Subsidy reimbursement rates in Texas remain far below the true cost of providing child care

CHILD CARE IN CRISIS: TEXAS CASE STUDY RESEARCH BRIEF #4

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Each state operates a child care subsidy program that provides financial assistance to make child care more affordable for families who meet state income and work requirements. Nationally, approximately one in four children meet federal guidelines for subsidy eligibility, and two million children receive subsidies each year.[1] Subsidy programs are paid for with a combination of state and federal funds, with federal contributions coming primarily from the Child Care and Development Block Grant (CCDBG).[2] The federal government provides guidance on how funds are used and the subsidy programs are administered at the state level. As such, states make key decisions that determine the affordability of child care for families and the profitability for providers.

> *"The child care subsidy reimbursement is so low that I lose money with every subsidy slot. Essentially, I am subsidizing the subsidy system."*
> **- Texas child care director**

Reimbursement rates – that is, the amount that child care programs are paid for the care they provide to children using subsidies – play a critical role in ensuring the subsidy system meets the needs of both families and child care programs. States have considerable flexibility on the reimbursement rates they set, though federal guidelines recommend that states set and regularly update reimbursement rates using a market rate survey or other approved method, and set rates high enough to promote equal access to child care for children using subsidies. If reimbursement rates are too low, child care programs will lose money by accepting subsidies compared to serving a private-pay child, potentially limiting the number of programs willing to accept subsidies, limiting the number of subsidy-eligible children who can access care, and straining the finances of child care programs that do accept subsides.

Along with conducting a landscape scan of policies and practices across other states, the Prenatal-to-3 Policy Impact Center surveyed more than 800 child care directors and convened a Workgroup of 27 child care experts to create consensus recommendations on how to improve the quality of the Texas child care workforce. The central finding from this research quickly emerged: the child care industry is under-funded and under-resourced, and the key to improving workforce quality begins with providers' financial stability.

Contributing to financial instability, current subsidy reimbursement rates in Texas are too low – sometimes substantially too low – to cover the true cost of providing child care. Further, the method for calculating reimbursement rates may perpetually reimburse providers inadequately for the care provided, contributing to the ongoing instability of the industry, in the absence of corrective policy action.

Texas sets reimbursement rates using a market rate survey, but market prices do not necessarily reflect the full cost of providing child care

Most states – including Texas – set subsidy reimbursement rates using a market rate survey. A market rate survey asks child care providers across a state about the prices they charge for child care, and the state uses that information to set reimbursement rates. In Texas, reimbursement rates vary based on the age of the child, type of child care program (home- vs center-based), region, and program quality, but as of October 1, 2022, regional Workforce Boards must set reimbursement rates to at least the 75th percentile of the market rate within their region (in line with federal recommendations).[3] In other words, reimbursement rates must meet or exceed what 75 percent of child care programs charge for tuition within a region.

> *"The market rate survey reflects only what is charged and doesn't really reflect the true cost of what it takes to assure a quality program."*
> **- Texas child care director**

A market rate survey measures what child care programs are able to charge families in their region. However, the market rate cannot account for the fact that child care prices are constrained by what families can afford to pay. As a result, setting reimbursement rates based on a market rate survey may *underestimate* the cost to child care programs for providing care, especially for infants whose care is more expensive, and in low-income regions where the market rate is especially low.

Several states have adopted a cost estimation model to set reimbursement rates at the true cost of providing child care

To calculate what child care subsidy reimbursement rates should be to cover the cost of the care provided, several states – including New Mexico,[4] Washington D.C.,[5] and Virginia[6] – have received approval to use a cost estimation model to set reimbursement rates at the true cost of care. The idea behind the true cost of care model is simple: the payment child care programs receive for their services should be equivalent to the actual cost of the service they provide, to ensure a sustainable business. Cost estimation models consider all of the costs that go into providing child care - such as costs for labor, toys, and facility expenses - to generate an accurate estimate of the true cost of care.[7]

To better understand the role of subsidy reimbursements in the financial struggles of child care providers across Texas, the Prenatal-to-3 Policy Impact Center created a Texas-specific cost estimation model. Using the framework of a cost estimation model developed by the Center for American Progress (CAP),[8] we adapted the model to account for Texas licensing requirements, quality guidelines, and Texas-specific costs, and we incorporated flexibility to include Workgroup-driven budget priorities to produce estimates for the cost of providing child care in Texas. Estimates for the true cost of providing child care across different age groups, regions, and quality levels can be used to identify subsidy reimbursement rates that adequately compensate child care programs for the care they provide.

