The 2017-18 Budget:

Analysis of Child Care and Preschool Proposals

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LAO

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Overview of Governor's Budget

Governor's Budget Includes $3.8 Billion for Child Care and Preschool Programs. The Governor's budget augments child care and preschool programs by a total of $76 million (2 percent) from the revised 2016-17 level. This augmentation primarily supports the full-year cost of the Regional Market Rate and State Preschool slot increases initiated last year pursuant to a multiyear budget agreement. Though the Governor proposes to fund these parts of the multiyear agreement, he does not fund other parts. The Governor also makes caseload changes for CalWORKs and non-CalWORKs child care programs and increases Transitional Kindergarten funding. Under the Governor's budget, proposed funding would support an estimated 437,000 child care and preschool slots.

Preschool

Governor Proposes Changing Certain Requirements for Certain Preschool Providers. The Governor also proposes several preschool-related policy changes. Specifically, the Governor proposes to allow part-day State Preschool programs to serve children with special needs from families above the income threshold as long as all eligible and interested children are served first. The Governor also makes several proposals intended to more closely align State Preschool and Transitional Kindergarten by modifying certain licensing, staffing, and program duration requirements.

Concerns With Preschool Proposals. We are concerned that allowing State Preschool programs to serve children above the income threshold would displace low-income children who are currently eligible but unserved. Additionally, we are concerned that the Governor's other preschool proposals make an already complicated system more complicated, without creating much alignment between programs.

Recommend Different, More Holistic Approach. We recommend the Legislature ensure already eligible children are served before expanding preschool eligibility. We also recommend the Legislature reject most of the preschool alignment proposals and take a more holistic approach. Under such an approach, the Legislature would consider how best to serve four-year olds, including what eligibility criteria, program standards, and funding levels it desired for these children. Making these decisions in tandem would promote greater coherence.

Quality Improvement Activities

California Department of Education (CDE) Recently Submitted Revised Quality Improvement Expenditure Plan. The federal government requires California to spend a certain amount each year on activities to improve the quality of child care and preschool. In 2016-17, the state spent $78 million (ongoing) to support about 30 quality improvement programs—some of which are run at the county level and others at the state level. As required by the *2016-17 Budget Act*, CDE submitted a revised quality improvement expenditure plan in February 2017. The revised plan leaves virtually all existing programs in place but eliminates one program and shifts a small portion of funding away from eight programs to create a $5.4 million Quality Rating and Improvement System (QRIS) block grant for child care providers serving infants and toddlers. Block grant funds would be used to rate the quality of child care providers and support providers in achieving and maintaining high ratings.

Current System Has Several Serious Shortcomings. The state's current quality improvement plan has several major shortcomings: existing county-level activities can lack coordination and funding can be difficult to target to the highest priorities, little information is available on the effectiveness or efficiency of existing state-level programs, and funding disproportionately serves providers that already meet higher standards. The department's revised plan addresses a few of these issues by giving county-level entities somewhat more flexibility in the activities they undertake and allowing them to serve some providers that do not meet higher standards. The proposal, however, restricts support to a small share of providers statewide (only those participating in QRIS) and does nothing to address the other shortcomings.

Recommend Shifting More Funding Into a New County Block Grant and Reassessing Most State-Level Programs Over Next Several Years. We recommend repackaging $21 million from seven county-level programs into a new county block grant that would allow county-level agencies to support any provider serving subsidized children. We recommend funding the remaining state-level programs as budgeted but hiring an independent evaluator to assess the cost-effectiveness of these programs over the next several years. The Legislature could revisit funding levels for these programs in the future based on the results of the evaluations.

Alternative Payment (AP) Agencies

State Funds AP Agencies to Administer Most Voucher-Based Programs. The state allocates AP agencies operational funding equal to 21 percent of the voucher payments they make to child care and preschool providers. The AP agencies' primary activities involve determining family eligibility and paying providers.

Current Funding Model Not Tightly Linked With Underlying Cost Drivers. AP agencies' costs are driven primarily by their caseload and the wages they offer their staff. Although the current funding model has some connection to these underlying cost drivers, some components of the model are not tightly linked to costs. Most notably, an AP agency working with providers that serve a larger share of infants and toddlers receives more operational funding than an agency working with providers serving older children, even though the amount of associated AP workload is the same. Agencies' funding levels also fluctuate when provider rates change, despite no changes in associated AP workload.

Recommend Adopting a Regionally Adjusted Per-Child Funding Model. We recommend the state provide operational funding to AP agencies based on the number of children served. We recommend the state adjust these rates based on regional wage data and phase in the new system over several years.

INTRODUCTION

In this report, we analyze the Governor's child care and preschool proposals. The report has six main sections. In the first section, we provide background on child care and preschool programs in California. In the second section, we provide an overview of the Governor's child care and preschool proposals. In the third section, we analyze the Governor's preschool proposals and make associated recommendations. In the following two sections, we provide in-depth analyses of (1) the state's various quality improvement activities and (2) Alternative Payment agencies, which administer certain child care programs. The final section consists of a summary of the recommendations we make throughout the report.

CHILD CARE AND PRESCHOOL IN CONTEXT

In this section, we provide a high-level overview of the child care and preschool system in California and then discuss eligibility and access, settings and standards, funding, and trends over the last decade.

Overview

Three-Fifths of Children Under 13 in California Live in Families Where Parents Work or Are in School. According to 2015 American Community Survey data from the U.S. Census Bureau, 6.6 million children in California are under the age of 13. Of these children, about 60 percent live in families where all parents or guardians work or are in school. As a result, many families must find child care arrangements for their children. Children may be cared for in settings licensed by the state or in non-licensed settings, such as the home of another family member, friend, or neighbor.

California Subsidizes Child Care and Preschool for Some Families. In 2016-17, California allocated nearly $3.7 billion to provide 434,000 children with subsidized child care and preschool. Of these children, 12 percent are birth through age 2, 59 percent are ages 3 and 4, and 29 percent are age 5 or older. The funding primarily benefits children from low-income, working families. As Figure 1 (see next page) shows, the funds are spread across nine state programs. Three programs relate to California Work Opportunity and Responsibility to Kids (CalWORKs), focusing on families engaged in or transitioning out of welfare-to-work activities. The remaining programs are designed for other low-income, working families. In addition to the programs that directly provide subsidized child care and preschool, California provides two tax benefits. The Child Care and Dependent Tax Credit supports about 180,000 tax filers who pay for child care or preschool with an annual tax credit of up to $516 per filer. The Employee Child and Dependent Care Benefit Exclusion allows taxpayers to exclude up to $5,000 of income per year from tax calculations if their employer offers a payroll deduction program for child care expenses. These provisions primarily benefit families with incomes over $50,000.

Federal Government and Local Agencies Also Subsidize Programs. The federal government subsidizes child care and preschool through Early Head Start (serving children birth through 2) and Head Start (serving children ages 3 through 5). In 2015-16, the federal government allocated roughly $1 billion to providers in California that served

Figure 1

State's Child Care and Preschool Programs

Program	Description
CalWORKs Child Care	
Stage 1	Child care becomes available when a participant enters the CalWORKs program.
Stage 2	Families transition to Stage 2 child care when the county welfare department deems them stable.
Stage 3	Families transition to Stage 3 child care two years after they stop receiving cash aid. Families remain in Stage 3 until the child ages out (at 13 years old) or they exceed the income eligibility cap.
Non-CalWORKs Child Care	
General Child Care	Program for low-income, working families that subsidizes care provided in licensed settings.
Alternative Payment	Program for low-income, working families that subsidizes care provided in licensed and non-licensed settings.
Migrant Child Care	Program for migrant children from low-income, working families.
Care for Children With Severe Disabilities	Program for children with severe disabilities living in the Bay Area.
Preschool	
State Preschool	Part-day, part-year program for low-income families. Full-day, full-year program for low-income, working families.
Transitional Kindergarten	Part-year program for four-year olds with birthdays between September 2 and December 2. May run part day or full day.

109,000 children through these programs. The federal government also has a child care tax credit, which provides about 670,000 Californians with an annual credit of up to $6,000. Finally, some school districts support preschool programs using federal Title I funds, special education funding, or local funds.

Eligibility and Access

Below, we discuss eligibility criteria and access to the state's various child care and preschool programs.

Eligibility Criteria

For Most Programs, Eligibility Based on Income and Working Status. To be eligible for subsidized child care, children must be under the age of 13 and from a family with an income below 70 percent of state median income (SMI) as calculated in 2007 ($42,216 for a family of three). Parents also must demonstrate a "need" for care during the hours that the state subsidizes—for example, they must be working, looking for work, in school, or unable to care for their child for medical reasons. Homeless children and children identified as being (or at risk of being) abused or neglected also are eligible for child care, regardless of parent income and work status.

Additional Eligibility Criteria for Migrant Child Care and Care for Children With Severe Disabilities. For Migrant Child Care, families must meet all the criteria for the state's child care programs as well as earn at least 50 percent of their gross income through agricultural work. To be eligible for subsidies through the Care for Children With Severe Disabilities (CCSD) program, a child must have a physical, mental, or emotional handicap of such severity that he or she cannot be served appropriately in another child care program (as determined by the individualized education program designed by a special education team). Children participating in CCSD may remain in the program until they reach 21 years of age. The CCSD program is available only in the Bay Area.

Special Rules for State's Preschool Programs. State Preschool and Transitional Kindergarten each has its own set of rules regarding the age of children served, family income, and work requirements.

- ***Age.*** State Preschool providers primarily serve four-year olds but may enroll three-year olds if all eligible and interested four-year olds have been served. School districts are required to provide Transitional Kindergarten to all children who turn five between September 2 and December 2. (Districts also can choose to serve children with birthdays between December 2 and the end of the school year, but only receive funding for these children after their fifth birthday.)

- ***Income.*** Whereas State Preschool shares the same income threshold as state child care programs, it allows up to 10 percent of children to be from families with incomes up to 15 percent above the income threshold if all eligible and interested children have been served. Transitional Kindergarten has no income-eligibility requirements.

- ***Work Status.*** To enroll their children in full-day State Preschool, families must demonstrate they have a need for care during the hours the program operates. Part-day State Preschool and Transitional Kindergarten, however, do not require families to demonstrate that they have need for care (that is, they do not need to be working or in school for their children to participate in the programs).

California's Eligibility Criteria Relatively Generous Compared to Other States. A National Women's Law Center (NWLC) survey of states from February 2016 shows that California's income-eligibility threshold results in a higher percentage of families being eligible for child care than in 41 other states. In addition to having a higher income threshold, California has fewer other eligibility restrictions than many states. For example, 22 states require parents to work a minimum number of hours per week to receive care, while 20 states cap the number of hours parents can receive child care. California imposes neither of these restrictions.

Access

CalWORKs and Transitional Kindergarten Families Guaranteed Services. By statute, the state guarantees child care subsidies for CalWORKs families from their initial participation until two years after they stop receiving cash aid (known as CalWORKs Stage 1 and Stage 2 child care). Families off cash aid for more than two years are not statutorily guaranteed child care subsidies, but the Legislature typically has funded all eligible families (through CalWORKs Stage 3 child care). California is relatively generous to its welfare-to-work population in this regard. Only 20 other states guarantee child care for welfare-to-work recipients and only 17 other states guarantee child care for families transitioning off welfare-to-work. All children eligible for Transitional Kindergarten also are statutorily guaranteed a spot in their local school district program.

All Other Families Are Prioritized Based on Income. Given state funding historically has been insufficient to serve all families eligible for non-CalWORKs child care and State Preschool programs, the state requires providers to prioritize children based on a number of factors. Providers must give first priority to children who are receiving child protective services or at-risk of abuse or neglect. Once all such children are served, providers must serve children from families with the lowest incomes. To that end, providers place interested families into income brackets and must first offer child care to all families in the lower income brackets before offering to families in higher brackets. Within each income bracket, the state requires providers to prioritize children with special needs. A family who does not immediately receive a subsidized slot may request to be placed on a provider's waiting list. In some areas, providers may work together to develop centralized eligibility lists so that a family can put its name on one list and be alerted if any slot in the area becomes available. (Every county had a centralized eligibility list between 2005 and 2010, when the state provided direct funding for the development and maintenance of these lists.)

School-Aged Children Also Can Participate in After School Programs. Families with school-aged children have access both to the child care system and various after school programs that may be funded by the state, the federal government, their school, or other organizations in their community. Families may use both after school programs and child care. For example, a family could enroll their child in an after school program during the school year and use child care during the summer and winter breaks. The nearby box describes the two major after school programs currently available to families.

Two Major After School Programs

After School Education and Safety (ASES) Program. In 2002, voters passed Proposition 49, which created the ASES program. Funded beginning in 2006-07, ASES provides $550 million annually to support after school programming for children at schools with high concentrations of low-income students. In 2016-17, ASES served about 400,000 children in kindergarten through ninth grade at 4,201 schools. The average program operates in schools where four-fifths of students are eligible for free or reduced price meals. (This threshold equates to about $37,000 per year for a family of three.) Programs must operate a minimum of 15 hours per week and must include an educational component (such as tutoring) and an enrichment component (such as art, music, physical activity, career awareness, or community service).

