Developing a Single-Rate System Reimbursement Structure for California

Guiding Principles and Recommendations to: Regionalize the Standard Reimbursement Rate, Revise the Regional Market Rate-Setting Methodology, and Incentivize and Compensate for Quality

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Developing a Single-Rate System Reimbursement Structure for California: Executive Summary

California needs a single, regionalized reimbursement rate system for child care, preschool, and early learning services that achieves the following vision:

1. Compensates all teachers and providers for the true cost of providing care by reimbursing them at rates that reflect the economic diversity of California,[1]
2. Recognizes the costs of meeting varying quality standards and regulations, and
3. Strengthens the ability of the state's mixed delivery system to provide quality early learning options.

California currently has two different and unaligned systems for reimbursing early learning services: child care providers meeting Title 22 standards are reimbursed using a Regional Market Rate (RMR) that accounts for geographic economic cost factors, while directly state-contracted early learning centers that meet Title 5 standards, in addition to Title 22 standards, are reimbursed at a flat Standard Reimbursement Rate (SRR).[2] This unaligned, two-system approach limits access, fails to maximize program quality, and is forcing many child care providers out of business in California.

To create a single, regionalized reimbursement rates system in California for child care, preschool, and early learning services that accomplishes the vision above, California must implement a sequenced process of reimbursement rate reform. **This white paper outlines crucial steps in moving toward a single system: regionalizing the Standard Reimbursement Rate, revising the Regional Market Rate-setting methodology, and incentivizing and compensating for quality.**

To regionalize the SRR, California should:

- Hold all providers harmless, ensuring that no child care providers and state-contracted centers receive a lower reimbursement than their current rate.[3]
- Revise the RMR survey methodology to redefine age groups so that age groups are aligned across program standards (Title 5, Title 22).
- Create a new county Standard Reimbursement Rate that reimburses all programs at the current RMR ceiling of their county (Base Rate), incentivizes quality by providing additional funding (adjustment factors) for meeting higher quality standards and contracting burdens for Title 5 programs, and incentivizes full-day programs.

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[1] The National Academies of Sciences, Engineering, and Medicine's recently released report, "*Transforming the Financing of Early Care and Education"* defines true costs of high-quality early care and education as the costs inclusive of resources for improving the quality and availability of professional learning during ongoing practice, and supporting well-qualified educators and administrators with adequate compensation through complete wage and benefit packages that are comparable across settings and children's ages. National Academies of Sciences, Engineering, and Medicine. (2018). *Transforming the Financing of Early Care and Education*. National Academies Press.

[2] It is important to note that Title 5 standards build on Title 22 standards; therefore, a program meeting Title 5 standards also meets Title 22 standards.

[3] This is particularly important for Title 5 Infant/Toddler programs, which, due to recent adjustment factor increases, are receiving a considerably higher rate in most cases than Infant programs that are reimbursed through the Regional Market Rate.

- Set annual targets to allocate investments to close the gap between the current SRR and the RMR in each county over a number of years.
- Close gaps between each county's current SRR and RMR at a consistent rate across counties each year through rate increases (in addition to a cost of living adjustment for all counties).
- Evaluate changes to the system and identify course corrections as needed.

To revise the Regional Market Rate-setting methodology, California should:

- Ensure that the next iteration of the RMR survey methodology supports efforts to bring together the two existing reimbursement systems by setting common age ranges and times of care.
- Incorporate a cost analysis in future iterations of the RMR survey methodology and move forward a more robust incorporation of true cost in future rate-setting methodologies.
- Refine the RMR survey and future rate-setting methodologies to address equity issues, and use California's reimbursement rate system to maximize access to early childhood learning opportunities for children in poverty and maximize public benefit.
- Ensure that future iterations of the rate survey or alternative rate-setting process prioritize simplicity and use of real-time data.

