Low-Income Families and the Cost of Child Care

State Child Care Subsidies, Out-of-Pocket Expenses, and the Cliff Effect

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High prices can make it very difficult for low-income families to access reliable child care, particularly in formal settings (Sandstrom, Giesen, and Chaudry 2012). The average annual price of full-time care for an infant in a child care center ranges from $4,600 in Mississippi (about 30 percent of annual full-time minimum-wage earnings) to $15,000 in Massachusetts (roughly equal to annual full-time minimum-wage earnings; see Child Care Aware of America 2012).

Child care subsidy programs such as those funded under the Child Care and Development Fund (CCDF) help low-income families pay for care. For families that obtain subsidies, child care assistance programs cover some or all of the price of care, with families contributing a copayment. Very low income families are usually assessed a very low copayment, sometimes equal to zero. As family income increases, the amount of the copayment increases. Once income exceeds a certain limit, which varies by state and family size, families are no longer eligible for subsidized care. State copayment systems vary widely on a number of factors, including minimum and maximum copayments, how copayments increase as family income rises, and the amount paid by families whose income is approaching the subsidy income limit.[1] All these factors affect out-of-pocket child care costs for subsidized families.

In this paper, we first give an overview of CCDF child care assistance, touching briefly on how certain eligibility policies vary across states. Next we discuss the full, unsubsidized out-of-pocket cost of child care as well as the amount families receiving child care assistance pay. We then turn to the focus of the analysis: how subsidized families' costs rise with increases in income, up to the point where families no longer receive assistance and become responsible for paying the full amount charged by providers. At this point, families may see relatively small increases in income coupled with large increases in child care costs, sometimes referred to as the "cliff effect." We examine selected states as examples of how families' child care costs can change depending on a state's assistance policies. This analysis uses data from the CCDF Policies Database, focusing on state policies as of October 1, 2011 (Giannarelli et al. 2012).

This analysis looks at a hypothetical family and child care provider, using state-defined maximum reimbursement rates as a proxy for the full price of care. Real-life experiences of families both on and off child care assistance programs vary depending on family characteristics and the

prices charged by the child care providers they choose upon leaving the subsidy system. Nevertheless, the analysis shows that many families who become ineligible for child care subsidies due to increased earnings face substantial increases in child care expenses. Subsidized families using center-based care who want to continue using the same care after losing the subsidy would see their expenses more than double in some states. In other states, because copayment amounts are higher, the cliff effect is lower.

What Is CCDF, and Who Is Eligible?

CCDF provides federal block grant money to the 50 states, five territories, and the District of Columbia in an effort to reduce the cost burden of child care for low-income families.[2] Under the block grant, states receive funds from the federal government and, within broad federal guidelines, are given discretion to use those funds to administer their child care subsidy programs. In 2011, approximately 1.6 million children received child care subsidized through CCDF, according to the most recent preliminary data from the Administration for Children and Families.[3] Under federal CCDF guidelines, eligible families must have income below 85 percent of state median income (SMI), must have a child who is either under age 13 or under age 19 with special needs, and must have an approved reason for needing child care (usually either work or school).

Although federal CCDF guidelines establish an overall maximum income limit of 85 percent of SMI, states may establish lower income limits, and, in some cases, states choose to establish different income limits for initial and continuing eligibility. Initial income limits are used to determine eligibility for families newly entering the subsidy program, while higher continuing income limits are used to assess ongoing eligibility for families already participating in the program. By establishing continuing eligibility thresholds in addition to initial eligibility thresholds, states allow subsidized families additional leeway to work toward increasing income without losing child care benefits.

In addition to establishing income eligibility thresholds, states establish several other policies within the broad federal guidelines, including the amount providers are reimbursed and what families pay in out-of-pocket expenses.

What Is the Full Price of Care?

The price of child care varies by many factors. As seen in the opening examples of Massachusetts and Mississippi, out-of-pocket expenses for child care can vary widely across states, from rural to urban areas, or even from neighborhood to neighborhood. Within an area, prices may be higher for child care centers versus family child care homes, or for younger children versus older children.

For this analysis, we use the states' maximum reimbursement rates as a proxy for the full price of child care without subsidy assistance. Maximum reimbursement rates are preestablished rates that subsidy programs use to compensate participating child care providers. The rates vary by state and often by local region as well. They can further vary depending on type of care, quality ratings or certifications, amount of care, and the age of the children in care. Maximum reimbursement rates are based on market-rate survey information for the price of child care in a particular area. While states are encouraged to establish rates at the 75th percentile of the current market rate, states often set rates lower than this because of budget constraints and competing needs (Rohacek 2012).