21st Century Community Learning Centers (21st CCLC). California also receives about $130 million for after school programs through the federal 21st CCLC program. In 2016-17, the program served about 70,000 students at 684 schools. (About 55 percent of these schools also received funding through ASES.) The average 21st CCLC program operates in schools with similar shares of low-income students as ASES. The 21st CCLC's program requirements also are very similar to ASES, with each program operating a minimum of 15 hours per week and including both educational and enrichment components. Unlike ASES, however, 21st CCLC funds can be used to run programs for high school students.

Settings and Standards

Below, we discuss child care settings and standards.

Settings

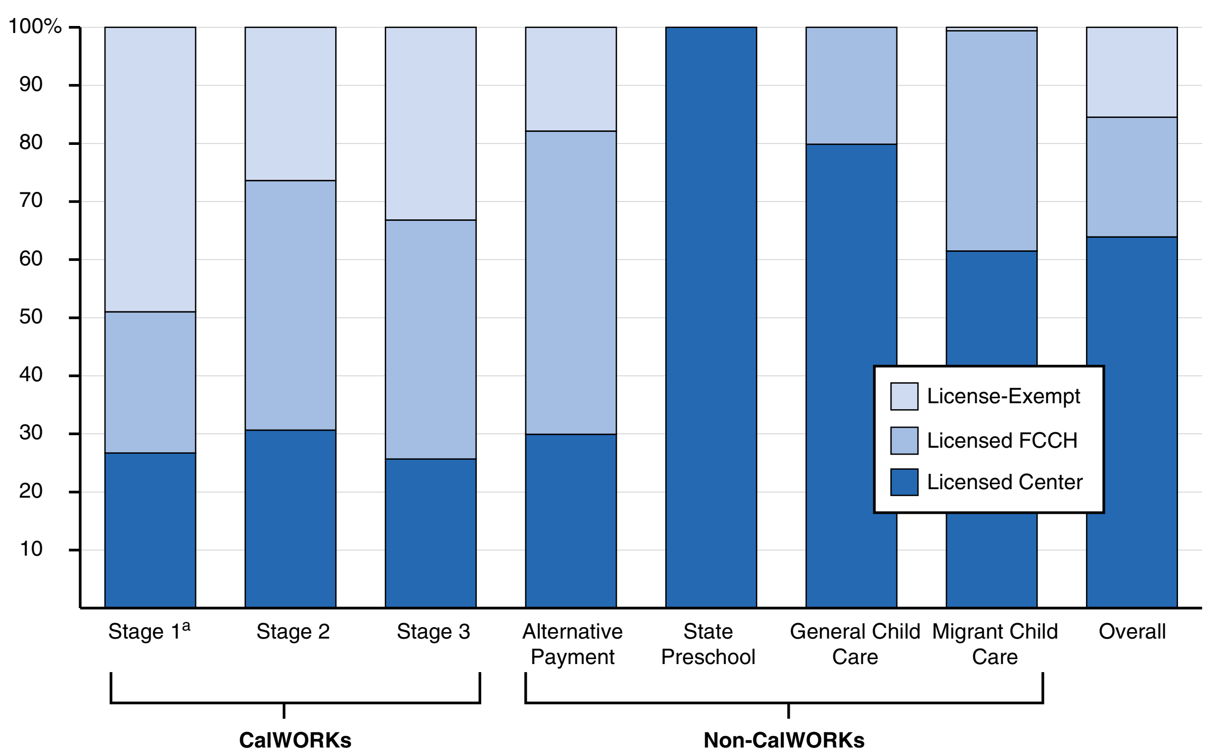
Children Receive Care in a Variety of Settings. Child care and preschool are provided in four types of settings: licensed centers, licensed family child care homes (FCCHs), license-exempt homes, and classrooms. Centers typically are run by community-based organizations or local education agencies and serve an average of about 50 children. Run by interested individuals out of their own homes (modified in certain ways to meet licensing standards), FCCHs may each serve up to 14 children. License-exempt care is typically provided by a family's relative, friend, or neighbor in the provider's private home. These providers can provide care only for one family at a time. Transitional Kindergarten programs are run by school districts in a classroom setting similar to kindergarten. These programs are not subject to licensing requirements. In 2015-16, the average kindergarten classroom had 23 students.

Use of Particular Settings Varies Across Programs. Figure 2 shows the types of settings in which subsidized children are served by the various child care and preschool programs, excluding Transitional Kindergarten. As the figure shows, 85 percent of children were served in licensed settings in 2015—64 percent in centers

Figure 2

Participation in Child Care and Preschool Programs by Setting

2015



[a] Based on 2014 data.

FCCH = family child care home.

and 21 percent in FCCHs. Although a relatively small share of children are served in license-exempt settings, the amount varies substantially by program. In CalWORKs Stage 1, for example, almost half of families use license-exempt care, whereas in the Alternative Payment program, 18 percent of children use license-exempt care. The State Preschool and General Child Care programs do not allow for license-exempt care.

Use of Particular Settings Also Varies Across Counties. The percentage of subsidized children in centers ranges from 5 percent in Mariposa County to 85 percent in El Dorado County. The percentage of subsidized children in FCCHs ranges from 10 percent in Fresno County to 80 percent in Mariposa County. Variation in use of license-exempt care is lower, ranging from less than 1 percent in Sierra County to 24 percent in San Bernardino County.

California Relies More on License-Exempt Care Than Other States. Based on preliminary federal Health and Human Services (HHS) data from 2015 (the most recent data available), California ranks 11th among the 50 states in terms of having a relatively high percentage of subsidized children in license-exempt child care. California has a relatively high percentage of children in license-exempt settings receiving care offered by relatives (such as a grandparent), ranking 10th in the nation.

Standards

Standards Vary Across Programs and Settings. As Figure 3 shows, all licensed providers, at a minimum, must meet health and safety standards. Licensed providers serving children in the CalWORKs and Alternative Payment programs (or other children not subsidized by the state) also must meet certain staff qualifications and staffing ratios, with more stringent requirements for centers than FCCHs. Compared to the CalWORKs and Alternative Payment programs, the General Child Care and State Preschool programs require somewhat higher staff qualifications and staffing ratios.

Some Programs Also Required to Include Developmental Component to Care. In addition to being subject to health, safety, and staffing standards, the General Child Care and State Preschool programs must provide children with developmentally appropriate activities. This developmental component often is referred to as "learning foundations" after the frameworks developed by the California Department of Education (CDE) for the programs. The learning foundations describe the skills that children of different ages should be able to exhibit.

Program Monitoring Varies by Provider Type. Community Care Licensing (CCL), which is part of the Department of Social Services (DSS), processes applications for child care licenses and periodically monitors all licensed entities to ensure compliance. These reviews relate to all health, safety, and staff standards. The General Child Care and State Preschool programs are subject to these CCL reviews as well as CDE reviews. The CDE reviews check that providers meet the higher staff standards and offer developmentally appropriate activities.

Transitional Kindergarten Has Different Standards and Monitoring System. Transitional Kindergarten is subject to the standards that apply to kindergarten. Specifically, Transitional Kindergarten teachers must have a multiple subject Teaching Credential. Teachers hired after July 1, 2015 also must demonstrate knowledge in early childhood education (through coursework or previous work experience). Class sizes cannot exceed 33 students, with no requirements for additional instructional aides to support teachers. As with all other school buildings, school districts are required to keep Transitional Kindergarten facilities in good repair but are not required to meet CCL health and safety standards.

Regarding program standards, Transitional Kindergarten classrooms are required to use a modified kindergarten curriculum that is age and developmentally appropriate. Transitional Kindergarten class sizes—as well as class sizes for all other grades—are reviewed as part of a school district's annual independent audit.

Federal Law Requires State to Spend a Certain Amount Each Year on Quality Improvement Activities. In 2016-17, the federal government required the state to spend $78 million on quality improvement activities. The state allocated almost half of these resources to training and professional development activities, including stipends for early educators to take more classes and direct funding for various trainings and resources. The rest of the funds supported activities such as resource and referral services for parents seeking child care, licensing enforcement, and coordination among local child care agencies.

Figure 3

Standards by Program and Setting

Infant Children (Through 24 Months Old [a])

	CalWORKs, Alternative Payment, and Certain Migrant Child Care Programs			General Child Care, CCSD, and Certain Migrant Child Care Programs
	License-Exempt	**FCCHs**	**Centers**	**Centers[b]**
Health and Safety Standards	Criminal background check. Self-certification of certain health and safety standards.	Staff and volunteers are finger printed. Subject to health and safety standards.	Same as shown for FCCHs.	Same as shown for FCCHs.
Staff Qualifications	None.	15 hours of health and safety training.	Child Development Associate Credential or 12 units in ECE/CD.[c]	Child Development Teacher Permit (24 units of ECE/CD plus 16 general education units).[d]
Staffing Ratios	May serve children from only one family at a time.	1:4 adult-to-child ratio.[e]	1:12 teacher-to-child ratio and 1:4 adult-to-child ratio.	1:18 teacher-to-child ratio and 1:3 adult-to-child ratio.
Developmental Standards	None.	None.	None.	Requires developmentally appropriate activities.
Oversight	None.	Unannounced visits by CCL every three years or more frequently under special circumstances.	Same as shown for FCCHs.	Same as shown for FCCHs, but also onsite reviews by CDE every three years (or as resources allow) and annual self-assessments.

[a] Standards for children of other ages similar to those displayed here. For General Child Care, CCSD, and certain Migrant Child Care programs, standards apply to children through 18 months old.
[b] Same standards generally apply to FCCHs serving children in General Child Care and certain Migrant Child Care programs.
[c] The Child Development Associate Credential is issued by the National Credentialing Program of the Council for Professional Recognition.
[d] The Child Development Teacher Permit is issued by California's Commission on Teacher Credentialing.
[e] Ratio applies when all children in home are infants. When mix of ages in home, can have up to 1:8 adult-to-child ratio.
CCSD = Care for Children With Severe Disabilities; CCL= Community Care Licensing; CDE = California Department of Education; ECE/CD = Early Childhood Education/Child Development; and FCCHs = family child care homes.

State Also Supports Local Quality Rating Improvement Systems (QRIS). In 2012-13, California received a $75 million four-year grant from the federal government to develop and fund QRIS. A portion of the funds went to create a common matrix that rates child care and preschool providers based on a certain set of indicators, including staff qualifications, ratios, and environment. The remaining funds went to 17 local QRIS consortia to rate programs and help those programs achieve and maintain high ratings. Subsequent state and local funding has expanded QRIS to 48 consortia serving the entire state. Each consortium is responsible for rating participating programs according to the common matrix and deciding how to assist providers. Support services vary by consortium, but typically include stipends to allow teachers to take more early education classes, coaching for staff, grants to help providers improve their classroom environment, and additional funding for highly rated sites. California is 1 of 42 states with a QRIS. Unlike most other states, however, California's QRIS is locally run, with QRIS consortia in each county conducting the ratings and deciding what kind of support will be the most beneficial to participating providers.

Funding

Below, we discuss funding sources and allocations, reimbursement rates, and family fees.

Funding Sources and Allocations

Child Care and Preschool Supported With Mix of State and Federal Funding. In 2016-17, state funding (Proposition 98 and non-Proposition 98 General Fund combined) comprised approximately 70 percent of total funding, with federal funding comprising the remainder. Federal support is provided through the Child Care and Development Fund (CCDF) and Temporary Assistance for Needy Families (TANF). Whereas TANF supports CalWORKs child care, CCDF is blended with state funding to support the state's child care and preschool programs generally. The federal law governing CCDF was recently reauthorized. The nearby box highlights substantial changes in the new act.

State Subsidizes Programs in Four Ways. The DSS provides funding for CalWORKs Stage 1 child care to county welfare departments via a "single allocation," which can be used for any combination of Stage 1 child care and welfare-to-work services. County welfare departments then use this funding to determine eligibility and issue voucher payments to the child care provider of the family's choice. For CalWORKs Stage 2, Stage 3, and the Alternative Payment program, CDE provides funds directly to Alternative Payment agencies to make child care voucher payments (with a specified share set aside to cover agencies' operational costs). For the General Child Care, State Preschool, and CCSD programs, the state directly contracts with providers to serve a specified number of eligible children. For the Migrant Child Care program, the state subsidizes care using both vouchers and direct contracts. Finally, the state provides grants to school districts for Transitional Kindergarten through the state's K-12 funding formula.

Reimbursement Rates

State Generally Funds Contract-Based Providers Using Standard Reimbursement Rate (SRR). Providers running the General Child Care, State Preschool, contract-based Migrant Child Care, and CCSD programs generally are paid using the SRR. The SRR is higher for centers than FCCHs and is adjusted to account for length of care and various characteristics of the child served—including age, limited English proficiency, or having a disability. Over the years, the state periodically has updated the SRR to reflect increasing program costs.

