBG provided $3 billion in FY 1997 and is scheduled to increase to $3.7 billion by FY 2002. The CDCTC currently has a progressive rate structure, but it is non-refundable. Estimated tax expenditures are $2.8 billion for FY 1998.

ARGUMENTS FOR CDCTC REFUNDABILITY OVER INCREASED SUBSIDES

Reaching more people for a given expenditure. A fundamental tradeoff between increasing the CCDBG and making the CDCTC refundable is the tradeoff between giving a larger group of people a smaller subsidy and concentrating the subsidy so that larger subsidies are given to fewer people.[1] A refundable CDCTC provides a subsidy to *all* low income families with working mothers and children in paid child care who file federal tax returns. In contrast, states concentrate CCDBG subsidies on about 10 percent of eligible children, leaving approximately 9 million low income children whose mothers work without access to subsidies for paid child care.[2] Of course, credits through the CDCTC would be considerably smaller than those given out through the block grant.[3] However, such credits would provide a minimum level of support to all those in need; states could then use their CCDBG block grant funds to target subsets of this group as they see best.

Reaching groups who currently may not receive much child care assistance

- **The near-poor.** 70 percent of federal block grant funds go to families at or below poverty, leaving little funding for near-poor working families. These families are also unable to get the full benefits of the current CDCTC: Due to low tax liabilities, a taxpayer may not receive the full amount of the credit until his income exceeds 140 to 160 percent of poverty, depending on

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[1]We assume that the federal government cannot easily affect targeting and the amount of benefits per recipient in the subsidy program.

[2]HHS preliminary estimates based on FY 1995 data (the most recent available data). All estimates about the CCDBG are based on this data. Note that the subsidy program has been changed since then.

[3]At the existing credit rates, a low income family with two children could receive a maximum credit of $1440 per year ($720 for a family with one child). Annual federal subsidies in the programs that CCDBG replaced averaged approximately $3200 in FY 1995. Average annual child care expenditures were $3,848 in 1993.

family composition. Making the credit refundable would therefore benefit a population that is currently receiving little support from *either* the CCDBG or the existing CDCTC.

- **The non-welfare population.** States have an incentive to spend their CCDBG funding on the welfare population, in order to help move this population into the labor market and thus meet their work requirements and avoid financial penalties. Some anecdotal evidence suggests that states are targeting their subsides to the welfare population, at the expense of the working poor and near-poor, although data are not yet available to confirm this.[4] A refundable CDCTC, would ensure that non-welfare poor and near-poor working families also receive some federal funding for child care.

The link to quality. A subsidy administered through the tax code can bypass state regulations of child care providers and facilities. To the extent that these regulations are inefficient or serve to increase the cost of care, this is a benefit to providing subsidies through the tax code.

Administrative costs. Although in general a tax credit is less costly to administer than a direct subsidy program, given that the CCDBG administrative framework is already in place in all states, the administrative costs of the two options may be comparable.

State choices. A refundable CDCTC would provide subsidies to consumers of child care, while increases in the CCDBG might give states flexibility to use the money for provider subsidies. There is evidence that such provider subsidies are an inefficient use of resources, providing subsidies to providers for what they would have done anyway.

Political issues. It may be easier to chip away at direct subsidies than at a refundable tax credit.

ARGUMENTS FOR INCREASED SUBSIDIES OVER CDCTC REFUNDABILITY

Spreading money too thinly. The CDCTC provides a much smaller subsidy than average CCDBG subsidies (see above). It might be that a better use of scarce resources is to provide a smaller group with larger subsidies. For example, larger subsidies would have much larger effects on decisions to use paid care and decisions of mothers to work. Of course, an option is to increase the credit rates for low income families as well as making it refundable; this however would increase the cost of the reform.

Link to quality. A subsidy administered through the tax code can bypass state regulations of child care providers and facilities. To the extent that these regulations are important to ensure the basic health and safety of children and/or to promote their development, this is an advantage to increasing the CCDBG rather than making the CDCTC refundable.

Timing. The CDCTC is currently received once a year, when taxes are filed. Child care costs,

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[4]Furthermore, the CCDBG requires that states spend at least 70 percent of their mandatory funds (2/3 of the total) to provide child care services to families that are on TANF, trying to get off TANF through work activities, or at risk of becoming dependent on TANF.

however, are a large burden throughout the year to low income families. Direct subsidies, which can be delivered at more regular intervals, may therefore be a more effective policy tool. However, it would be possible to allow workers to reduce their monthly withholdings with a refundable CDCTC, as is done with the EITC.[5]

Monitoring/compliance. It is difficult for the IRS to verify that there is a child living in the house who is receiving paid care. The state social service office may be better able to monitor its subsidy recipients for potential abuse.

Leveraging state money. Although no state match is required for the discretionary component of the CCDBG (approximately one-third of the total), or the mandatory part equal to the funding the state received in an average of recent years, additional mandatory funding requires a state match. In this way, increases in mandatory CCDBG funding may help to 'leverage' additional state funding in a way that a refundable CDCTC would not.

Political issues. An initiative to make the CDCTC refundable may bring increased scrutiny and criticism of the EITC.

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[5]Use of this option by EITC recipients has historically been quite low; in 1989, the most recent year for which data are available, less than one-half of one percent of all EITC recipients availed themselves on this early payment option. Although there is no direct evidence on why this option is so little used, it may be because the EITC varies substantially with income. The CDCTC currently provides a flat credit rate of 30% for families with adjusted gross income of $10,000 or less and then gradually phases down to 20% for families with AGI above $28,000. Therefore, if reduced monthly withholdings were only allowed at the minimum credit rate of 20 percent, this would alleviate that problem. Use of this reduced monthly withholdings option for a refundable CDCTC might decrease if a more complex rate structure were introduced for lower income families.

CEA Preliminary Draft

cc: jen | melanne
Marsha

WorkingMother

October 30, 1997

Mrs. Hillary Rodham Clinton
The White House

Dear Mrs. Clinton,

Thank you so much for inviting me to the White House Conference on Child Care. Your commitment was inspiring to all of us who care so much about this issue. I'm also pleased that the administration is already at work on implementing changes.

I know you will be bombarded with suggestions on the subject, so I will offer only two. If Dependent Care Spending Accounts were extended until a child was 17, it would help increase the supply of after-school care and engage teens in positive activities during those years when risky behavior is so prevalent. And consider making the law more flexible so that parents could use the funds from the accounts to help schools subsidize a band, intramural activities, the school newspaper or yearbook (where my interest in journalism began). As the President mentioned, many of these extracurricular activities have been victims of budget cuts.

Again, my thanks for including Working Mother. And happy birthday!

Best wishes,

Judsen

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