The rates used for the CCDF program often understate the true price of child care (Mezey et al. 2002); however, using those rates allows us to make general comparisons across states and look at the potential financial impacts on families that transition from subsidized care to paying the full price of child care at the going market rate. In reality, what an unsubsidized family pays for care may be higher or lower than a particular maximum rate depending on the type of provider a family chooses (e.g., center-based care vs. care provided in the child's home). Additionally, families may be using higher-tiered providers (providers meeting additional quality standards) under the subsidy program, but they may switch to a lower-tiered provider when they no longer qualify for subsidies. Because not all states have tiered rates, we use the base, or lowest reimbursement rate, for licensed centers, licensed family child care homes, and in-home providers for our analysis.[4]

How Much Do Families Receiving Child Care Subsidies Pay?

Federal rules require states to establish their own copayment policies within the broad federal guidelines. States generally vary their copayments by family size and income, and they have considerable flexibility in developing the method for calculating copayments. States determine exactly how much they will require families to pay at different income levels; how to vary

copayments for families with multiple children in care, children with special needs, or needing care only part time; and whether to exempt some families from paying a copayment.

The variation in copayment policies across states leads to different experiences for families depending on the family's state of residence. For example, across the states, a family of three, with two children and a single parent earning approximately $12,500 a year (roughly the earnings of a minimum-wage worker at 30 hours a week), would pay a monthly copayment ranging from $0 in 13 states to $156 in Louisiana.[5] That same family, if earning $30,000 annually, would pay a monthly copayment ranging from $69 in Wyoming to $945 in Hawaii.

How Do Families' Child Care Costs Rise with Income?

Generally speaking, as a family's income increases, the family is expected to pay a larger portion of the total price of care. How copayments change as family income rises varies significantly by state. Additionally, while small income increases may lead to relatively small increases in copayments, once a family's earnings exceed the income eligibility threshold for that state's CCDF program, the family must pay the entire price of care. At this point, families may face a very large increase in child care expenses, depending on what type of care is sought post-subsidy.

To illustrate how these copayments and costs change between states, we consider a prototypical family consisting of a single parent with two children, ages 2 (35 months) and 4 (59 months), without special needs, enrolled full time in center-based care. In cases where the state uses both initial and continuing eligibility thresholds, we assume the family enters the program using the initial income limit and exits the program after reaching the higher continuing eligibility limit.

If the family enters the subsidy program earning $12,500 annually, the monthly copayment ranges from $0 in 13 states to $156 in Louisiana, with a median copayment of $43 (approximately 4 percent of monthly income), depending on where the family lives. If the family's annual income increases to $15,000 while receiving the subsidy, the median monthly copayment rises to $65 (approximately 5 percent of monthly income; see Giannarelli et al. 2012).

The income level at which the family would no longer qualify for subsidies varies greatly depending on where the family lives. The highest annual income the family could earn and still qualify for subsidies ranges from approximately $22,000 in Nebraska to $71,500 in Massachusetts, with a median across states of roughly $35,000. Looking at the maximum amount the family will pay

