Looking Into New Mirrors: Lessons for Early Childhood Finance and System-Building
By Louise Stoney. Horizons Initiative, 1998.
http://www.earlychildhoodfinance.org/pdf/mirror.pdf

Providing affordable early care and education for families of all income levels requires that we redesign the way the sector is financed. The field needs new strategies for developing and managing multiple funding streams, while promoting quality and choice. In order to help early childhood education advocates "think outside the box," Stoney examines finance and service delivery models from other policy areas. A few themes run through these four cases that offer important lessons for early care and education.

- Public investment is viewed as economic development, rather than charity.
- A wide range of public sector funding strategies are used to provide assistance to families of all income levels, through direct aid, portable assistance, and effective tax policies.
- Public policy encourages private sector involvement, both financially and through organizations for accreditation and quality monitoring. Private sector actors become important stakeholders in lobbying for increased public involvement.

Health Care. The health care system effectively structures networks of small private providers to achieve economies of scale, while promoting consumer choice and quality.

Higher Education. The higher education finance system has developed flexible models for student financial aid that leverage multiple funding sources and are designed to make it possible for all students to attend college.

Transportation. The transportation sector combines public and private funding sources to ensure that users do not have to pay the full cost of services.

Housing. Tax incentives for housing are designed to help families of all income levels, and affect a variety of private sector actors, including housing providers, private lenders, and households themselves.

Models from Health Care: Using Provider Networks to Ensure Quality and Consumer Choice

Stoney examines the US health care provision model in order to gain insight on possibilities for a child care system. She notices several similarities between the ways that individuals and families purchase early childhood care and health care. First, both sectors are comprised of many small private sector providers. In both sectors the quality of services is critical, but choosing a provider can be difficult and consumers often have little time and information to make informed choices.

Stoney picks out a number of lessons from health care delivery systems that can be applied to child care.

- Health care management organizations assign a primary physician responsible for coordinating all care, including referrals. Families receive comprehensive services from a range of providers. This system serves to balance quality, accountability, and choice.
- Providers form alliances and joint ventures to achieve administrative efficiencies. They contract as a coordinated entity to save the time and resources of individual providers and to give them more power in the field.
- Health care has an accreditation and licensing system that monitors and assures quality.
- Health care has been transformed from a "cottage industry" to a large corporate structure in which practitioners must work together and in which they are able to share knowledge and resources.

Child Care Management Organizations, based on the health care model, would have the following features to ensure quality, access, and choice:

- **Primary practitioner.** Each family would have a primary practitioner responsible for coordinating the family's child care and early education needs. This would help establish continuity and communication among various caregivers, coordinate financing and service delivery, and facilitate transitions to school.
- **Out-of-network providers.** Parents within a CCMO would always have the option of using an out-of-network provider and being reimbursed up to some capped level.
- **Networks that promote quality.** CCMOs could enhance quality if they had flexibility to select providers and establish rates. For example, agencies could admit only programs that meet higher standards or become nationally accredited. Out of network providers would be paid less and have no direct agency contact.
- **Quality assessment.** Each provider would be licensed by the state, with some Managed Care Organizations having their own certification criteria and program accreditation.
- **Administrative efficiencies.** CCMOs could remove some administrative burden from individual providers and could contract with families as a corporate entity.

While HMOs provide interesting lessons for child care advocates concerned with developing better provider networks, Stoney does not address the many problems of managed care. Exploring these problems would help us better evaluate the model.

[Back to top]

Models from Higher Education: Developing and Managing Multiple Sources of Funding

There are both parallels and striking differences between the finance systems for higher education and early care and education. One of the most important differences is that tuition represents only 18% of revenue in public higher education institutions and 41% in private higher ed. By contrast, parent fees represent 72% of revenue in center-based child care. There are many lessons that the early care and education field can learn from higher education about how to structure and manage multiple sources of funding:

- Federal, state and local funding for higher education is not limited to low-income families but is available to families of all income levels.
    - In early education, resources are targeted to low income families. This often results in economically segregated environments.

- Institutions of higher education receive direct public support in addition to the portable aid (grants and loans) that students receive.
    - Restructuring the early childhood care and education financing system so that programs may receive direct aid and portable student aid would encourage diversity and help to improve the quality of all early childhood programs and make it easier for moderate income families to afford the services. Direct aid could be made available as "base funding" to lower parent fees or as "special purpose funding" used to support specific initiatives. Student-based aid could be made available in ways designed to assist families who can't afford full fees. (Currently direct funding and portable child care vouchers cannot be mixed.)

- Higher education scholarships, grants, and loans are designed to cover the difference between the tuition charged by the college and the family's ability to pay.
    - Loans may be beneficial for early education if repayment is spread over many years and the interest is tax-deductible. This is especially true for middle- and higher-income families.

- Institutions of higher education have built endowment funds.
    - Developing endowment funds for early education may be difficult because families who are being served are often unable to contribute to a fund, and donors don't see links between early education and later success. However, it may be possible to establish a community-wide endowment fund that is built by a local community foundation.

- Tax benefits for higher education offer substantial help for middle-income families and are indexed for inflation.
    - The child care tax credit is capped at low levels and hasn't increased over time.

- Standard application forms for assessing need and ability to pay have been developed in the higher education system. This simplifies the process for families and encourages them to assemble a "package" of assistance from a number of sources.
    - It is nearly impossible to measure the use of and need for assistance in paying for child care since so many systems are involved in eligibility determination and

multiple methods are used to determine need. Some early childhood programs have developed methods to coordinate early childhood funding streams so that multiple sources can be used for a single program and/or child, but this is difficult and requires breaking or challenging a few rules.