As a core principle of this single-rate system, the system will incentivize and compensate for quality. California should:

- Incentivize and compensate for quality through funding enhancements.
- Establish and adhere to consistent measures of quality.
- Clearly and transparently engage and communicate with parents and providers about quality.
- Build infrastructure for quality improvement and quality assessment that supports quality improvement efforts and quality assessment efforts at scale and avoids conflicts of interest by separating the functions of quality improvement and quality assessment to different entities.
- Ensure all providers and early childhood programs have access to quality improvement and quality assessment opportunities and infrastructure.
- Ensure raters are reliable, certified, and do not have conflicts of interest in order to promote inter-rater reliability and increase providers' trust in raters and in the reimbursement rate system.
- Build on the state's quality rating and improvement system (QRIS) progress and systems.
- Develop a sustainable and scalable statewide system.

To address the problems of a bifurcated rate system, resource expenditure should be streamlined and expended in a way that: 1) compensates teachers and programs for the cost of providing care, 2) is responsive to the economic diversity of California, 3) recognizes the costs of meeting varying quality standards, regulations, and contracting burdens, and 4) incentivizes quality and participation in research-based quality improvement efforts as a means to improve child outcomes. Through these reforms, California can achieve a more equitable system to support children and families and maximize public benefit.

Part 1: Developing a Single-Rate System Reimbursement Structure for California

Guiding Principles and Recommendations to Regionalize the Standard Reimbursement Rate

1. Introduction

California has a mixed delivery system that provides child care, preschool, and early learning services for the state's youngest learners.[4] California is strengthened by its ability to provide parents with a choice when it comes to selecting the early learning experiences that are most appropriate for their children and their families. However, California currently has two different and unaligned systems for reimbursing child care providers and state-contracted centers (the Standard Reimbursement Rate System and the Regional Market Rate System). This unaligned, two-system approach limits access, fails to maximize program quality, and is forcing many child care providers out of business in California.

A group of early learning stakeholders, representing elements of both systems, came together to identify guiding principles and recommendations for bringing these two systems into alignment. The goal is to develop a single system of state reimbursement rates for child care, preschool, and early learning services that compensates all teachers and providers for the true cost of providing care, by reimbursing them at rates that reflect the economic diversity of California and the true costs of meeting varying quality standards and regulations.

This document outlines the problems with the current two-rate system and presents a vision of the first step in a reimbursement system that will better meet the needs of California's young children, their families, and their teachers—a regionalized Standard Reimbursement Rate. It also presents a set of assumptions, guiding principles, and recommendations for the first step in a multi-step process to achieve this system. These changes would affect the Standard Reimbursement Rate and Title 5 child care centers tied to this rate system.[5]

2. Problem Statement

A bifurcated rate system and inadequate reimbursement rates complicate efforts to fund and deliver high-quality early care and education (ECE) programs that meet the developmental needs of all children while addressing the health, safety, and wellbeing of the children being served. This current structure and overall lack of funding limit California's ability to increase teacher compensation, adequately resource ECE programs, and incentivize quality improvement efforts.

In the current system, Title 5 programs, which are required to meet higher and more costly quality standards in addition to meeting Title 22 standards, are paid a flat Standard Reimbursement Rate (SRR) of $45.73 per day in every county, regardless of the economic cost

[4] These services currently include licensed family child care, center-based infant/toddler and preschool programs, and friend and family care that meet either Education Code Title 5, Title 22, or health and safety requirements.
[5] Reimbursement rate reform must be accomplished through a sequenced process. This document makes recommendations for the first step in this process.

drivers within that county.[6] Title 22 programs are reimbursed at the Regional Market Rate (RMR) based on the results of the RMR Survey, which considers the private market for child care and preschool services and sets the reimbursement rate for subsidized Title 22 programs at the 75th percentile of the regional market. As a result, Title 22 programs receive a different reimbursement rate depending on the economic conditions of their location. The payment type of different programs/providers is included in **Figure 1** below.[7]