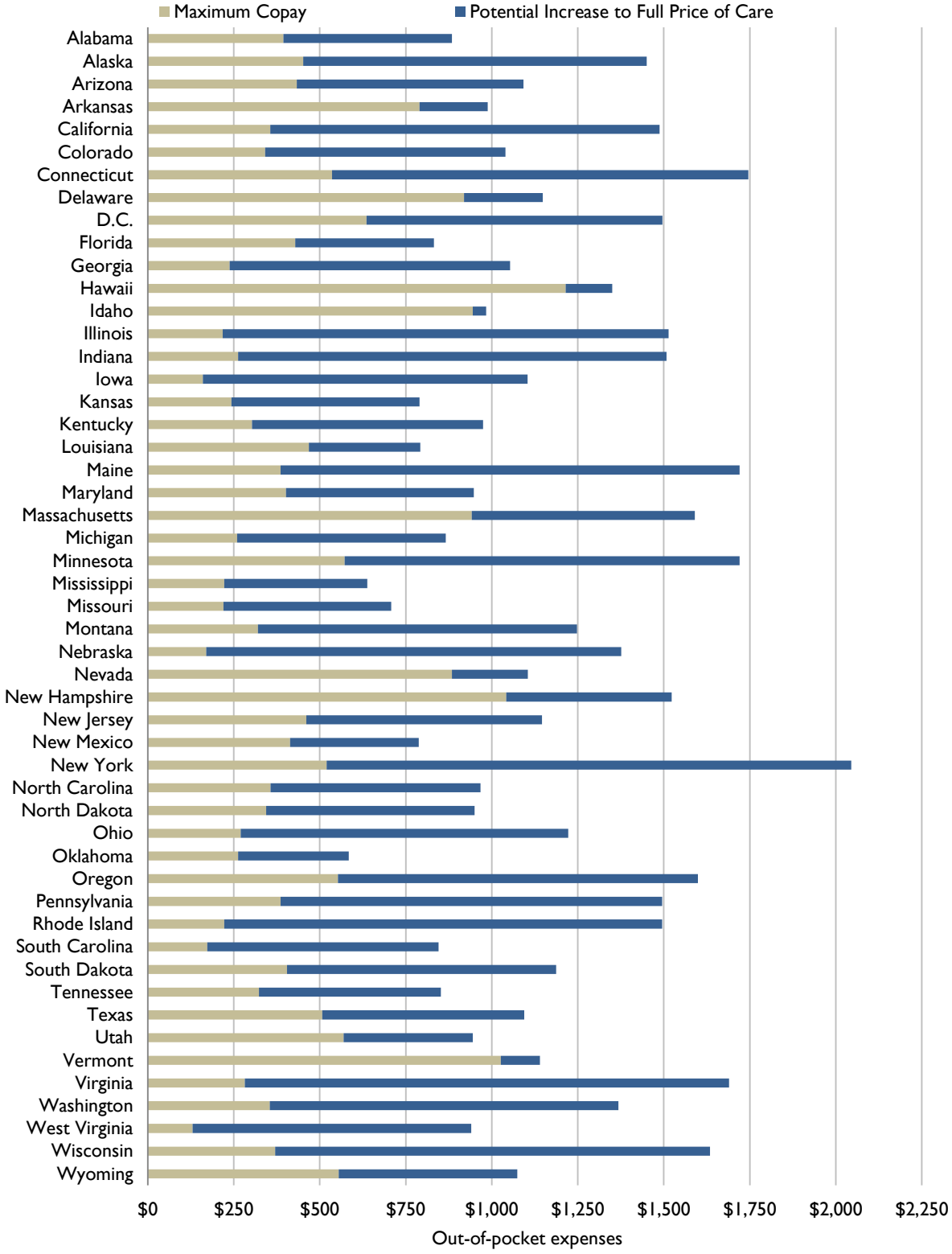
at the highest point of eligibility, monthly copayments range from $130 in West Virginia to $1,215 in Hawaii, with a median across states of $386 (figure 1).

Once the family earns $1 more than the state's income limit, the family no longer qualifies for assistance, and the monthly expense for a child care center (using state maximum reimbursement rates as an approximation of the price) ranges from $584 in Oklahoma to $2,045 in New York.[6] If we compute the family's out-of-pocket expense as a percentage of family income just $1 over the eligibility limit, the full cost of center-based care post-subsidy ranges from 20 percent of monthly income in Oklahoma to 74 percent of monthly income in Nebraska.[7] Figure 1 illustrates the copayment amount at the highest eligibility level as well as the full reimbursement rate, or the potential cost for families that no longer qualify for assistance. The cliff effect, or potential increase in the monthly child care cost once the family no longer qualifies for assistance, ranges from as little as $39 a month in Idaho to as much as $1,525 in New York.

In reality, many families may lose assistance before reaching the highest allowable income levels. For example, families at lower income levels may lose subsidies because they do not complete the recertification process. Additionally, in states with limited funding, if a family loses priority under a particular status (i.e., Temporary Assistance for Needy Families [TANF] or Transitional Child Care), the family may then be classified under a different, non-priority status for which there is limited funding and, therefore, moved to a waiting list. When families with lower incomes, and therefore lower copayments, leave the assistance program before reaching the income eligibility limits, the cliff effect may be much larger as the families go from paying a lower copayment than seen in figure 1 to paying the full price of child care.

Figure 1. The Cliff Effect

Maximum Copays and the Full Price of Center Care, Monthly Dollar Amounts



Source: The CCDF Policies Database, 2011 data.
Note: Amounts shown for a single parent with two children, ages 2 and 4.

To more closely examine how a family's child care expenses increase as income increases, we look at a family of three's experience in six states: California, Georgia, New Jersey, Idaho, New Hampshire, and Washington. These states represent a mix of copayment policies and schedules, demonstrating how a family's experience varies with location. For each state, we show how copayments for care increase with income, the amount of the family copayment at the highest eligibility threshold, and the full price of care (as approximated by the maximum reimbursement rates). Because a family may choose more affordable child care options once it is no longer eligible for subsidies, we show the price of care for family child care homes and in-home care in addition to the price of center-based care.[8]

It is important to keep in mind that families exiting the subsidy program may face higher or lower expenses than those discussed in this paper. Once families are faced with the full price of care, they may make different choices, such as finding informal arrangements for child care. Providers' actual prices may be higher or lower than the reimbursement rates used by the subsidy program, and they may choose to offer discounts to families with multiple children in care.