- Government funders rely on private accrediting bodies, with expertise in evaluating colleges and universities, to ensure that programs meet standards of quality.
    - Early childhood accreditation could be adopted by all funding sources (federal, state, and local governments, school districts and private sector funding sources) as a common standard for high-quality programs. Funding sources would work together to ensure that early childhood programs received the support they need to achieve accreditation.

[Back to top]

Models from Transportation: Encouraging Public and Private Investment

Stoney points out in this chapter that there are some important similarities between transportation and early childhood care and education. Both provide essential services needed by the entire community. Both often rely on user fees, but the total cost of services is greater than the users can reasonably be expected to afford. Finally, both use a combination of public and private financing strategies. Despite these similarities, the child care sector can learn a number of lessons from the way that transportation is financed.

- Public subsidies for transportation are designed to help families at all income levels. With public transit, for instance, federal subsidies primarily support capital costs, which prevents these charges being passed on to consumers. Operating assistance is also often available, and fares generally provide only about 30% of transit system revenues. Any subsidies to low-income individuals are provided completely independently of operating or capital assistance.
    - In early childhood programs, by contrast, government funding sources can generally not be combined. Subsidies to centers are usually provided in lieu of subsidies to users, and no operating subsidies are available to keep costs down for middle-income families. Furthermore, federal funds cannot be used for capital costs.

- Public spending on transportation is viewed as economic development, rather than charity. Thus, policies are designed to encourage private sector investment. Federal funds, for instance, are often used to leverage private sector lending for transportation improvements. In New York State, private entities are allowed to apply for state matching funds.
    - Early childhood care and education policy, by contrast, has generally not recognized the sector's importance in generating local jobs, income, and tax revenue.

- Public sector transportation financing has often been structured to provide economic incentives, rather than regulation and monitoring, to ensure that contractors meet performance standards. For instance, funding may require that contractors rent the lanes they repair. This provides an incentive to work quickly and to work at off-peak hours, when rental rates are set lower.

    - Similar strategies could be used in early childhood programs, as well. Florida's *Caring for Kids* program provides low-interest loans to child care programs, and forgives the loan principle after two years if the program takes certain steps for quality enhancement.

- Transportation policymakers view the field broadly, and provide support for a number of public services through transportation systems. For instance, funding is available for alternative transportation systems (such as pedestrian and bicyclist projects), as well as environmental mitigation, protection of historic sites, and promoting safety.
    - Early childhood care and education policy should also think broadly about how to meet the field's goals. For instance, policymakers might consider creative methods of providing infant care, whether through encouraging informal care by friends and neighbors, or by allowing paid parental leave.

[Back to top]

Models from Housing: Using Tax Policies to Help Families Afford Needed Services

The federal Low-Income Housing Tax Credit and the home mortgage tax deduction are useful models for federal day care tax deductions and tax credits for several reasons. While housing tax incentives are treated as an investment and are available to families of all income levels, day care tax incentives are usually viewed as charity and are only available to low-income families. Also unlike day care tax policy, housing tax incentives are designed to affect a wide range of actors, including housing providers, households, and private sector investors.

Low Income Housing Tax Credit (LIHTC)
The LIHTC allows states to grant private and non-profit affordable housing developers tax credits against federal taxes owed for over ten years. Developers sell these tax credits to investors in the private market via intermediaries (both nonprofits and banks). LIHTC investors receive a competitive rate of return from their tax credits. The program is successful because it gives members of the community a reason to invest, and it provides incentives for proper maintenance and for keeping properties affordable for ten to fifteen years.

In the child care field, on the other hand, no federal tax incentives for private sector investment exist. State business tax incentives have been underutilized, in part because incentives are not designed to encourage investment from a broad range of investors, but rather only from employers. In addition, they do not offer a competitive rate of return.

Home Mortgage Tax Deduction
The mortgage interest tax deduction allows homeowners to deduct the interest paid on home mortgages of less than $1 million, and reduces monthly mortgage payments by up to 30 percent. The deduction is very widely used. Some of its advantages are that it is available to families of all income levels, and that it allows a deduction of the full amount of interest paid.

The federal Child and Dependent Care Tax Credit (CDCTC), by contrast, is underutilized, and benefits cover only a small portion of child care costs. Families with incomes below $10,000 can deduct 30 percent of child care expenses, and the percentage declines as income rises. The maximum benefit of $1,440 requires that a family making $10,000 spend nearly half its income on care.

Families can claim larger benefits if their employer sponsors a Dependent Care Assistance Plan, (DCAP). DCAPs allow employees to set aside up to $5,000 of salary in a special tax free account to be used for dependent care expenses. In New York State in 1996, the average family with a DCAP saved approximately $1,500 in federal and state income taxes.

Recommendations for New Child Care Tax Incentives
Stoney suggests a number of possible ways to structure tax policies to better finance child care:

- Give tax credits to developers to provide low rents to day care programs.
- Use tax credits to generate investments in the long-term operating costs of day care programs.
- Allow families to deduct the full cost of day care, and make the CDCTC refundable to benefit low-income families who pay no taxes. Structure CDCTC incentives to encourage higher quality care.

In addition, Stoney argues that the day care community should market current tax benefits to parents and potential investors.

[Back to top]