Federal Government Recently Reauthorized CCDBG Act With New Rules

The federal government reauthorized the Child Care and Development Block Grant (CCDBG) Act in 2014 and made substantial changes to the rules at that time. Many of these changes would require both changes in state law and additional funding. The more substantial changes include: (1) requiring states to reimburse providers based on the most recent Regional Market Rate survey, (2) requiring states to allow subsidized families to continue to receive child care until their incomes reach 85 percent of the most recent State Median Income, (3) allowing families to remain eligible for child care if changes in income and work status are minor or likely temporary, (4) requiring annual inspections of licensed and license-exempt providers who serve subsidized children, and (5) increasing the amount the state is required to spend on quality improvement activities. The state has been granted until September 30, 2018 to comply with the new rules. The consequences for failing to comply with the new requirements after that time are unclear.

State Funds Voucher Providers Using Regional Market Rate (RMR). Reimbursement rates for voucher providers and certain General Child Care providers vary based on the county in which the child is served. These reimbursement rates are referred to as the RMR and are based on regional market surveys of private providers. Like the SRR, the RMR rates vary based on the age of the child, setting, and length of care. The state also applies an adjustment factor to the RMR rates for children with disabilities. Unlike the SRR, variation in RMR rates is based on the results of the regional market survey. The RMR sets the maximum amount the state is willing to pay for a certain type of care. If a provider charges less than the maximum amount, the state reimburses the actual charge. (The state currently reimburses license-exempt providers at 70 percent of each county's maximum RMR for FCCHs.) The state often sets the RMR at a certain percentile of the survey. This percentile effectively reflects the purchasing power and amount of choice associated with a voucher. Currently, the state links the RMR to the 75th percentile of the 2014 survey, ensuring that all children have access to at least 75 percent of their local child care providers.

Most States Base RMRs on Outdated Market Information. Federal law requires states to conduct regional market rate surveys every three years, but it has not always required states to base child care rates on the most recent surveys. As a result, many states (including California) have not always updated their actual RMR ceilings to reflect the most recent survey results. For example, the state used the 85th percentile of the 2005 survey as the basis for setting rates for five years, even though more up-to-date surveys were available during this period. A February 2016 NWLC survey shows that one-third of states were using RMRs based off of market information more than five years old. Of the states that were using more recent market information, most states set the rates at or below the 75th percentile.

California Relies More on Contracts Than Other States. Preliminary federal HHS data from 2015 shows that California is 1 of 12 states that directly contracts with child care and preschool providers. Among these states, California had the fourth-highest share of child care and preschool slots funded via direct contracts. Most states rely primarily on vouchers to provide subsidized child care. In 2015, 30 states reimbursed providers using exclusively vouchers, whereas another 17 states reimbursed them using vouchers in conjunction with other payment methods, such as direct contracts. Five states provide cash directly to families either as the only funding mechanism or in combination with vouchers for providers or direct contracts.

State Funds Transitional Kindergarten Through Primary K-12 Funding Formula. Funding for Transitional Kindergarten is provided through the Local Control Funding Formula (LCFF), the state's primary school funding formula. The LCFF provides schools with base per-student funding, adjusted by four grade spans, with additional funding generated for students who are low income, English learners, or foster youth. The LCFF provides the same funding rate for students in Kindergarten (including Transitional Kindergarten) through third grade. As with Kindergarten, schools are required to offer only part-day Transitional Kindergarten. They receive the same amount of funding per student whether they run part day or full day.

Rates for Similar-Aged Children Vary by Rate System. As Figure 4 shows, annual reimbursement rates can vary substantially within the same age group and setting. For example, the RMR for centers that provide full-time, full-year care to a preschooler averages about $13,000—almost $3,000 higher than the equivalent SRR rate. Rates also differ notably for part-time, preschool-aged children in centers. The SRR rate, which funds the part-day State Preschool program to operate for 175 days a year and at least four hours per day, is less than half the rate provided for Transitional Kindergarten, a program with similar school year and school day requirements (180 days per year, 3 hours per day). The RMR for part-time, preschool-aged children in centers is $559 higher than the Transitional Kindergarten Rate, although voucher-based providers receive this level of funding based on about 250 days of care per year.

Family Fees

State Charges Fees to Some Families. In all programs except part-day State Preschool and Transitional Kindergarten, families making above 40 percent of the SMI as calculated in 2007 (about $24,000 per year for a family of three) pay a family

Figure 4

Comparing Reimbursement Rates for Centers

Annual Reimbursement Rates for Select Ages, 2016-17[a]

	Full-Time Care	Part-Time Care[b]
Infants (Birth to 18 Months)		
SRR	$17,087	$12,815
RMR averages[c]	16,973	11,903
Toddlers (18 to 24 Months)		
SRR	$14,072	$10,554
RMR averages[c]	16,973	11,903
Preschool (Ages 3-4)		
SRR[d]	$10,114	$4,386
RMR averages[c]	13,008	9,369
LCFF[e]	N/A	8,810
School-Age (Ages 6-12)		
SRR	$10,051	$7,538
RMR averages	9,408	5,993

[a] All rates reflect cost of full-year program, except for part-time preschool SRR and LCFF rates. These rates reflect 175-day and 180-day programs, respectively.

[b] SRR part-time care rates based on 4 to 6.5 hours of care per day.

[c] RMR average costs are weighted by the number of subsidized children receiving child care in each setting and county. Estimates assume half of children reimbursed at weekly rate and half at monthly rate.

[d] Displays State Preschool rates.

[e] Operated by school districts, rather than licensed centers.

SRR = Standard Reimbursement Rate; RMR = Regional Market Rate; and LCFF = Local Control Funding Formula.

fee. These fees range from $21 to $373 per month, depending on family size, income, and whether children are in part- or full-time care. In 2015-16, the state collected $59 million in family fees. The use of family fee revenue varies by program. For the CalWORKs programs, where the state subsidizes all eligible families, parent fee revenue offsets state General Fund spending. For all other programs, where the state does not serve all eligible children, state practice is for fee revenue to serve additional children.

Family Fees in California Lower Than in Many Other States. According to the NWLC, in February 2016, the average state charged $206 per month to a family of three earning about $30,000 with one child in full-time care. Such a family paid $128 per month in California, a lower monthly fee than in 40 other states. California also is one of three states that did not charge any fees to a family of three earning about $20,000 a year with one child in full-time care. The average state charged a family of this size and income level $84 a month.

Trends Over Last Decade

Funding Cut During Recession, Increased During Recovery. Figure 5 shows funding for child care and preschool programs between 2007-08 and 2016-17. Funding for child care and preschool programs decreased by roughly $1 billion between 2007-08 and 2013-14. Since that time, funding for child care and preschool programs has increased by $871 million. We discuss these decreases and subsequent increases in more detail below.

Rates Mostly Flat During Recession, Increased in Recent Years. While most child care rates were held flat during the recession, the state reduced license-exempt rates (from 90 percent to 60 percent of the FCCH rate). The state also reduced the rates for Alternative Payment agencies' operational expenses by 8 percent. Starting in 2014-15, the state provided three consecutive rate increases, with spending on rates in 2016-17 $397 million higher than in 2013-14. The state augmented the SRR by 17 percent over these three years ($198 million). The state also increased the RMR three times, most recently updating to the 75th percentile of the 2014 survey ($162 million). In addition, the state increased license-exempt rates to 70 percent of the FCCH rates ($37 million).

Slots Decreased During Recession, Increased During Recovery. Between 2007-08 and 2013-14, CalWORKs slots decreased significantly, with 65,000 (35 percent) fewer slots in 2013-14 than in 2007-08. The reduction in slots was due to state actions that changed the number of CalWORKs families using child care. Most notably, beginning in 2009-10, the state exempted certain CalWORKs parents with young children from the work requirement and allowed them to stay home while continuing to receive cash aid. Since 2013-14, CalWORKs slots have increased by 6,148 (5 percent) due to the net effect of the state reengaging these families in the workforce and an offsetting decrease in the CalWORKs caseload due to an improving economy. Non-CalWORKs slots also decreased notably between 2007-08 and 2013-14 with 44,000 (17 percent) fewer slots

Figure 5

Child Care and Preschool Funding Over Time[a]

(In Millions)

	2007-08	2010-11	2013-14	2016-17
CalWORKs Child Care	$1,442	$1,108	$862	$1,150
Non-CalWORKs Child Care and Preschool	1,711	1,608	1,251	1,834
Totals	**$3,153**	**$2,716**	**$2,113**	**$2,984**

[a] Does not include Transitional Kindergarten funding. Makes no inflationary adjustments.

in 2013-14 than in 2007-08. This reduction was due to various across-the-board reductions to all non-CalWORKs programs. Since 2013-14, state augmentations resulted in non-CalWORKs slots increasing with slots in 2016-17 about 25,000 (12 percent) higher than in 2013-14.

Some Changes in Quality Improvement Funding Activities. The state reduced its spending on a variety of quality improvement and support activities by $28 million (27 percent) between 2007-08 and 2013-14. Since 2013-14, the Legislature has increased funding for quality and support activities by $65 million (87 percent). In addition to ongoing increases, the Legislature has provided $59 million in one-time funding. The ongoing augmentation primarily has supported the State Preschool QRIS block grant, while the one-time funding has supported preschool teacher training, QRIS for infants and toddlers, and loans for acquiring portable preschool facilities.

OVERVIEW OF GOVERNOR'S BUDGET PROPOSALS

In this section, we provide an overview of the Governor's child care and preschool budget, then describe his major spending and policy proposals.

Governor Proposes $3.8 Billion for Child Care and Preschool Programs in 2017-18. Of this amount, about half is for child care programs and half for preschool programs. As Figure 6 shows, the Governor's budget augments these programs by a total of $76 million (2 percent) from the revised 2016-17 level. Proposition 98 General Fund accounts for $30 million of this increase, with the remainder covered by federal funds ($28 million) and non-Proposition 98 General Fund ($18 million). Under the Governor's budget, proposed funding would support 437,000 child care and preschool slots (a 1 percent increase from 2016-17).

Governor Proposes Suspending Much of Multiyear Budget Agreement. As part of the 2016-17 budget package, the Legislature and the Governor agreed on a four-year plan to increase ongoing child care and preschool funding by roughly $500 million (roughly $200 million in Proposition 98 General Fund and $300 million in non-Proposition 98 General Fund). In 2016-17, the state provided $145 million for the first year of implementation ($137.5 million for rates and $7.8 million for 2,959 additional State Preschool slots). Though not formalized in statute, the agreement for 2017-18 assumed (1) annualization of the increases initiated the prior year, (2) 2,959 additional State Preschool slots, and (3) $86 million in non-Proposition 98 General Fund rate increases. The Governor's budget proposes annualizing some of the rate and slot increases initiated in 2016-17 but suspending the rest of the agreement for 2017-18. Given the one-year hiatus, the Governor proposes extending implementation of the plan through 2020-21.

Governor Proposes Mix of Spending and Policy Changes. Figure 7 (see page 16) shows proposed 2017-18 funding changes. As described in more detail below, spending changes are primarily associated with implementing elements of the budget agreement and making caseload changes for CalWORKs and non-CalWORKs child care programs. The budget plan also contains a notable federal fund swap. In addition to these changes, the Governor proposes several policy changes, primarily to give more flexibility to the state's two preschool programs. These proposed policy changes have no associated spending changes.

Spending Changes

Annualizes Funding for RMR Increases Initiated in 2016-17. The *2016-17 Budget Act* initiated two voucher rate increases beginning January 1, 2017. Specifically, the budget increased the RMR to the 75th percentile of the 2014 survey—reflecting an average RMR increase of 5 percent over the former rates. The budget also increased the rate for license-exempt providers from 65 percent to 70 percent of the RMR for family child care home providers. These rate increases affected providers participating in the Alternative Payment Program and all three CalWORKs child care stages. The Governor's 2017-18 budget includes $68 million

Figure 6

Child Care and Preschool Budget

(Dollars in Millions)

	2015-16 Revised	2016-17 Revised[a]	2017-18 Proposed	Change From 2016-17 Amount	Change From 2016-17 Percent
Expenditures					
CalWORKs Child Care					
Stage 1	$334	$418	$386	-$32	-8%
Stage 2[b]	419	445	505	60	13
Stage 3	257	287	303	15	5
Subtotals	($1,010)	($1,150)	($1,193)	($43)	(4%)
Non-CalWORKs Child Care					
General Child Care[c]	$305	$321	$319	-$1	—[d]
Alternative Payment Program	251	267	279	12	4%
Migrant Child Care	29	31	31	—[d]	—[d]
Care for Children With Severe Disabilities	2	2	2	—[d]	—[d]
Infant and Toddler QRIS Grant (one time)	24	—	—	—	—
Subtotals	($611)	($620)	($630)	($10)	(2%)
Preschool Programs[e]					
State Preschool—part day[f]	$425	$447	445	-$2	—[d]
State Preschool—full day	555	627	648	21	3%
Transitional Kindergarten[g]	665	704	714	10	1
Preschool QRIS Grant	50	50	50	—	—
Subtotals	($1,695)	($1,828)	($1,857)	($29)	(2%)
Support Programs	$76	$89	$82	-$7	-8%
Totals	**$3,392**	**$3,688**	**$3,763**	**$76**	**2%**
Funding					
Proposition 98 General Fund	$1,550	$1,679	$1,709	$30	2%
Non-Proposition 98 General Fund	885	984	1,002	18	2
Federal CCDF	573	639	606	-32	-5
Federal TANF	385	385	446	61	16

[a] Reflects Department of Social Services' revised Stage 1 estimates. Reflects budget act appropriation for all other programs.
[b] Does not include $9.2 million provided to community colleges for certain child care services.
[c] General Child Care funding for State Preschool wraparound care shown in State Preschool—full day.
[d] Less than $500,000 or 0.5 percent.
[e] Some CalWORKs and non-CalWORKs child care providers also use their funding to offer preschool.
[f] Includes $1.6 million each year used for a family literacy program at certain State Preschool programs.
[g] Reflects preliminary LAO estimates. Transitional Kindergarten enrollment data not yet available for any year of the period.
QRIS = Quality Rating and Improvement System; CCDF=Child Care and Development Fund; and TANF=Temporary Assistance for Needy Families.