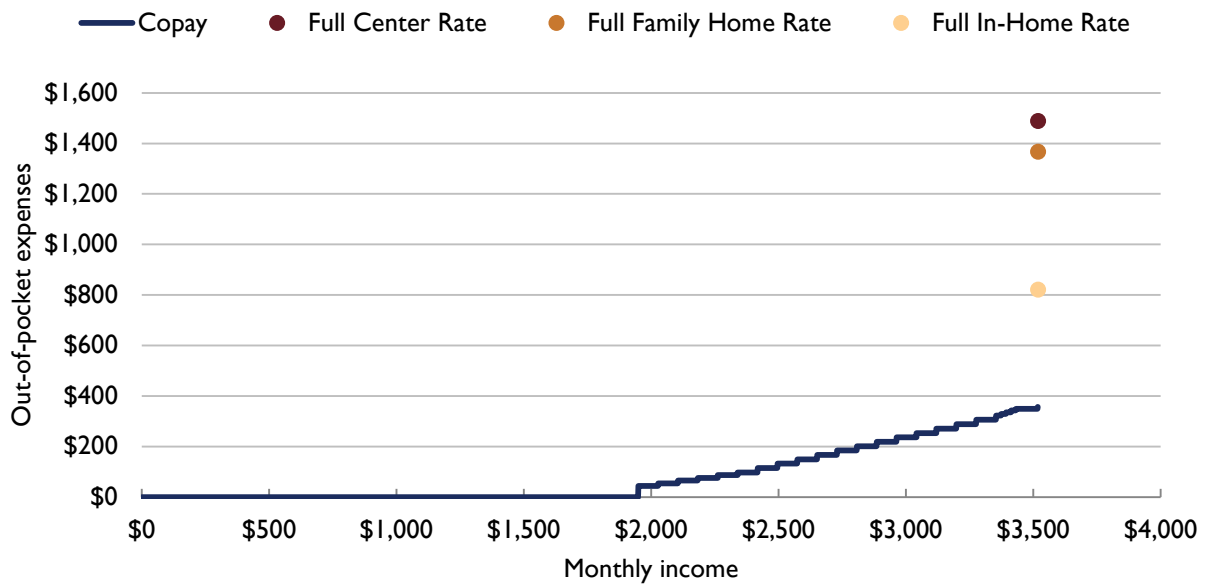
California

California's copayment schedule establishes dollar amounts that are charged to families in different income ranges. As the family's income crosses specific income thresholds, the family faces higher copayments. The copayment does not vary based on the number of children in care.

California's copayment amounts remain $0 for families earning less than $1,950 monthly and increase at regular intervals thereafter (figure 2). The increases are relatively small, allowing families room to adjust to the increased payment that accompanies a rise in income. However, once the family's income exceeds the $3,518 eligibility threshold, a family whose children remained in a child care center would face a 318 percent increase in child care expenses; the cost of care would increase by 283 percent if the children moved to a family child care home, and expenses would increase by 130 percent if the family began to use informal care in the child's home. (All these cost estimates use the state's maximum reimbursement rates for each type of care.)

Some of the increase in the price of care we see when the family is no longer eligible for subsidies stems from the fact that while the state's copayment schedule does not differ for families with one child versus families with two children, the number of children very much factors into the price of care at the market rate.

Figure 2. California
Changes in Family Copayments as Income Increases



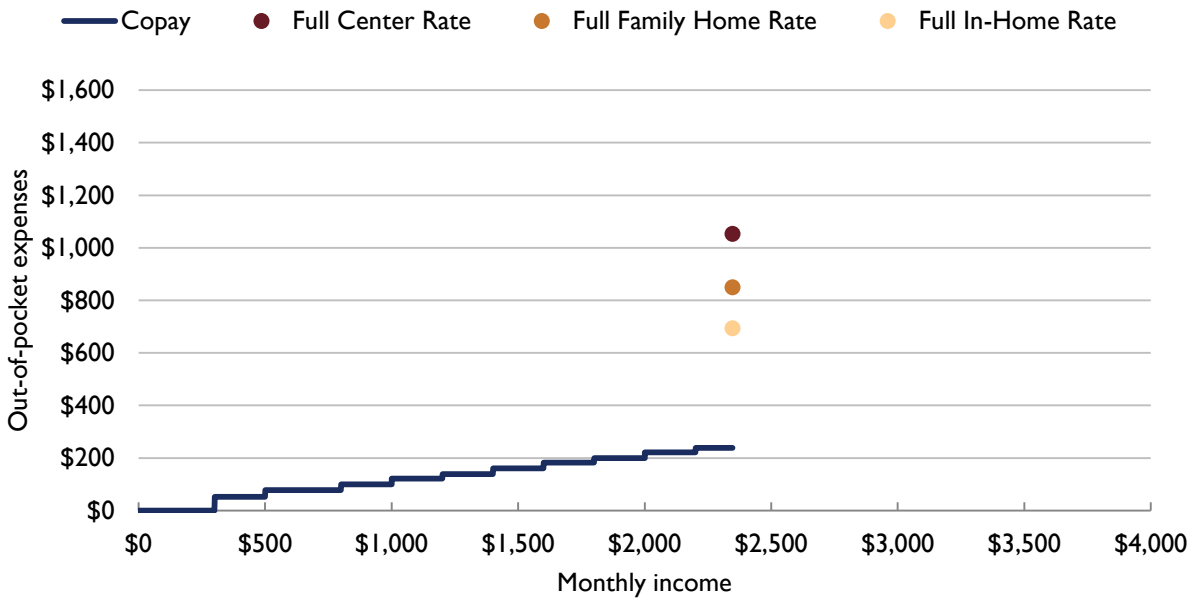
Source: The CCDF Policies Database, 2011data.