The true cost of infant care in Texas is $1,757 per month, almost twice as much as the statewide average reimbursement rate for infant care

The cost estimation model for the Texas true cost of care incorporates the day-to-day expenses of Texas child care programs, including costs associated with care provision and running the business, as well as costs associated with renting or owning and maintaining the facility where care takes place. Because both costs and cost considerations differ between center- and home-based care, we focused on center-based rates for this analysis. As with current reimbursement rates, the cost estimation model generates different reimbursement rates based on tiered levels of quality (Two-, Three-, or Four-Star care). The goal of tiered reimbursement rates is to incentivize quality child care, and support Texas child care programs to raise and maintain the quality of child care provided. The rates presented in this brief reflect the ultimate goal of high-quality, Four-Star care, but all rates can be found online.

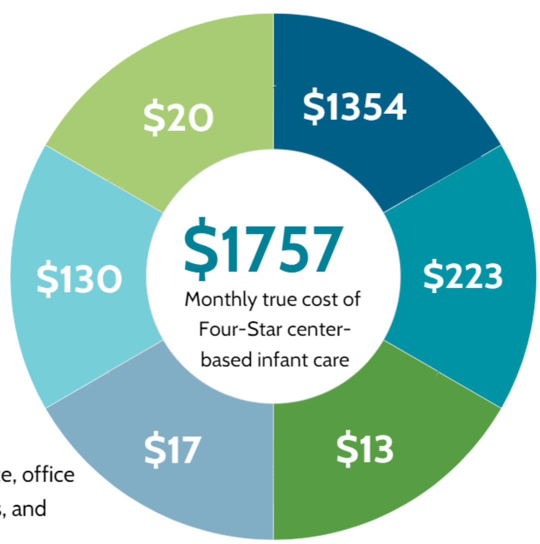
> *"If the child care subsidy was raised, we could afford to raise compensation for staff members."*
> **- Texas child care director**

Most day-to-day costs for child care programs are fixed – programs cannot pay less for rent or food regardless of their revenue. Staff wages and benefits are often the only place where child care programs can try to lower costs to stay afloat, resulting in low wages and scarce benefits for early childhood educators across the child care industry. Texas Director Survey results demonstrate the implications to the workforce: 90 percent of early childhood educators don't earn a living wage,[9] 70 percent of educators don't have access to benefits,[10] and 97 percent of child care directors face difficulties hiring, but cannot afford to raise wages.[11] As a result, many child care businesses are closing[12] or operating while understaffed,[13,14] leading to ever-diminishing access to care for Texas families.[15] The Texas cost estimation model builds in fair, competitive wages[a] to combat workforce instability and ensure child care programs can hire and retain high-quality early childhood educators.

Educational expenses
Costs related to the educational aspects of child care, including educational supplies (e.g., toys, activities, curriculum), and child assessment tools.

Food-related expenses
Cost to provide required meals and snacks, including the costs of food, food preparation, and kitchen supplies.

Business expenses
Cost of internet and phone service, office supplies, miscellaneous expenses, and advertising fees.



Personnel expenses
Cost of competitive wages and benefits for staff and early childhood educators to allow for the appropriate number of lead and assistant teachers per classroom to ensure safe and responsive child-to-educator ratios, and to cover classrooms during planning time and PTO.

Facility expenses
Costs to pay for the facility where child care takes place. Includes rent or mortgage and property tax, as well as costs for utilities and maintenance.

Legal expenses
Costs to pay for essential fees and permits, insurance, and annual expenses related to tax preparation/audit.