Figure 7

2017-18 Child Care and Preschool Changes

(In Millions)

Change	Proposition 98 General Fund	Non-Proposition 98 General Fund	Federal Funds	Total
Annualization of Changes Initiated in 2016-17				
Annualizes Regional Market Rate increase[a]	—	$45	$12	$57
Annualizes State Preschool slot increase	$24	—	—	24
Annualizes 5 percent license-exempt rate increase	—	9	2	11
Subtotals	($24)	($54)	($13)	($91)
Caseload Changes				
Decreases non-CalWORKs slots for statutory growth adjustment[b]	-$4	-$3	—	-$7
Makes CalWORKs caseload and average cost of care adjustments	—	61	-$73	-11
Subtotals	(-$4)	($58)	(-$73)	(-$18)
Other Adjustments				
Adjusts Transitional Kindergarten for increases in LCFF	$10	—	—	$10
Replaces state funds with federal funds	—	-$93	$93	—
Removes one-time funding	—	-1	-6	-7
Subtotals	($10)	(-$95)	($88)	($3)
Totals	**$30**	**$18**	**$28**	**$76**

[a] Includes a hold harmless provision so that no provider receives less than it received in 2015-16. This provision will expire at the end of 2017-18.

[b] Reflects 0.4 percent decrease in the birth-through-four population.

LCFF = Local Control Funding Formula.

to annualize these rate increases ($57 million for the RMR increase and $11 million for the license-exempt rate increase).

Annualizes Funding for Full-Day State Preschool Slots Initiated in 2016-17. The 2016-17 budget included $8 million for 2,959 full-day State Preschool slots at local education agencies (LEAs) beginning April 1, 2017. The Governor's 2017-18 budget includes an additional $24 million for the full-year cost of these slots.

Does Not Complete SRR Increase Initiated in 2016-17. The *2016-17 Budget Act* included a 10 percent increase to the SRR that was scheduled to begin January 1, 2017. Because CDE has difficulty implementing a mid-year SRR increase, CDE instead gave a 5 percent increase to all providers at the start of the fiscal year. The Governor's budget does not provide funds to annualize the 10 percent increase—effectively maintaining the 5 percent increase implemented last year.

Makes Adjustments for Changes in CalWORKs Child Care Caseload and Average Cost of Care. The Governor's budget includes a year-to-year decrease of $11 million to reflect changes in CalWORKs child care caseload and the types of care families select. (Changes in types of care used affect the average cost of care, independent from the rate increases described above.) This decrease is comprised of a $49 million decrease in Stage 1, offset by a $36 million increase in Stage 2 and a $2 million increase in Stage 3.

Applies Statutory Growth, but Not Cost-of-Living Adjustment (COLA), to Non-CalWORKs Child Care Programs. The budget decreases non-CalWORKs child care and preschool funding by $7 million to account for a 0.4 percent decrease in the birth-through-four population in California. The budget does not include a COLA (estimated to be 1.48 percent) for non-CalWORKs child care and State Preschool programs. The Governor's budget, however, does include a $10 million increase for Transitional Kindergarten associated with the Governor's overall proposed augmentation for LCFF.

Swaps State With Federal Funds. The Governor's budget allocates an additional $93 million in federal funds to offset state General Fund expenditures. This increase in available federal funds is the net result of a $120 million increase in federal TANF funds for the CalWORKs Stage 2 program offset by a $27 million reduction in available federal CCDF funds. The additional TANF funds are due to lower overall CalWORKs costs coupled with more realignment-related funding for CalWORKs. Both factors work to free up TANF funds for CalWORKs Stage 2 costs.

Policy Changes

Allows More Flexibility for State Preschool and Transitional Kindergarten Programs. The Governor's budget includes four proposals to provide more flexibility for State Preschool and Transitional Kindergarten providers. For State Preschool, the Governor proposes to: (1) exempt programs run by school districts from licensing requirements, (2) give all programs more flexibility in meeting minimum requirements for staffing ratios and teacher qualifications, and (3) allow part-day programs to enroll children with special needs whose families do not meet income eligibility criteria (so long as all eligible and interested children are served first). For Transitional Kindergarten, the Governor proposes to allow school districts more flexibility in determining the number of hours they operate per day. We discuss these specific proposals in the next section.

Aligns the State Definition of Homelessness With the Federal Definition. Currently, children can be deemed eligible for subsidized care if they are homeless and a parent needs to access child care while looking for permanent housing. The state currently considers children to be homeless for the purposes of child care eligibility if they are sleeping in a shelter, transitional housing, or places not designed for use as sleeping accommodations. The Governor proposes to expand the state's definition of homelessness so that it is the same as the definition used for the federal McKinney-Vento Homeless Assistance Act. The definition used for federal purposes also classifies children as homeless if they are temporarily staying with other people due to the loss of housing. This slightly expanded definition of homelessness likely would increase the number of children eligible for child care. We have no concerns with this proposal.

Allows Providers to Accept Electronic Applications for Child Care. Currently, providers are required to collect paper applications with handwritten signatures from families applying for subsidized child care or State Preschool programs. The Governor proposes to allow providers to accept electronic applications and signatures from families applying for subsidized child care or State Preschool. We have no concerns with this proposal.

ANALYSIS OF PRESCHOOL PROPOSALS

In this section, we provide an overview of California's preschool programs, then discuss key issues relating to preschool slots and preschool program alignment.

Overview

State Has Two Main Preschool Programs. In 2016-17, California spent $1.8 billion on two main preschool programs: State Preschool and

Transitional Kindergarten. Of this amount, $1.1 billion supported 164,000 State Preschool slots and $700 million supported nearly 80,000 Transitional Kindergarten slots. As Figure 8 shows, these programs have different eligibility criteria, program length, staffing requirements, and funding rates. Transitional Kindergarten is run exclusively by LEAs. By comparison, about half of State Preschool providers are LEAs (accounting for two-thirds of slots) and half are non-LEAs (accounting for one-third of slots). In addition to these state programs, the federal government runs the Head Start preschool program. Of all subsidized preschool slots for four-year olds in California in 2014-15, 52 percent were in State Preschool, 31 percent in Transitional Kindergarten, and 18 percent in Head Start.

State Authorized Districts to Create "Expanded" Transitional Kindergarten in 2015-16. As part of the 2015-16 budget plan, the Legislature enacted trailer legislation that allows school districts and charter schools to enroll four-year old children in Transitional Kindergarten if their fifth birthday falls between December 2 and the end of the school year. These children generate attendance-based funding when they turn five. A child with a birthday in the middle of January, for example, would generate funding for roughly half of the school year. The state does not collect data on the number of children enrolled as a result of these expanded Transitional Kindergarten provisions. Several large school districts, however, indicate they have expanded their Transitional Kindergarten programs under the new provisions. In 2015-16, for

Figure 8

Comparing California's Two Major Preschool Programs

	State Preschool	Transitional Kindergarten
Eligibility criteria	Four-year olds from families with incomes at or below 70 percent of state median income as calculated in 2007.[a] Children in full-day program must have parents working or in school.	Four-year olds with birthdays between September 2 and December 2.[b]
Providers	Local education agencies and subsidized centers.	Local education agencies.
Program length	At least 3 hours per day, 175 days per year for part-day program. At least 6.5 hours per day, 250 days per year for full-day program.	At least 3 hours per day, 180 days per year.
Teacher qualifications	Child Development Teacher Permit (24 units of ECE/CD plus 16 general education units).[c]	Bachelor's degree, Multiple Subject Teaching Credential, and a Child Development Teacher Permit or at least 24 units of ECE/CD or comparable experience.[c,d]
Staffing ratios	1:24 teacher-to-child ratio and 1:8 adult-to-child ratio.	1:33 teacher-to-child ratio.
Annual funding per child[e]	$4,386 (part-day) and $10,114 (full-day).	Average of $8,810.

a Programs may serve three-year olds from income-eligible families if all eligible and interested four-year olds have been served first.

b Schools may serve younger four-year olds with birthdays before the end of the school year but those children do not generate state funding until they turn five.

c Referenced permit and credential are issued by California's Commission on Teacher Credentialing.

d The requirements shown apply to teachers hired after July 1, 2015.

e Funding rates are 2016-17 estimates.

ECE/CD = Early Childhood Education/Child Development.

example, the Los Angeles Unified School District indicated it served 2,900 children through the expanded Transitional Kindergarten provisions.

State Has Complicated Way of Funding Preschool Programs. For State Preschool, CDE contracts with individual providers using the SRR for every child served. The funding source is primarily Proposition 98 General Fund, though full-day programs run by non-LEAs receive non-Proposition 98 General Fund for the wraparound portion of their program. The state funds Transitional Kindergarten through LCFF, which is funded with Proposition 98 General Fund and local property tax revenue.

Preschool Slots

Below, we provide background on recent increases in preschool slots, describe the Governor's slot-related proposals, assess those proposals, and offer associated recommendations.

Background

State Added Total of Almost 10,000 Full-Day State Preschool Slots Over Last Two Years. In 2015-16, the Legislature added 7,030 full-day State Preschool slots, scheduled to begin January 1, 2016. Of these slots, the budget act earmarked 5,830 for LEAs and 1,200 for non-LEAs. In 2016-17, the Legislature added another 2,959 full-day State Preschool slots, all for LEAs, scheduled to begin April 1, 2017.

LEAs Have Not Shown Sufficient Interest in New Full-Day Slots. To allocate new slots across the state, CDE requests applications from interested entities and awards contracts to those that demonstrate they can meet the minimum program requirements. In 2015-16, due to a lack of applicants, CDE issued only 1,646 of the 5,830 full-day State Preschool slots for LEAs. With the remaining funding, the department issued 3,700 part-day slots for LEAs, 851 part-day slots for non-LEAs, and 1,490 full-day slots for non-LEAs (above the 1,200 already earmarked in the budget). In 2016-17, LEAs to date have applied for only 519 of the 2,959 full-day State Preschool slots available. The CDE is currently in the process of issuing a second request for applications. If CDE is still unable to find enough LEAs interested in offering the full-day slots, it will make funding available for part-day slots.

Some State Preschool Providers Report Challenges Earning Their Contracts. Each State Preschool provider contracts with the state for a specified amount of funding. If it does not spend its full contract amount, the associated funds return to the state. If this occurs for multiple years, CDE can reduce the contract in future years. In 2014-15, the most recent year of data available, $101 million in State Preschool funding allocated to providers was "unearned." This represents 12 percent of all State Preschool funding and is almost double the unearned rate for other contract-based child care programs (7 percent). This amount also is 77 percent higher than the amount unearned for the program in 2013-14. Several factors might contribute to the increased difficulty in filling slots, including: providers being unable to expand or open new sites quickly enough to accommodate the rapid and significant increase in slots since 2014-15; increased enrollment in other large competing programs for four-year olds, such as Transitional Kindergarten and Head Start; and the state's outdated income eligibility threshold, which is based on state median income as calculated in 2007.

Multiyear Budget Agreement Assumes Total of Almost 9,000 Additional Slots Over Four-Year Period. While not formalized in statute, the multiyear budget agreement for preschool included 8,877 additional full-day State Preschool slots for LEAs. These slots were to be implemented in three equal batches on April 1 of 2017, 2018, and 2019. The first batch was funded through the

2016-17 Budget Act, with future batches intended for inclusion in the 2017-18 and 2018-19 budgets respectively.

Governor's Proposal

Does Not Include Funding for Additional Slots in 2017-18. While the Governor's budget includes funding to annualize the cost of the slots implemented mid-year in 2016-17, it does not include funding for the second batch of additional slots in 2017-18. (These slots would cost $7.5 million under the rates proposed in the Governor's budget.)

Allows Part-Day State Preschool Programs More Flexibility to Serve Children With Special Needs. To allow providers more flexibility to serve as many children as their contract allows, the Governor proposes to allow part-day State Preschool programs to serve children with special needs who do not meet the income-eligibility criteria as long as all eligible and interested children are served first. (Current law allows part-day State Preschool programs to fill up to 10 percent of their slots with children from families with incomes up to 15 percent over the income-eligibility limit if all eligible and interested children are served first. Under the Governor's proposal, over-income children with special needs would not count toward this cap.)