Georgia

Like California, Georgia's copayment schedule establishes dollar amounts that are applied to different income ranges. Unlike California, however, the copayments are adjusted for families with multiple children in care. The state uses separate copayment schedules for families with two or more children in care, and these copayment amounts are higher than the amounts used for families with one child in care. Additionally, Georgia's income eligibility threshold is much lower than California's.

Georgia's copayment increases are small and occur at somewhat regular intervals, but these increases begin lower on the income scale compared with California's copayments (figure 3). The cost of care increases significantly once the family no longer qualifies for subsidies, with the highest increase (342 percent) seen for center care.

Figure 3. Georgia
Changes in Family Copayments as Income Increases



Source: The CCDF Policies Database, 2011 data.

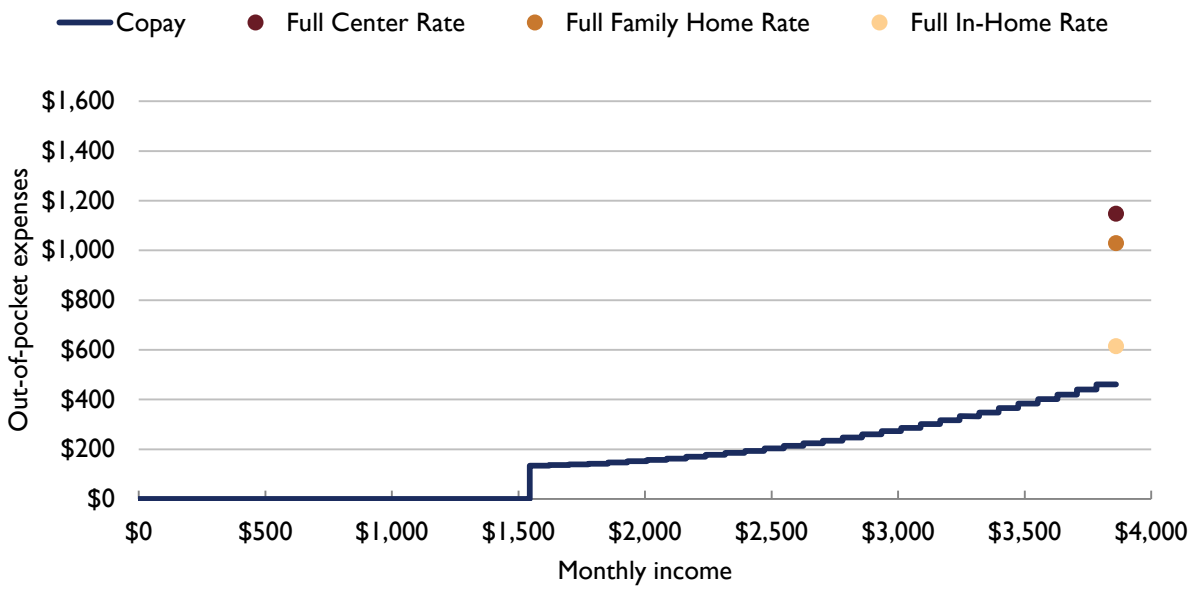
New Jersey

Like Georgia, New Jersey's copayments are a dollar amount that varies across different income ranges and are adjusted when additional children receive care. However, rather than establishing a second copayment schedule when multiple children need care, New Jersey determines the additional

copayment based on a percentage of the first child's copayment. In the case of a second child needing care, the copayment is 75 percent of the first child's copayment.