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[a] *Wages included in the cost estimation model have parity with Texas K-12 public schoolteachers and range from $15 to $19.42, based on education and experience.*

Cost of living varies across Texas regions, and therefore reimbursement rates based on the true cost of care vary regionally as well. Looking at the statewide average, however, accounting for the personnel, facility, legal, educational, food-related, and business expenses that contribute to the cost of providing child care, the model estimates that the monthly true cost of providing Four-Star center-based care in Texas ranges from $1,040 for a school-age child up to $1,757 for an infant.

Texas is underpaying for child care by as much as $870 per month

The Texas cost estimation model indicates that the monthly cost of Four-Star infant care in Texas is $1,757. Even with reimbursements at the 75th percentile of the market rate, Texas monthly reimbursement rates for Four-Star center-based care fall short of the true cost of care by at least $327 and up to $870 per child. For infants, who are most expensive to care for because of the need for low child-to-educator ratios, Texas pays just over half of the actual cost of care and the child care program must make up the difference, often at the expense of early childhood educator wages. The Texas Director Survey shows that early childhood educators who work at subsidy-accepting programs earn, on average, $1,240 less per year than those working at programs that do not accept subsidies.[16]

Table 1. Comparison of monthly true cost of care and current reimbursement rates for center-based, Four-Star child care (statewide averages)

	Monthly true cost of care	Current monthly reimbursement rates	Monthly loss to child care programs per subsidy
Infant	$1,757	$887	$870
Toddler	$1,548	$778	$770
Preschool	$1,130	$740	$390
School-Age	$1,040	$713	$327

Reimbursing at the market rate discourages child care programs from participating in the subsidy program, limiting access to child care for families. Among programs that do participate, low reimbursement rates lead to thinner margins for child care programs, lower wages for early childhood educators, and lower quality care for families. In other words, when Texas does not pay the actual cost of child care, child care programs, early childhood educators, and families pay the price.

Conclusion

Child care subsidies are an important tool for Texas, allowing families to work and children to access care, promoting healthy child development and family self-sufficiency and economic wellbeing. In Texas, this system operates at the expense of child care providers who are underpaid by as much as $870 per month, per child, for their services. Texas, like most states, uses a market rate survey to set subsidy reimbursement rates, but switching to a cost estimation model may generate more accurate reimbursement rates that fairly compensate child care programs for their services and could support the development of a stable child care workforce and a thriving child care industry.

About the Report: *Workgroup Recommendations to Inform the Strategic Plan*

In response to Texas HB 619 (2021), the Prenatal-to-3 Policy Impact Center worked in partnership with the Texas Workforce Commission and convened a Workgroup of 27 child care experts and designed and administered an original survey, collecting data from more than 800 child care directors across the state. Using novel data on workforce characteristics, wages, and education collected from the statewide, representative sample of directors, the Policy Impact Center and the Workgroup created a comprehensive set of recommendations to improve the quality of the child care workforce in Texas and create sustainable, long-lasting changes to improve the quality of child care across Texas.

The Workgroup recommends that the Texas legislature increase funding for child care to stabilize the market and ensure access to high-quality care, including through 1) providing retention bonuses to educators, 2) increasing subsidy reimbursement rates to reflect the true cost of care, and 3) expanding the number of subsidized slots provided. The workgroup also provides a series of recommendations for state and local government entities and educational institutions to raise workforce quality and support the child care sector, and outlines how other states are funding their improvements to early childhood education.

The full methods for calculating the true cost of care are in Appendix D of the full report.

Read the full report here: https://pn3policy.org/resources/workgroup-recommendations-to-inform-the-2022-texas-child-care-workforce-strategic-plan/

Who We Are

The Prenatal-to-3 Policy Impact Center translates the science of the developing child into state level policies that have the strongest evidence of improving outcomes for infants and toddlers and their parents. Based in Vanderbilt University's Peabody College of Education and Human Development, the Center's team of researchers and nonpartisan policy experts work with policymakers, practitioners, and advocates to navigate the evidence on solutions for effective child development in the earliest years. Learn more at www.pn3policy.org.

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