Assessment

School Districts Do Not Have Strong Incentives to Apply for Full-Day State Preschool Slots. The lack of interest among LEAs in new full-day State Preschool slots may be due to their strong fiscal and programmatic incentives to serve children using expanded Transitional Kindergarten. Districts receive substantially more funding per day for Transitional Kindergarten than they receive for State Preschool. On a per-day basis, Transitional Kindergarten funding is 21 percent higher than the average full-day State Preschool rate and nearly twice the average part-day State Preschool rate. Despite receiving higher levels of funding, Transitional Kindergarten programs operate for a shorter length of time and have fewer programmatic restrictions. They do not, for instance, have to determine income eligibility, conduct child assessments, or set up their classrooms according to specific state standards. Because of higher funding rates and fewer restrictions, we think many LEAs might be choosing to serve additional four-year olds using expanded Transitional Kindergarten rather than through full-day State Preschool.

Not All Eligible Children Are Being Served. Although some providers have difficulty earning their State Preschool contracts, we estimate a substantial portion of eligible children remain unserved. Specifically, we estimate that at least 1 in 5 income-eligible four-year olds in California are not receiving subsidized preschool through a state or federal preschool program. (If other similar programs are indicative, some families with eligible children might not be interested in participating in a preschool program, but other unserved families might desire it yet be unable to access it.)

Recommendations

Allow All Types of Providers to Apply for New Full-Day Slots. If the Legislature is interested in supporting more full-day State Preschool slots over the next few years, we recommend it make funds available to all providers, not only LEAs. LEAs currently do not seem to have sufficient interest in offering more full-day slots and have strong fiscal incentives to serve children through expanded Transitional Kindergarten rather than State Preschool. If the Legislature wants more LEAs to operate State Preschool programs over the longer term, it could address funding disparities between State Preschool and Transitional Kindergarten or change eligibility requirements so that each program serves a distinct group of students.

Focus on Unserved Eligible Children Before Expanding Eligibility. Given many children eligible for State Preschool currently are unserved, we recommend the Legislature reject the Governor's proposal to expand State Preschool eligibility to higher-income children with special needs. Though the Governor's proposal to serve more children with special needs seems well intended, it has the effect of displacing low-income children who otherwise would be able to access the program. Moreover, LEAs are responsible for ensuring all four-year old children with special needs receive service according to their individualized education program. As a result, this proposal effectively shuffles children with special needs from one program to another while bumping out low-income children who have no other program option.

Preschool Program Alignment

Below, we provide additional background on State Preschool and Transitional Kindergarten, describe the Governor's proposals to better align the two programs, assess those proposals, and offer associated recommendations.

Background

State Preschool and Transitional Kindergarten Have Different Health and Safety Requirements. State Preschool programs must be licensed and follow CCL health and safety standards. (The CCL is a division within DSS.) These licensing standards include requirements that classrooms be clean and sanitary, children be constantly supervised, teachers be trained in first aid, and medication and cleaning supplies be stored out of reach of children. Members of the public can submit complaints to CCL regarding possible licensing violations. The CCL is then required to visit the facility within 10 days. State Preschool programs also must follow standards set by CDE regarding classroom environment, which include a mix of health, safety, and programmatic requirements. These CDE rules include requirements that furniture and toys be clean and well-maintained and classrooms be set up with multiple stations to support different types of learning (for example, classrooms could have a science area and an art area). Both CCL and CDE visit sites once every three years to monitor compliance with regulations. By contrast, Transitional Kindergarten programs are not licensed or inspected. Instead, they must operate in buildings with the same safety specifications as other K-12 buildings. For example, these facilities must be built to minimize the risk of damage in an earthquake.

Many State Preschool Programs Participate in Local QRIS. The state provides $50 million for State Preschool QRIS each year, with funding allocated in 2016-17 to 37 local consortia serving 49 counties. These consortia use the funds to evaluate the quality of State Preschool providers and offer additional resources to help providers improve or maintain program quality. Local consortia assess providers based on a five-tier matrix, which awards points for different levels of staffing ratios and qualifications, the quality of child-teacher interactions, and the implementation of certain child assessments, among other program aspects. The minimum State Preschool requirements are roughly equivalent to a Tier 3 rating.

Schools Required to Operate Transitional Kindergarten Same Length of Day as Kindergarten. Under state law, Transitional Kindergarten is the first year of a two-year Kindergarten program. If a school district runs Transitional Kindergarten and Kindergarten programs on the same site, the two programs at that site must be run for the same length of the day. Districts that want to operate a full-day Kindergarten and a part-day Transitional Kindergarten program on the same site must obtain a waiver from the State Board of Education. (Districts can operate programs of differing lengths on separate school sites.)

Governor's Proposal

Governor Interested in Better Aligning State Preschool and Transitional Kindergarten. The Governor's budget includes several proposals to more closely align these two programs. Most of the proposals are designed to make State Preschool programs more similar to those of Transitional Kindergarten but one proposal is designed to make Transitional Kindergarten more similar to State Preschool.

Exempts State Preschool Programs Run by School Districts From Licensing Requirements. The Governor proposes to exempt State Preschool programs from CCL requirements if they operate in facilities constructed according to the state's K-12 building standards. Programs still would be required to follow CDE's requirements for staffing and environment.

Includes Two Flexibility Proposals for Meeting State Preschool Staffing Requirements. The Governor proposes to exempt State Preschool providers with QRIS Tier 4 or higher ratings from the State Preschool staffing ratio requirements. These providers, however, still would need to meet licensing requirements (that is, have an adult-to-child ratio of 1:12). Similarly, for State Preschool programs with lower QRIS ratings or no rating, the Governor proposes to allow classrooms taught by a teacher with a Multiple Subject Teaching Credential to operate with an adult-to-child ratio of 1:12 (rather than the 1:8 ratio currently required).

Allows Districts to Run Part-Day Transitional Kindergarten and Full-Day Kindergarten on Same Site. The Governor proposes to allow school districts to run their Transitional Kindergarten and Kindergarten programs on the same site for different lengths of time without a waiver.

Assessment

Better Alignment of State Preschool and Transitional Kindergarten Programs Worthy Goal. The state currently lacks a systematic approach to providing early learning to four-year olds, which results in wide disparities in eligibility, funding, and the types of services provided. Given this lack of coherence and unnecessary complexity, we think better alignment of the state's two largest preschool programs is a very worthy goal.

Proposals Make Complicated System More Complicated. Although the administration intends to better align State Preschool and Transitional Kindergarten, many elements of his proposals add greater complexity to the existing system. For example, exempting only certain State Preschool programs from licensing requirements would create different requirements for State Preschool programs at LEAs and non-LEAs. Similarly, while State Preschools run by LEAs would be exempt from licensing requirements (and more similar to Transitional Kindergarten in that respect), they still would have to follow CDE's regulations about classroom environment (which do not apply to Transitional Kindergarten). By creating new staffing ratio standards for State Preschool teachers with a teaching credential, the staffing flexibility proposals also add complexity without allowing for complete alignment. A State Preschool classroom with a credentialed teacher still would be required to have an adult-to-child ratio (1:12) almost three times lower than that of Transitional Kindergarten (1:33).

Additional Concerns With Minimum Staffing Requirement Proposals. In addition to our concerns about making the system more complicated, we also have specific concerns with the proposal to allow higher staffing ratios for credentialed teachers. Specifically, we are concerned that a teacher with a Multiple Subject Teaching credential and no early education training requirements might not be better prepared than a teacher with early education training to serve more children with less adult support.

Transitional Kindergarten and Kindergarten Funding Not Aligned With Program Length. Given the state currently allows school districts to choose the length of day for their Transitional Kindergarten and Kindergarten programs at different school sites, we see no reason to restrict their ability to offer programs of different length on the same school site. We are concerned, however, that Transitional Kindergarten and Kindergarten programs receive the same amount of funding per student regardless of program length. This lack of alignment results in a funding structure that has little connection to districts' underlying program costs.

Recommendations

Reject Preschool Proposals, Pursue Alignment More Holistically. Rather than make marginal changes to existing preschool programs to get them to operate somewhat more similarly, we recommend the Legislature take a more holistic approach. Under such an approach, the Legislature would consider how best to serve four-year olds, particularly those from low-income families. To this end, it would consider what eligibility criteria, program standards, and funding levels it desired for these children. Making all these decisions in tandem would provide for better alignment and coherence.

Adopt Transitional Kindergarten and Kindergarten Flexibility in Tandem With Differential Rates. If the Legislature does not pursue holistic reform of programs serving four-year olds, we recommend it adopt the Governor's proposal regarding Transitional Kindergarten and Kindergarten flexibility and also establish differential funding rates for full-day and part-day programs. Such an approach would better align school district funding to actual program costs and reduce funding disparities between part-day State Preschool and part-day Transitional Kindergarten programs.

QUALITY IMPROVEMENT ACTIVITIES

In this section, we provide background on a federal requirement that states spend a certain amount each year on improving the quality of their child care and preschool programs. We then describe a recently revised quality expenditure plan submitted by CDE, provide an assessment of the state's existing quality improvement programs as well as CDE's expenditure plan, and make several associated recommendations.

Background

Federal Law Requires States to Spend a Certain Amount Each Year on Improving Quality of Child Care and Preschool. California receives roughly $600 million each year from the federal government through CCDF. As a condition of receiving the funds, the state is required to spend an additional $200 million each year in state funds to meet a matching requirement. Of this combined $800 million, the federal government requires the state to spend a certain percentage on quality improvement. In 2016-17, the state was required to spend 10 percent ($78 million) on quality improvement activities, with 3 percent ($22 million) required for activities benefitting infants and toddlers and the remaining 7 percent ($56 million) not restricted to any particular age group. In addition, the state reappropriated $6 million in unspent prior-year quality funds, bringing total quality spending to $84 million in 2016-17. California is required to submit an associated expenditure plan to the federal government every three years. The state's most recent plan was approved in June 2016 and extends through September 30, 2018.

Federal Requirement for Quality Spending Set to Increase Through 2020-21. Due to a recent reauthorization of the federal act governing the CCDF, the federal requirement for quality improvement spending will increase gradually over the next few years, reaching 12 percent by 2020-21. The percentage of funds for infant and toddler quality improvement activities will remain at 3 percent, with the percentage not restricted to any particular age group growing to 9 percent by the end of the period. Assuming federal CCDF funding remains flat, the state would be required to spend $95 million on quality improvement activities in 2020-21.

Federal Law Allows States to Count Various Activities Toward Meeting Requirement. As listed in Figure 9, federal law specifies ten allowable quality improvement activities. These activities range from training for child care and preschool providers to developing early learning materials for these providers to enforcing licensing requirements to providing information about child care options to parents.

California Currently Supports About 30 Quality Improvement Programs. California appropriates funding for quality improvement programs in the annual budget act. In recent years, the budget act has earmarked a portion of funds for specific activities ($22.4 million in 2016-17) but given CDE discretion in allocating the remainder ($61.3 million in 2016-17). In 2016-17, CDE allocated quality improvement funds to about 30 programs. About half of the funds were used for training activities, financial aid programs for

Figure 9

Federal Law Specifies Ten Allowable Quality Improvement Activities

- **Training and professional development of child care workforce.**
- **Developing or implementing early learning and development guidelines.**
- **Supporting Quality Rating and Improvement Systems.**
- **Improving the supply and quality of child care programs for infants and toddlers.**
- **Supporting a statewide system of resource and referral services.**
- **Facilitating compliance with licensing requirements and other state requirements for inspection, monitoring, training, health, and safety.**
- **Evaluating and assessing the quality and effectiveness of child care programs and services offered.**
- **Supporting child care providers in the voluntary pursuit of accreditation by a national accrediting body with demonstrated, valid, and reliable program standards of high quality.**
- **Developing standards for health, mental health, nutrition, physical activity, and physical development.**
- **Carrying out other activities where the state can measure those activities' effects on provider preparedness, child safety and well-being, or entry into kindergarten.**

teachers taking additional classes, and supporting community colleges in serving students in their early childhood education programs. Nearly one-third of funds supported 57 Resource and Referral agencies (R&Rs), which collect data on child care providers and help parents find child care in their area. The remaining funds supported various activities, including licensing enforcement, development of early learning resources, and local planning activities.

Each Program Has Its Own Requirements. Each of these programs has rules specifying how funds can be used. These rules typically are created by CDE. For example, CDE specifies how much certain programs may spend on specified program activities. Some programs also have certain rules specifying who is eligible to participate. For example, the AB 212 Child Care Retention Program (commonly referred to as the AB 212 program) can be used only by teachers employed in settings contracting directly with the state. In other cases, programs give priority to certain teachers but allow other types of teachers to participate if additional space is available. Training on child assessments, for example, is prioritized for teachers employed in state-contracted settings but allows other teachers to participate.

Funds Used for Mix of State- and County-Level Activities. In California, quality improvement funding is used for a mix of state-level activities, base allocations for certain county-level support entities, and specific county-level activities. At the state level, quality improvement activities include licensing enforcement at DSS, the development of resources for child care programs around the state, and training on using CDE-developed assessments. In addition, CDE contracts with other entities to operate the California Preschool Instructional Network (CPIN) and the Program for Infant and Toddler Care (PITC)—both of which provide statewide training using standard curricula. Regarding county-level support entities, California counts base funding for both R&Rs and Local Planning Councils (LPCs) toward its quality improvement requirement. (Each county has an LPC tasked with identifying areas with the greatest unmet need for child care and coordinating activities of local support entities and child care providers.) California also counts as quality improvement specific county-level activities, including the AB 212 program, which provides stipends to some early educators in each county taking child development courses.