The copayment in New Jersey remains $0 for a family earning up to $1,544 per month, and gradually increases as the family's income continues to rise (figure 4). As in California and Georgia, the price of care increases significantly once the family is no longer eligible for subsidies. But, the percentage increase is less severe (148 percent for center care) for families in New Jersey.

Figure 4. New Jersey
Changes in Family Copayments as Income Increases



Source: The CCDF Policies Database, 2011 data.

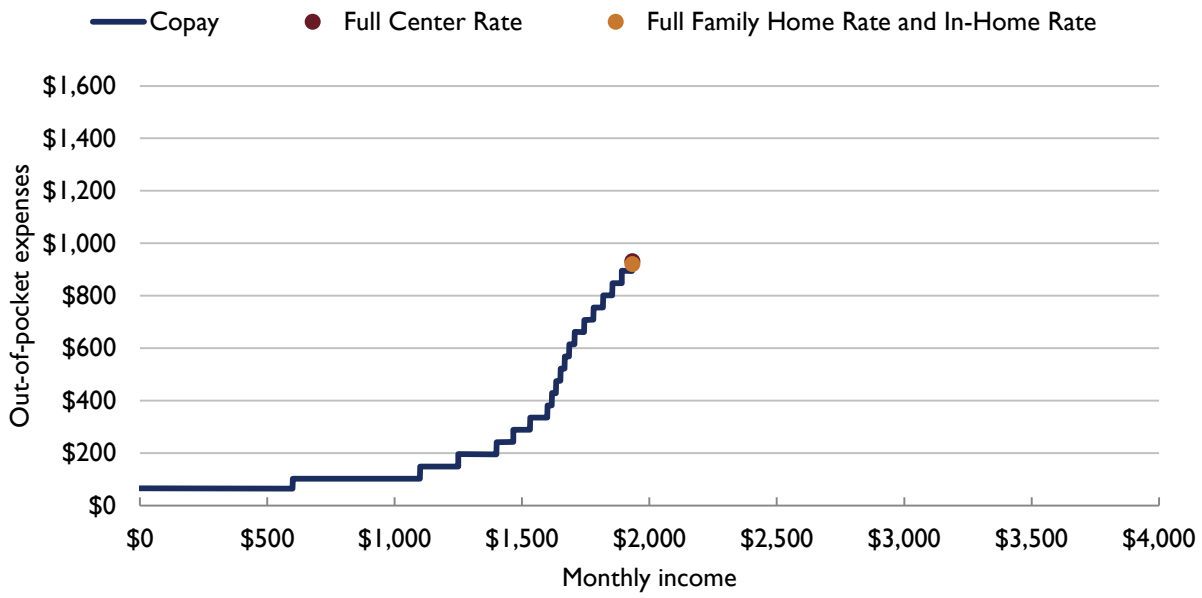
Idaho

In Idaho, copayments are based on the price of care, with families in different income ranges paying different percentages of the price. For example, if a family's monthly income is between $0 and $599, the family pays 7 percent of the monthly child care cost; if a family's monthly income is between $600 and $1,099, the family pays 11 percent. Above $1,100, the percentage increases rapidly with income until reaching 100 percent of the monthly child care costs when income reaches $1,933. Because the copayment is based on a percentage of the price of care, families pay more if more than one child is receiving care, and if the children are in a more expensive type of care (e.g., center care compared with a family child care home). For this analysis, the copayments represent a percentage

of the price for center-based care. Like Georgia, Idaho's income eligibility threshold is lower than the other highlighted states.

The copayment amount starts off a bit higher for Idaho than for California or Georgia, but it remains relatively low until roughly the $1,200 mark (figure 5). At that point, the copayment begins to increase fairly quickly, with a steep incline between $1,500 and $2,000 monthly income. The amount of the maximum copayment for center care comes very close to the full price of care for all three child care types, with the percentage increase equaling just 4 percent for center care and less than 3 percent for family child care homes and in-home care. Compared to some states, this copayment system provides lower subsidy values in the higher income ranges. There is very little difference between the family's copayment at the higher income ranges and the full price of care, but a family faces a steep rise in copayments once its income reaches $1,600.

Figure 5. Idaho
Changes in Family Copayments as Income Increases



Source: The CCDF Policies Database, 2011 data.

New Hampshire

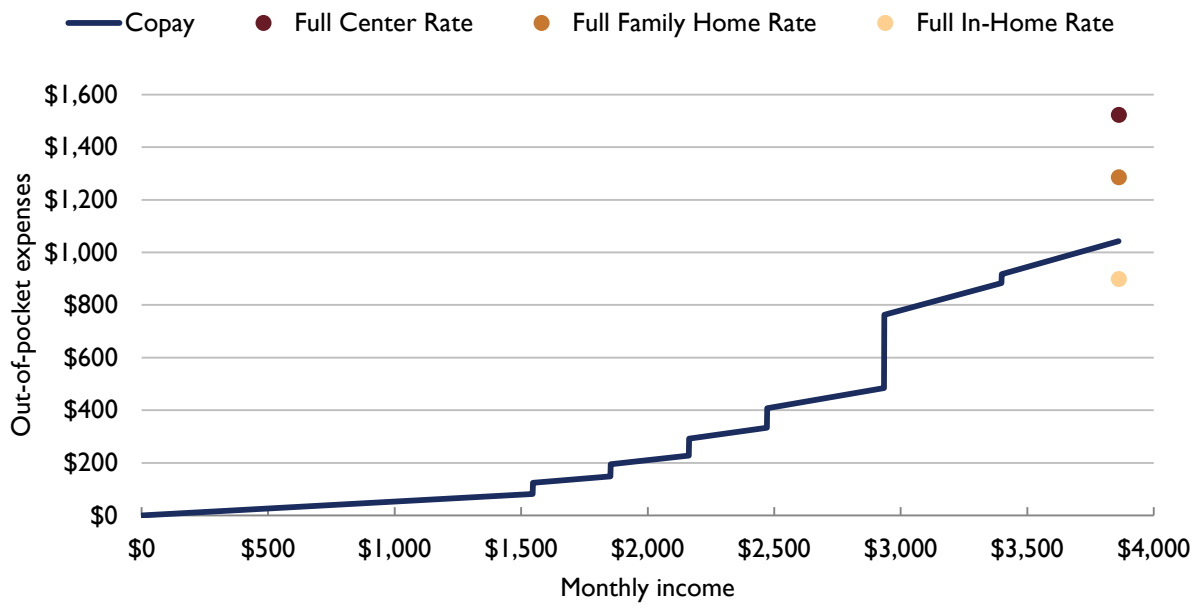
Copayments in New Hampshire are based on a percentage of income that varies across income ranges. For example, if a family's monthly income is between $0 and $1,545, the family pays 5.25 percent of its monthly income as a copayment; if a family's monthly income is between $1,546 and $1,853, the family pays 8 percent of its monthly income as a copayment. Like California, New

Hampshire does not adjust copayments based on the number of children in care; therefore, the share of income the family pays does not increase if there are two or more children in care.

New Hampshire's copayment amounts remain low with steady increases until just after the $1,500 income mark, at which point the copayment amount moves into the next percentage bracket (figure 6). The family's copayment amount jumps substantially at the $3,000 mark, and the final copayment is much closer to the full price of center-based or family home care in New Hampshire than in California or Georgia. As with Idaho, although this copayment system may give families more of a chance to adjust to higher child care prices, New Hampshire copayment amounts overall are higher than in some other states, and there are bigger jumps in copayment amounts within the eligible income ranges.

Unlike the other states discussed, the full price of in-home care in New Hampshire is lower than the maximum copayment for families using center care under the subsidy program. Therefore, families that are no longer eligible for the state's CCDF program could find informal care within the price range they are used to paying for center care until such time as they can afford family home care or center care at the market rate.

Figure 6. New Hampshire
Changes in Family Copayments as Income Increases



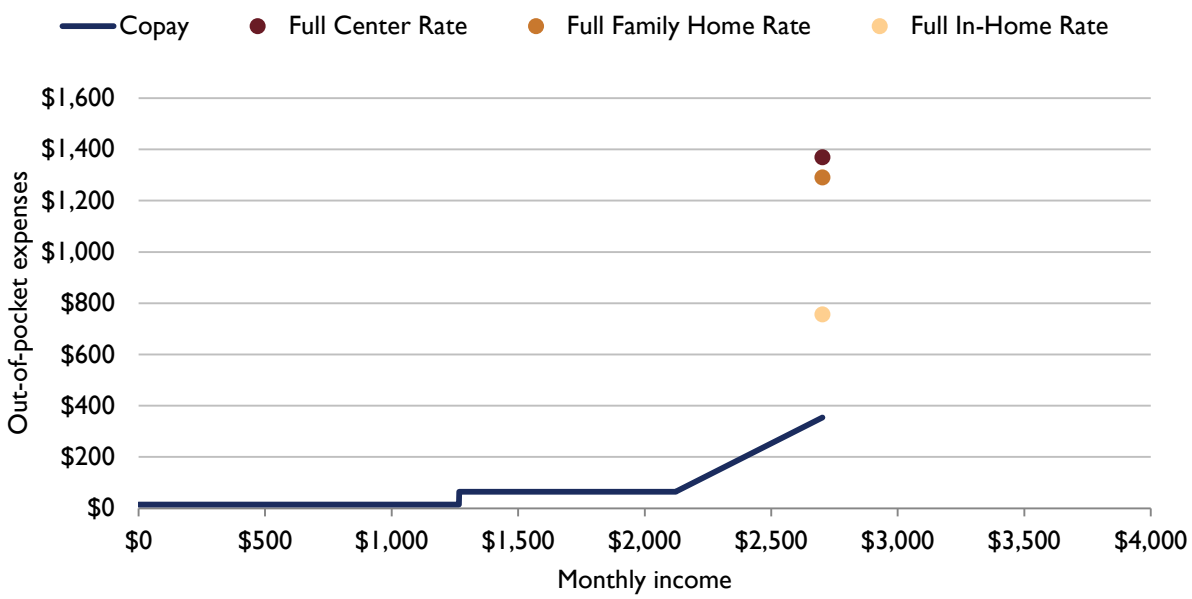
Source: The CCDF Policies Database, 2011 data.