QRIS Consortia Receive Additional Funds. Of the $84 million provided for quality improvement activities in 2016-17, QRIS consortia received $800,000 for child care programs serving migrant children. In addition, consortia received $75 million that was not counted toward the federal spending requirement. Of this amount, $50 million is funding from Proposition 98 General Fund for State Preschool QRIS and $25 million is from First 5 California for QRIS for all types of programs. (First 5 California is an independent state commission funded with cigarette tax revenue. It is charged with spending a certain amount on child care and school readiness activities.) In addition, the state designated $24 million on a one-time basis for infant and toddler QRIS in 2015-16, with a three-year allowable expenditure window extending through 2017-18. The state also did not count this allocation toward the federal quality improvement requirement.

QRIS Consortia Have Small Presence in Many Areas of the State. Currently, California has 48 QRIS consortia serving a small percentage of child care and preschool providers located across all 58 counties. These consortia are comprised of a variety of county-level support entities such as R&Rs, LPCs, and First 5 commissions. Consortia are responsible for rating participating child care and preschool programs, helping these programs achieve and maintain high ratings, and encouraging unrated sites to participate in QRIS. Consortia have substantial flexibility in how they help programs achieve and maintain high ratings. For example, a consortium might provide financial aid to teachers so they can take classes or give grants to child care providers for purchasing materials and supplies. In 2016-17, the average consortium received $1.6 million from CDE and First 5 combined. Many consortia coordinate with other county-level support entities to align other quality improvement programs with QRIS. For example, some local training programs may give priority to teachers employed in QRIS-rated sites. Because such a large portion of QRIS funding is set aside for State Preschool, providers participating in QRIS are disproportionately State Preschool providers.

Consortia Use QRIS Matrix to Rate Providers in Key Areas. The QRIS matrix has five tiers (or ratings) for providers. Tier 1 is equivalent to meeting minimum licensing health and safety standards, whereas Tier 3 is roughly equivalent to the program requirements for State Preschool and the other contract-based child care programs. The matrix awards points in seven core areas: (1) staffing ratios, (2) staffing qualifications, (3) the quality of child-teacher interactions, (4) use of child observations to inform curriculum, (5) use of developmental screenings, (6) classroom environment, and (7) director qualifications. Each consortium hires individuals to rate programs in their region. Some of the areas of the matrix are easier to assess than others. Determining teacher qualifications, for example, only requires QRIS assessors to review paperwork on file. By contrast, measuring the quality of child-teacher interactions can be more time-consuming and expensive. Assessments of child-teacher interactions are made using the Classroom Assessment Scoring System (CLASS), a specific assessment developed by early childhood researchers. To conduct these assessments, assessors must be trained in the CLASS tool and certified as reliable in providing ratings in a consistent way. In 2016-17, CDE allocated $2 million in quality improvement funds (that counted towards the federal requirement) to help local assessors get trained and certified. Consortia also use other QRIS grant funds for rating and certification.

Revised Quality Improvement Expenditure Plan

2016-17 Budget Act *Required CDE to Revise Quality Improvement Expenditure Plan.* The *2016-17 Budget Act* required CDE to revise the state's plan and submit a draft to the Legislature by February 1, 2017. In developing the revised plan, the budget act directed CDE to (1) retain funding for R&Rs, LPCs, and licensing enforcement and (2) prioritize the rest for QRIS. The intent is for the state to submit a revised expenditure plan to the federal government upon enacting the *2017-18 Budget Act*.

Revised Plan Shifts Some Funding to New Infant and Toddler QRIS Block Grant. As required, CDE submitted its revised quality expenditure plan to the Legislature in February 2017. As Figure 10 shows, the proposed plan keeps funding flat for most programs, but eliminates one program and creates one new program. Specifically, under the revised plan, CDE proposes to eliminate the Child Development Teacher and Supervisor Grant program run by the California Student Aid Commission. In 2016-17, this program is providing about $300,0000 in grants to an estimated 160 students. The revised plan includes coupling this funding with $5.1 million in reductions to eight other programs and redirects the combined $5.4 million in freed-up funds to a new infant and toddler QRIS program. Consistent with the state's existing QRIS programs, under the new program, consortia would have broad flexibility to determine what activities they deem the most important in helping providers achieve and maintain high ratings. Of the redirected $5.4 million, $3.7 million is taken from specific activities currently conducted by county-level support entities and $1.7 million is taken from various state-level activities. This

Figure 10

Comparing Existing and Proposed Quality Improvement Expenditure Plans

(In Thousands)

Category	Activities	2016-17[a] Revised	2017-18 Proposed	Change
Parent resources	Resource and Referral Agencies	$22,280	$22,280	—
	1-800-KIDS-793 Phone Line for Parents	91	91	—
	Subtotals	($22,371)	($22,371)	(—)
Training and technical assistance	Program for Infant and Toddler Care	$6,846	$6,453	-$393
	California Preschool Instructional Network	4,000	4,000	—
	Child Care Initiative Project	3,057	3,027	-30
	Health and safety training grants and regional trainers	2,655	2,655	—
	Inclusion and Behavior Consultation Network	920	920	—
	Family Child Care at Its Best Project	767	767	—
	Map to Inclusive Child Care and CSEFEL	750	750	—
	Desired Results field training	667	667	—
	Developmental Screening Network	176	176	—
	California Strengthening Families Trainer Coordination	40	40	—
	Subtotals	($19,877)	($19,455)	(-$423)
Financial aid	AB 212 Child Care Retention Program	$10,750	$8,063	-$2,688
	Subsidized TrustLine Applicant Reimbursement	461	461	—
	Stipend for permit	435	435	—
	Child Development Teacher and Supervisor Grant Program	318	—	-318
	Subtotals	($11,964)	($8,958)	(-$3,006)
Enforcement	Licensing enforcement for child care programs	$8,000	$8,000	—
Support to community colleges	Child Development Training Consortium	$3,273	$2,892	-$381
	California Early Childhood Mentor Program	2,966	2,921	-45
	Subtotals	($6,239)	($5,813)	(-$426)
Early learning resources	Desired Results system for children and families	$1,025	$1,025	—
	Development of early learning resources	959	500	-$459
	Faculty Initiative Project	455	400	-55
	California Early Childhood Online	290	290	—
	Development of infant/toddler resources	180	180	—
	Subtotals	($2,909)	($2,395)	(-$514)
Local planning	Local Planning Councils	$3,353	$3,353	—
Quality Rating and Improvement System (QRIS)	QRIS certification grants	$2,000	$1,000	-$1,000
	Migrant QRIS Block Grant	800	800	—
	Infant/Toddler QRIS Block Grant	—	5,369	5,369
	Subtotals	($2,800)	($7,169)	($4,369)
Program evaluations	Evaluation of quality improvement activities	$570	$570	—
Totals		**$78,084**	**$78,084**	**—**

[a] Does not include $6 million in one-time funding provided for quality improvement activities in 2016-17.
CSEFEL = California Social Emotional Foundations of Early Learning.

component of the revised plan would provide more flexibility regarding the types of county-level activities that could be performed.

CDE Proposes to Add New Rules to Some Existing Programs. In conjunction with the revised quality expenditure plan, CDE proposes to change the rules for several non-QRIS programs. Among the most notable changes, CDE plans to require providers using PITC or CPIN coaching to participate in QRIS. For the California Early Childhood Mentor Program, CDE plans to require mentor teachers leading student practicums to be teaching at sites rated QRIS Tier 4 or higher.

Assessment

Some Activities Are Essential to Support Subsidized Child Care and Preschool System. We believe some current activities that count toward the quality improvement expenditure requirement are essential to ensure families have access to child care and state funding is used effectively. Most notably, quality improvement funding is used to help parents find child care, collect data on child care providers, and identify areas in the state with the greatest unmet need for subsidized care. These activities currently are conducted by R&Rs and LPCs. Quality improvement funding also partially supports the cost of inspecting licensed child care facilities—essential for ensuring providers meet health and safety requirements.

Quality Improvement Funding at County Level Can Lack Coordination and Be Difficult to Target to Highest Priorities. At the county level, multiple support agencies often use quality improvement funding to offer similar programs to providers and teachers. For example, teachers can receive training by accessing AB 212 stipends from LPCs, attending training at R&Rs, or accessing training offered by QRIS consortia. With so many training programs, coordination can be difficult, with no guarantee that training does not overlap. The restrictions placed on quality improvement funding also can limit county-level support entities from directing funding toward their highest priorities. For example, county-level support entities could identify a high priority for health and safety training but be unable to direct funding to this purpose given all the existing strings placed on their quality improvement funding.

Little Information on Effectiveness of State-Level Activities. We think the state can play an important role in supporting quality improvement activities. For example, developing training resources and making them available to entities across the state can reduce the need for local entities to reinvent the wheel. The state, however, currently does not have good information on the effectiveness or efficiency of its existing state-level programs. Data collected for each program is often insufficient to assess program effectiveness. For example, though CDE collects some data on participants who attend statewide trainings, it does not collect data on whether participants have access to similar trainings run by county-level entities or whether they teach in a voucher-based or a contract-based setting. In addition, though the state has conducted program evaluations of three activities between 2009 and 2016, none of these evaluations measured whether the programs improved the quality of child care or determined whether the activity was an effective use of funding. Instead, the evaluations primarily included descriptive information about how funds were used, who benefited from the programs, and what participants thought about the programs. Without better data and program evaluations, determining whether current state-level activities are effective will remain difficult.

Funding Disproportionately Serves Providers That Already Meet Higher Standards. The state has two sets of standards for child care providers. Providers receiving child care vouchers are required to meet licensing health, safety, and staff standards. Providers contracting directly with CDE must meet more rigorous quality standards, including higher staff qualifications, implementation of child assessments, and specific rules about program environment. Of the $28 million in CDE's revised plan for training and financial aid, 28 percent is restricted to contract-based providers. Under CDE's revised program rules, another 37 percent would be prioritized for programs participating in QRIS. Since participation in QRIS is more common among contract-based providers—particularly State Preschool programs—these funds likely would disproportionately benefit contract-based providers caring for preschool-aged children. Prioritizing such a large portion of quality improvement funds for providers with the highest standards comes at the expense of serving voucher-based providers that might benefit most from additional support. Of the state's subsidized child care and preschool slots, nearly three-quarters of the infant and toddler population (aged birth to three) and one-quarter of the preschool population (aged three through five) are served by voucher-based providers.

Shifting Funds to QRIS Block Grant Provides More Flexibility in Types of Activities . . . By shifting funds from programs with strict requirements to a more flexible QRIS block grant, the proposal allows more flexibility for county-level support entities to conduct activities and serve providers they deem most important. The additional flexibility also allows county-level support entities to develop their own coherent improvement systems, which could simplify access to improvement activities.

. . . But Restricting Funds to QRIS Limits Providers That Can Benefit. Although shifting funding to a QRIS block grant allows for more flexibility in the types of improvement activities offered, restricting the funds to QRIS consortia significantly limits the number of entities that can receive support. Although exact data is not available, a small percentage of providers serving subsidized children currently participate in QRIS.

Recommendations

Retain Funding for Essential Activities. Figure 11 (see next page) shows our recommended approach to funding quality activities. We recommend retaining funding for helping parents find child care, identifying areas in the state with the greatest unmet need for child care, and helping local child care providers coordinate resources. Currently, these functions are performed at the county level by R&Rs and LPCs. In the future, the Legislature could reconsider how best to support these activities, including potentially collapsing the two essential functions into one entity. We also do not have concerns with continuing to use quality funds for licensing enforcement activities.

Repackage Other County-Level Funding Into Block Grant. As Figure 11 shows, we recommend combining seven programs into a county block grant totaling $21 million. The funding for most of these programs currently is allocated to county-level support entities, including R&Rs, LPCs, and community colleges. We recommend the state require key support entities in each county—including R&Rs, the LPC, the First 5 county commission, community colleges, the county welfare department, and the county office of education—to designate a lead agency and agree on a plan for how funding will be used, taking into account the providers and the subsidized population in their area. (If desired, multiple counties could submit a joint application with one lead agency.) To offer greater flexibility, we recommend making any provider serving subsidized children eligible for funding. We recommend the state allocate the block grant funds based on each county's percentage of statewide subsidized child care and preschool slots.

Collect Data From Lead Agencies on How Block Grant Funding Is Spent. In tandem with greater flexibility, we recommend the state require lead agencies to submit annual data reports detailing how funding was spent and which providers benefitted from the funding. Specifically, we recommend reports be required to include the amount spent on each type of activity and detailed information regarding the types of providers participating (QRIS or non-QRIS, contract or voucher based). We recommend the reports also include data on the share of funding spent on each subsidized age group.