Washington

Washington uses a more complex copayment calculation than the other states. Families with income below 137.5 percent of the federal poverty guidelines pay preestablished dollar amounts, either $15 monthly for families with monthly earnings less than $1,267 or $65 monthly for families with monthly earnings of $1,267 to $2,123. Once the family's income exceeds 137.5 percent of the federal poverty guidelines, the state uses a formula that gradually increases the copayment amount as income rises.

Copayments in Washington remain relatively low for families earning less than $2,124 a month (figure 7). Once family income reaches $2,124, the copayment gradually increases with each additional dollar of earnings. Though Washington's copayment system is unique in how the copayments are calculated, as in many other states, families see a significant jump in prices once they no longer qualify for subsidies.

Figure 7. Washington
Changes in Family Copayments as Income Increases



Source: The CCDF Policies Database, 2011 data.

Considerations for Establishing Child Care Subsidies

State copayment policies demonstrate the trade-offs states must consider when determining how to serve families in need of child care assistance. The different copayment systems represent different approaches: either serving more low-income families but with somewhat lower benefit amounts (higher copayments), or providing higher benefits (to keep copayments lower) but with families facing larger increases in out-of-pocket expenses when they no longer qualify for subsidies. Additionally, setting lower eligibility thresholds gives states more funds for serving very low income families, but families who increase their earnings are more likely to become ineligible.

In some states, families see only small increases in copayments as their income increases, and copayments are kept relatively low across the life of the subsidy. In these same states, families may see much larger increases in child care expenses when they no longer qualify for subsidies. In other states, copayment amounts increase significantly over the life of the subsidy, and families may qualify for subsidies at higher income levels. In these states, families may struggle with the high copayment amounts while in the assistance program, but they may also be more prepared for the costs they face once they no longer qualify for subsidies.

There is no perfect set of decisions for states to make as they set their child care policies. However, states should consider the existence and magnitude of cliff effects along with the adequacy of subsidies for low-income families as they develop their child care policies and policies related to family self-sufficiency.

Notes

[1] The state policies, copayment amounts, and reimbursement rates referenced in this brief are taken from the OPRE-funded CCDF Policies Database. These policies and more detailed policy information are available from http://www.urban.org/center/ibp/Projects/The-CCDF-Policies-Database.cfm.

[2] For the purposes of this report, we examine only the 50 states and the District of Columbia. Information for the territories and outlying areas is available from the CCDF Policies Database.

[3] "2011 CCDF Data Tables (Preliminary Estimates)," US Department of Health and Human Services, Administration for Children and Families, Office of Child Care, May 3, 2013, http://www.acf.hhs.gov/programs/occ/resource/fy-2011-data-tables-preliminary.

[4] The maximum reimbursement rates used here may also somewhat overestimate the full price of care for a family since the rates are based on the full rate for each child. In reality, providers may choose to discount rates for families with multiple children in care. Because different providers use different discounts, or choose not to discount rates, we did not include discounts for additional children in care for this analysis.

[5] Because some states set their state minimum wage above the federal minimum wage, we chose the highest state minimum wage figure as the starting point in order to create a feasible starting point scenario for comparison across all states.

[6] Throughout this paper, the reimbursement rates for New York represent the rates used in New York City, Bronx, Kings, Queens, and Richmond.

[7] This comparison assumes the family continues to use the same type of child care (center-based care). In reality, once a family no longer qualifies for assistance, families often turn to more affordable, informal child care options, such as care provided in the child's home or in a relative's home. See Sandstrom et al. (2012).

[8] As defined for the CCDF Policies Database, family child care homes are usually licensed or accredited residential child care facilities. In-home providers usually provide unregulated care in the child's home.

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