Ensure Non-QRIS Participants Have Access to State-Level Programs. To ensure a greater share of existing providers can access state-level programs such as CPIN and PITC, we recommend rejecting

Figure 11

Recommended 2017-18 Quality Improvement Expenditure Plan

(In Thousands)

Recommendation	Activities	Amount
Fund essential activities as budgeted but revisit how best to provide these activities moving forward	Resource and Referral Agencies	$22,280
	Licensing enforcement for child care programs	8,000
	Local Planning Councils	3,353
	Evaluation of quality improvement activities	570
	Subtotals	($34,203)
Repurpose funding from other existing county-level entities and activities into county block grant	AB 212 Child Care Retention Program	$8,063
	Infant/Toddler QRIS Block Grant	5,369
	Child Care Initiative Project	3,027
	Health and safety training grants and regional trainers	2,655
	QRIS certification grants	1,000
	Migrant QRIS Block Grant	800
	Stipend for permit	435
	Subtotals	($21,349)
Fund most state-level activities as budgeted but reassess over next several years	Program for Infant and Toddler Care	$6,453
	California Preschool Instructional Network	4,000
	California Early Childhood Mentor Program	2,921
	Child Development Training Consortium	2,892
	Desired Results system for children and families	1,025
	Inclusion and Behavior Consultation Network	920
	Family Child Care at Its Best Project	767
	Map to Inclusive Child Care and CSEFEL	750
	Desired Results field training	667
	Development of early learning resources	500
	Subsidized TrustLine Applicant Reimbursement	461
	Faculty Initiative Project	400
	California Early Childhood Online	290
	Development of infant/toddler resources	180
	Developmental Screening Network	176
	1-800-KIDS-793 Phone Line for Parents	91
	California Strengthening Families Trainer Coordination	40
	Subtotals	($22,532)
Totals		**$78,084**

QRIS = Quality Rating and Improvement System and CSEFEL = California Social Emotional Foundations of Early Learning.

CDE's proposal to limit participation in certain state-level programs to QRIS participants.

Evaluate Effectiveness of State-Level Programs and Revisit Funding Levels in the Future. We recommend the state fund the remaining programs in 2017-18 at their existing levels (nearly $23 million combined), but use the planned evaluation funding to hire an independent evaluator to assess each program over the next several years, starting with the largest programs in 2017-18. (If the Legislature would like to complete the evaluation process over a shorter period, it could shift funds from the county block grant for this purpose.) To ensure evaluations provide valuable information, we recommend the independent evaluators be required to assess the comparative cost-effectiveness of programs and make recommendations on which activities to fund. We recommend the Legislature revisit funding levels in the future based on the results of the evaluations, eliminating state-level programs that are not cost-effective, augmenting state-level programs that are cost-effective, and potentially redirecting some freed-up funding to the county block grant.

ALTERNATIVE PAYMENT AGENCIES

In this section, we provide an overview of Alternative Payment (AP) agencies, identify several major shortcomings in the way the state funds these agencies, and make various recommendations for improving the state's funding model.

Background

Below, we provide background on (1) child care vouchers in California, (2) AP agencies' key responsibilities and activities, and (3) the current model the state uses to fund these agencies.

Child Care Vouchers in California

State Provides Child Care Vouchers to Roughly 160,000 Children From Low-Income Families. Of these children, roughly four-fifths receive vouchers via the three stages of CalWORKs child care. The other one-fifth of children receive vouchers via the Alternative Payment program. Because funding for the Alternative Payment program is not sufficient to fund all eligible families, those with the lowest income are prioritized and waiting lists for the program are common. Child care vouchers allow families to choose a provider that best meets their needs. Families can use vouchers in licensed centers, licensed family child care homes, or in license-exempt care—typically a relative, friend, or neighbor who provides care in a private home.

State Sets the Maximum Value of Child Care Vouchers. Vouchers are based on a maximum RMR, which is derived from a survey of regional market prices. The state conducts the survey every few years as required by federal regulations. The RMR varies by county, child care setting, and the age of the child served. Care in a licensed child care center is more expensive than license-exempt care and infant care is more expensive than care for a school-aged child. The state typically sets the maximum RMR at a certain percentile of the survey results so that families will have access to a certain share of child care providers in their area. Currently, the state bases the maximum RMR at the 75th percentile of the 2014 survey, ensuring that children have access to three-fourths of their local child care providers. If a provider charges less than the maximum RMR, the state reimburses the actual charge.

State Has Changed RMR Five Times in Past Seven Years. In 2010-11 and 2011-12, the state decreased the reimbursement rates for license-exempt care from 90 percent of licensed family child care home rates to 60 percent of family child care home rates, with associated spending in 2011-12 about $100 million lower than the 2009-10 level. In 2014-15, 2015-16, and 2016-17, the state provided consecutive increases to the RMR for all types of child care settings, with spending in 2016-17 $199 million higher than the 2013-14 level.

AP Agencies' Key Responsibilities and Activities

AP Agencies Administer Most Voucher Programs. Voucher programs are administered by AP agencies and county welfare departments. AP agencies administer CalWORKs Stage 2, Stage 3, and the Alternative Payment program. In 2016-17, the state's AP agencies received a total of $999 million to operate these programs—$824 million to pay child care providers on behalf of parents and $175 million for their operational costs. County welfare departments administer CalWORKs Stage 1 and receive funding via a "single allocation" that can be used for any combination of Stage 1 child care and welfare-to-work services. In some cases, however, county welfare departments contract with other entities, such as their local AP agency, to administer the program. In 2016-17, 34 county welfare departments contracted with AP agencies to administer Stage 1 child care programs.

AP Agencies Vary Substantially in Terms of Voucher-Related Funding and Caseload. As of 2015-16, 76 AP agencies were operating in California. Of the 76 AP agencies, 50 are community-based organizations, 14 are county offices of education, and 12 are other local government entities, such as county welfare departments or school districts. Figure 12 groups AP agencies by the size of their voucher-related operating budgets (excluding provider payments). Of AP agencies, 58 percent have operating budgets smaller than $1 million, 34 percent have budgets between $1 million and $5 million, and 8 percent have budgets greater than $5 million. Agencies with larger budgets serve more children. As Figure 12 shows, agencies with budgets smaller than $1 million together account for less than 15 percent of all caseload, whereas agencies with budgets in excess of $5 million account for 45 percent of all caseload. Figure 13 (see page 34) includes additional information about AP agencies that we collected through a survey.

AP Agencies' Primary Function Is Program Execution. AP agencies' primary voucher-related responsibilities are to determine a family's eligibility for child care, make payments to the child care provider of a family's choice, collect fees from certain families, ensure families and providers are complying with state rules and regulations, and create and maintain detailed records about each family and provider. To accomplish these tasks, AP agencies' staff spend most of their time talking with families and providers, reviewing paperwork, and requesting additional information. For example, to determine family eligibility, AP caseworkers must collect and review paperwork documenting family income, family size, and hours worked. In some cases, AP agencies also must contact the parent's employer to verify information provided or collect additional information. This workload does not vary based on child age or the type of care provided. Because AP agencies work so closely with the families they serve, their workload is primarily driven by how many families they are serving at any given time.

State Rules Strictly Govern How Program Execution Is to Be Conducted. State law, regulations, and AP agencies' contracts with CDE are highly prescriptive with respect to program execution. For example, regulations govern how AP agencies reimburse child care providers and

Figure 12

Alternative Payment (AP) Agencies Vary Greatly in Size

2015-16

Operating Budget[a]	Number of AP Agencies	Percent of All AP Agencies	Total Caseload	Percent of all Caseload
Less than $200,000	14	18%	1,742	1%
$200,001 to $500,000	15	20	4,282	4
$500,001 to $1,000,000	15	20	10,297	9
$1,000,001 to $3,000,000	18	24	25,234	22
$3,000,001 to $5,000,000	8	11	22,831	20
$5,000,001 to $10,000,000	4	5	22,055	19
$10,000,001+	2	3	30,384	26
Totals	**76**	**100%**	**116,825**	**100%**

[a] Reflects state funding for voucher-based programs excluding provider payments and CalWORKs Stage 1 contracts.

in which cases providers should be reimbursed if children are absent. The state also requires AP agencies to keep all documentation of income eligibility on file and up to date at all times. If AP agencies are found to be out of compliance with these rules, their funding can be reduced.

Many AP Agencies Also Provide Support Services to Families and Child Care Providers. Although state law does not prescribe specific support services that AP agencies must offer to families and child care providers, AP agencies commonly provide such services. These services vary from agency to agency, but commonly include parenting classes, translation services, referral to other social services (for example, county food assistance), and provider staff training and technical assistance.

Funding Model for AP Agencies

CDE Determines Amount Each AP Agency Receives for Provider Payments. For CalWORKs Stage 2 and 3, CDE calculates each AP agency's provider payments based on estimates of caseload and average cost of care. For the Alternative Payment program, CDE typically allocates AP agencies the amount they received in the previous year for provider payments, adjusted for any rate or slot changes specified in the most recent state budget.

AP Agencies' Operational Funding Based on Percentage of Provider Payments. After determining each AP agency's allocation for provider payments, CDE provides additional funding to cover operational costs, equal to 21.21 percent of provider payments. This funding together with the provider payments comprise the total contract amount, or "Maximum Reimbursable Amount" (MRA). For example, an AP agency that receives $1 million for provider payments also receives $212,100 for operational expenses, for a total MRA of $1,212,100. (An AP agency's operational funding is equivalent to 17.5 percent of the MRA.)

AP Agencies' Operational Funding Varies by Region. Because AP agencies' operational funding is based on a percentage of provider payments, and provider payments are affected by differences in regional market rates, AP agencies' funding also varies based on the regional cost of child care. For example, two AP agencies serving the same number of children would receive significantly different funding levels if they were in areas of the state with vastly different provider reimbursement rates.

Operational Funding Is Not Reduced, but Can Be Increased, Midyear. Though operational funding is initially determined based on the amount

AP agencies receive for provider payments, it is not reduced midyear if the AP agency does not spend as much on provider payments as CDE expected. (CDE can reduce an AP agency's allocation in future years if the agency is consistently unable to spend all of its provider payment allocation.) Not facing midyear reductions provide AP agencies with some fiscal stability. Such stability is particularly valued by AP agencies, as regulations restrict the amount of funding AP agencies can hold in reserve.

Figure 13

Key Characteristics of Alternative Payment Agencies

Our office conducted a survey of California's Alternative Payment (AP) agencies in May and June 2015. Below, we share some of the survey results.

Survey Information

63 Responding AP Agencies / 78 AP Agencies = 81% Response Rate

Responding agencies' share of statewide voucher caseload = 87%

Tenure and Locations

Average Length of Time in Business = 30-40 Years

Number of Offices Statewide = Over 100

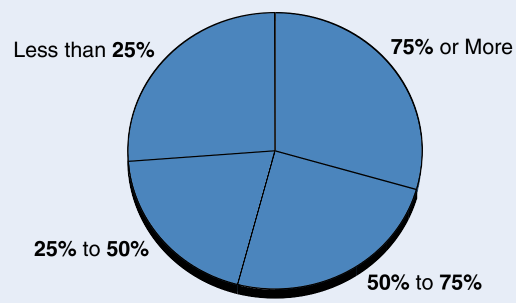
Other Activities/Funding

Of Surveyed AP Agencies:

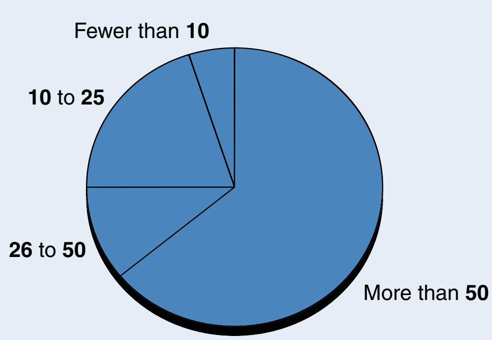
Are Also:
- 70% Resource and Referral Agencies
- 43% State Preschool Providers
- 37% General Child Care Providers
- 33% Early Head Start/Head Start Providers

Also Receive:
- 51% First 5 Funding for Various Activities
- 46% CDE Quality Improvement Funding

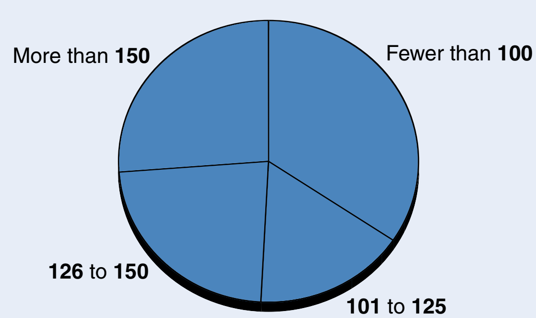
Percent of Total AP Agencies' Budgets Coming From Voucher Programs



Number of Employees Per Agency



Average Family Cases Per Caseworker



If CalWORKs provider payments turn out to be higher than budgeted and CDE provides the AP agency with more funding midyear to cover these additional costs (for example, due to higher-than-expected CalWORKs caseload), the AP agency also will receive a proportional increase in operational funding.

Funding Model Different for Stage 1 CalWORKs. County welfare departments that use AP agencies to run Stage 1 negotiate the amount they pay AP agencies as part of the contract process. In one large county, AP agencies that serve Stage 1 families receive a certain amount for each case they serve. In other counties, AP agencies that serve Stage 1 families receive a set percentage of the payments they make to providers.

Assessment

Current Funding Model for AP Agencies Has Some Connection to Underlying AP Cost Drivers . . . Since AP agencies' main workload is related to determining family eligibility and processing associated child care payments, their operational costs are driven primarily by their caseload and the wages they offer to staff managing that caseload. The current AP funding model has some connection to these cost drivers. AP agencies receive more operational funding when the child care providers they reimburse serve more subsidized children, which, in turn, affects AP agencies' own caseload. Somewhat similarly, AP agencies also receive more operational funding when the child care providers they reimburse pay higher wages for their staff. These higher wages become reflected in the prices child care providers charge, which, in turn becomes reflected in provider reimbursement rates. As AP agencies' operational funding is linked to a share of provider reimbursements, higher wages offered by providers effectively allow the AP agencies reimbursing them to offer higher wages to their own staff.

. . . But Two Key Components of the Funding Model Are Not Tightly Linked With Underlying Cost Drivers. Although the current AP funding model has some connection to AP agencies' underlying cost drivers, two components of the model are not tightly linked to these cost drivers. Specifically, AP funding varies according to the age of the child receiving care and type of child care that families seek. AP agencies, for example, receive more operational funding for an infant than a preschool-aged child receiving child care, even though the amount of associated AP workload is the same for both types of children. Similarly, AP agencies receive more operational funding for children receiving care in centers than family child care homes, though, again, the amount of associated AP workload is the same for children in the two settings. Taken together, these two components generate substantial differences in AP funding levels without justification. An AP agency that reimburses providers serving 100 infants in full-time center care, for example, receives on average more than double the amount of an AP agency that reimburses providers serving 100 school-aged children in full-time family child care homes—despite the two AP agencies having virtually identical workload checking these families' eligibility and processing their voucher payments.

Despite No Change in Workload, AP Agencies' Funding Levels Fluctuate When Provider Rates Change. Because operational funding for AP agencies is based on a share of provider payments, their operational funding fluctuates when the state changes its reimbursement rates. For example, when the state decreased the reimbursement rate for license-exempt providers in 2011-12, AP agencies' operational funding, in turn, collectively was reduced by nearly $7 million. (The effect on each AP agency varied, depending on the number of license-exempt cases they served.) Likewise, when the state increased the RMR for all settings in 2016-17, AP agencies, in turn, collectively received an additional $9 million in operational funding. In both cases, neither AP agencies' caseload nor mission changed, but their funding levels fluctuated.

A New Funding Model Would Not Need to Give AP Agencies With Small Voucher-Based Caseloads Special Treatment. In thinking about alternative ways to fund AP agencies, we examined if AP agencies with smaller voucher-based caseloads might warrant higher per case operational funding levels given their lack of economies of scale. We found, however, that AP agencies' voucher-based caseloads are not a particularly good indicator of their costs per case. This is because many AP agencies receive funding from other sources. For example, of the ten AP agencies that responded to our survey with less than $200,000 in voucher-related operational funding, their total funding from other sources ranged from $620,000 to $2.8 billion. With so many AP agencies also serving as R&Rs and having other funding sources such as State Preschool and General Child Care contracts, few AP agencies are so small that they do not benefit from any economies of scale. Moreover, the state does not mandate that a certain number of AP agencies operate in California. If a small AP agency finds it cannot cover its operational costs with the amount of operational funding the state is providing, then it may consolidate with another, presumably larger AP agency and merge their caseload. These factors suggest that a new funding model does not need to provide proportionally higher state funding rates for smaller AP agencies.

A New Funding Model Could Help Clarify Expectations About AP Agencies' Support Services. In thinking about alternative ways to fund AP agencies, we also sought to determine how much AP agencies currently spend on support services for families and providers. Data on this spending is not widely available, but we think AP agencies that receive relatively high operational funding levels likely offer more support services. Under a new, more straightforward funding model for AP agencies, the state likely would have an easier time both determining how much AP agencies spent on these support services and setting expectations for the type and extensiveness of such services it wanted all AP agencies to provide.

Recommendations

Adopt a Per-Child Funding Model. We recommend the state provide funding to AP agencies for operational costs based on the number of children served, not the amount allocated for provider payments. Under this model, AP agencies' funding would be more closely tied to its primary driver of workload. If the shift were cost-neutral, the Legislature could adopt rates that result in the same level of total AP agency operational funding. In 2016-17, we estimate that average operational funding is $1,325 per child.

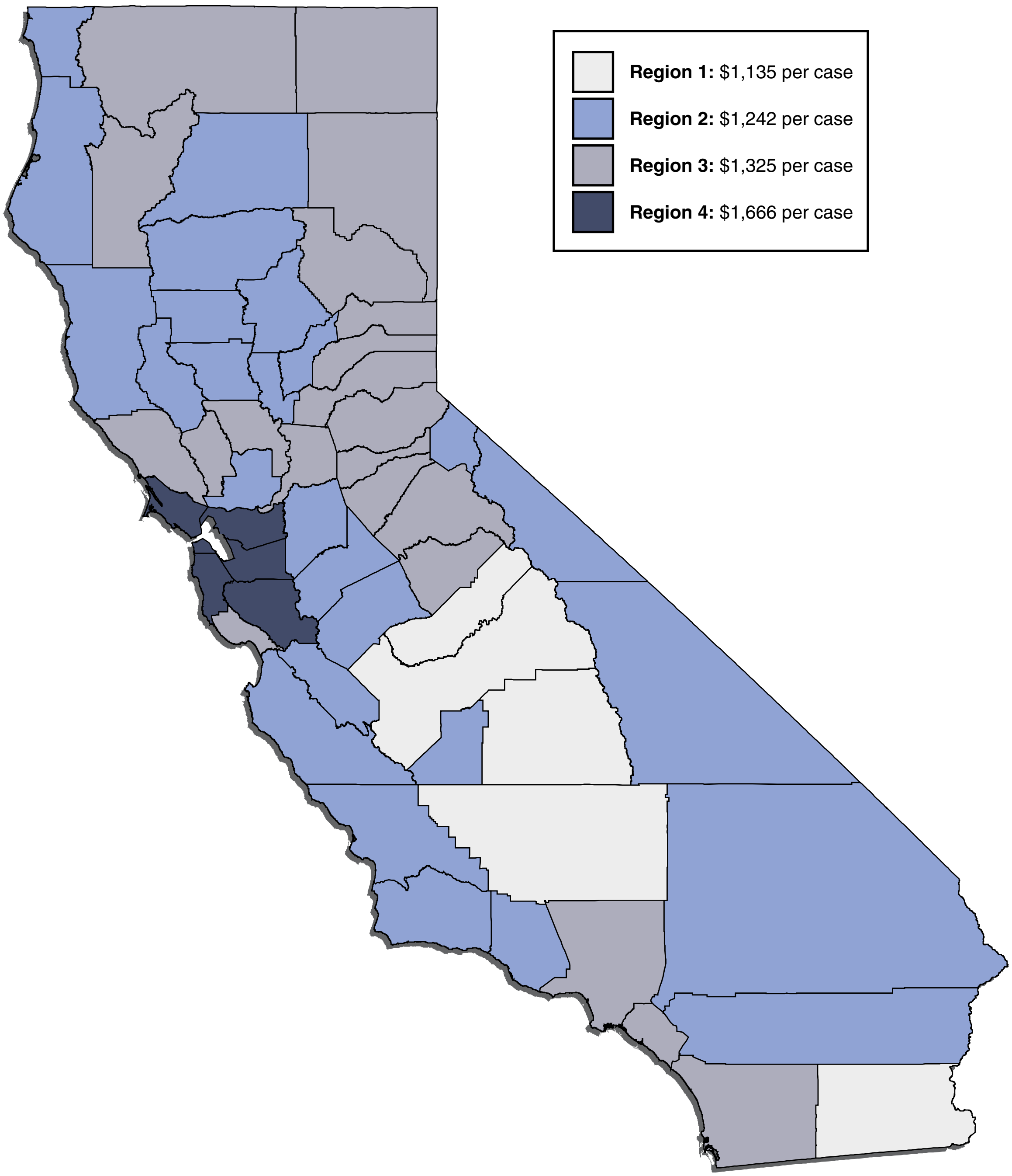
Adjust Per-Child Rates Based on Regional Wage Data. Because costs can vary significantly across the state, we recommend the state adjust per-case operational funding rates based on regional wage data collected by the Employment Development Department. Based on our review of existing data, we think a reasonable approach would be to set four per-case rates across the state. Figure 14 shows which counties fall into each group and possible per-child rates assuming total operational funding and caseload equivalent to 2016-17.

Apply COLA to Rates in Subsequent Years. We recommend the state apply a COLA to the regional per-child rates so that they keep up with the cost of doing business. The state could use the same COLA factor that it currently uses for the state's child care, preschool, and K-12 programs.

Periodically Review Regional Adjustments. To ensure that the per-child rates remain connected to regional costs over time, we recommend the Legislature review the rates periodically (for example, every three years) and determine whether (1) the number of current categories reflects the variation in wages across the state, (2) any counties should be moved into a different category, and

Figure 14

Recommended Regions and Per-Child Rates



(3) the rate differential between categories is aligned to differences in regional wages.

Set AP Agencies' Initial Allocations and Make Midyear Adjustments Using Existing Budgetary Approach. Similar to the current process, we recommend CDE use budget projections of CalWORKs child care caseload and prior-year Alternative Payment program caseload to determine total caseload for each AP agency. We then recommend that CDE multiply these caseload estimates by the regional per-child operational funding rate to calculate the amount for each AP agency's operational costs. We also recommend continuing to guarantee AP agencies a minimum amount of operational funding based on CDE's initial caseload estimates. This would provide budget stability to an AP agency whose caseload unexpectedly declined. (The CDE could reduce funding in future years if caseload did not return to higher levels.) If an AP agency serves more cases than projected over the course of the year, we recommend providing it with more funding based on the agency's per-child funding rate.

Phase In New System Over Period of Several Years. We recommend the Legislature separate the funding model for AP agencies' operational costs from provider payments beginning in 2017-18. Since AP agencies' effective per-child rates currently vary, we recommend the new operational funding rates be phased in over several years to minimize disruption to agencies. A longer phase-in period would allow for a smoother transition, particularly for AP agencies that will see a decline in their per-child rates. The trade-off, however, is that a longer phase-in preserves existing inequities for a longer period of time.

Set Standard Expectations for Family and Provider Support. Moving forward, we recommend the Legislature clarify AP responsibilities in terms of family and provider support. For example, the state could require that AP agencies screen families to determine eligibility for other health and human services programs and refer them to the appropriate agencies. Alternatively, the state could require that AP agencies make certain training programs available for parents. Setting these expectations would ensure families and providers across the state receive the same level of assistance from their AP agency. If the Legislature wants to increase support expectations such that the going per-child funding rates likely are too low to cover associated costs, it could increase the per-child rates moving forward. With a per-child funding model, such rate increases would be straightforward to implement and distributed equitably across the state, ensuring that AP agencies receive increases proportional to their increased costs.

SUMMARY OF RECOMMENDATIONS

Preschool

- Reject proposal to allow part-day State Preschool programs to serve children from families exceeding the income threshold. If providers cannot earn their contracts, recommend redistributing unearned funding to other part-day State Preschool providers that can serve additional low-income children.

- Allow all types of providers, not only local education agencies, to apply for full-day State Preschool slots if additional slots are funded over the next few years. Over longer term, consider options for encouraging local education agencies to run more full-day State Preschool programs. Such options include (1) addressing funding disparities between State Preschool and Transitional Kindergarten or (2) changing eligibility requirements so that each program serves a distinct group of students.

- Reject three proposals that make certain changes to licensing, staffing, and program duration requirements for certain State Preschool and Transitional Kindergarten providers. Instead, pursue alignment more holistically by reconsidering eligibility criteria, program standards, and funding levels in tandem.

- Adopt Governor's proposal regarding program duration for Transitional Kindergarten and Kindergarten programs, but, in tandem, establish differential funding rates for full-day and part-day programs.

Quality Improvement Activities

- Retain funding for Resource and Referral agencies, Local Planning Councils, licensing enforcement, and evaluation of quality improvement activities ($34 million total).

- Repackage $21 million from seven programs operated by county-level support entities into a single county block grant. Allow county-level support entities to serve all types of providers. Require county-level support entities to identify a lead agency and develop a plan for spending block grant funds. Require lead agency to report annually on how funds are spent.

- Retain funding for remaining programs (nearly $23 million), but use planned evaluation funding to hire an independent evaluator to assess them over the next several years, starting with the largest programs in 2017-18. Revisit funding levels in the future based on the results of the evaluations.

Alternative Payment (AP) Agencies

- Provide operational funding to AP agencies based on the number of children served. Adjust per-child rates based on regional wage data and apply a cost-of-living adjustment in subsequent years.
- Base AP agencies' operational funding on caseload estimates. If an AP agency serves more cases than projected over the course of the year, provide it with more funding based on the agency's per-child funding rate.
- Phase in new system over several years. Moving forward, clarify AP responsibilities in terms of family and provider support.

LAO Publications

This report was prepared by Virginia Early, and reviewed by Edgar Cabral and Jennifer Kuhn. The Legislative Analyst's Office (LAO) is a nonpartisan office that provides fiscal and policy information and advice to the Legislature.

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