Figure 1

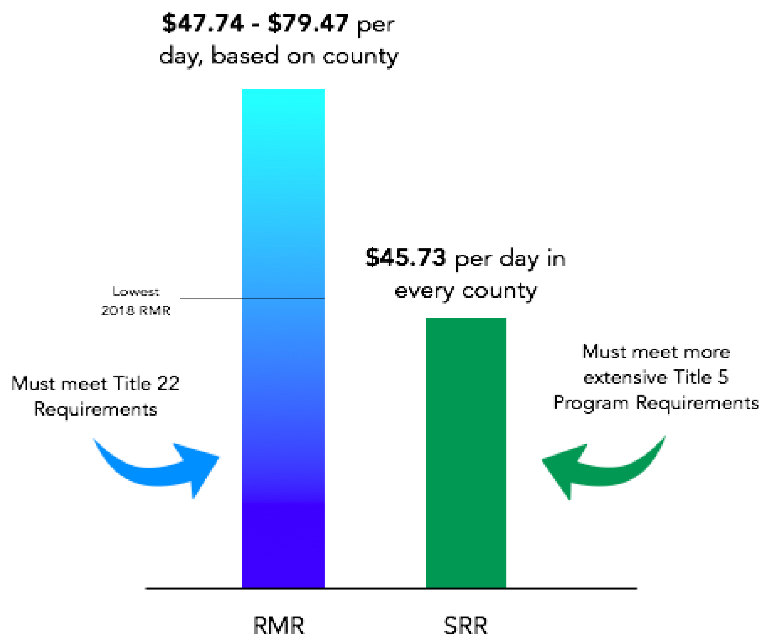
Program	Payment Type
CalWORKs Child Care	Voucher
Alternative Payment	Voucher
General Child Care	Direct contract
State Preschool	Direct contract
Care for Children with Severe Disabilities	Direct contract
Migrant Child Care	Voucher and direct contract

California has conducted a Regional Market Rate Survey since 1992 as a required component of the Federal Child Care and Development Block Grant (CCDBG). Prior to 2002, the survey was conducted by the California Child Care Resource and Referral Network. The methodology used by the Network included a direct survey of a cross section of providers in every county in California and worked well for over 10 years. In 2002, a flurry of state activity related to sole source contracting in all departments forced the California Department of Education (CDE) to put the contract out to bid. The contract was awarded to an out-of-state firm who developed a ZIP code-based demographic profile methodology to determine rates. When the initial survey was released in 2004, there were critiques from stakeholders in the field that the survey created inequities and, in some areas of the state, set lower reimbursement in areas with higher racial diversity. A compromise was reached to roll the ZIP code rates up to a countywide rate; however, the fundamental questions about the effectiveness and shortcomings of the survey methodology were never addressed.

[6] The SRR for a full-day California State Preschool Program (CSPP) reimbursement rate is $45.73 per child day of enrollment (CDE) or $11,432.50 per annum based on 250 days of operation (EC Section 8265[b] and State Budget Act of 2017, Item 6100-196-0001, Provision 3).This rate is used in this proposal instead of the Standard Reimbursement Rate (SRR) for General Child Care (CCTR) and Migrant (CMIG) which is $45.44 per CDE or $11,360 per annum based on 250 days of operation (California Education Code [EC] Section 8265(b) and State Budget Act of 2017, Item 6100-194-0001, Provision 5). This proposal uses the CSPP rate because it is more directly comparable to the January 1, 2018 weekly RMR reimbursement rate for Licensed Child Care (LCC) full-time preschool, which is used in other sections of the proposal. Notably, recent changes to the SRR infant rate will necessitate further review to develop a policy recommendation for aligning the Infant/Toddler SRR rate and the Infant RMR rate. The School-Age rate will also require additional review.
[7] Child Care Programs – Analysis of Governor's Hold Harmless Rate Proposal, March 19, 2018, Legislative Analyst's Office. https://lao.ca.gov/Publications/Report/3787

California's two-rate system is depicted graphically in **Figure 2** below.

Figure 2[8]



To address the problems of a bifurcated rate system, resource expenditure should be streamlined and expended in a way that: 1) compensates teachers and programs for the cost of providing care, 2) is responsive to the economic diversity of California, 3) recognizes the costs of meeting varying quality standards, regulations, and contracting burdens, and 4) incentivizes quality and participation in research-based quality improvement efforts as a means to improve child outcomes.

Efforts to reform California's reimbursement rate system must address the following problems:

1. ECE teachers throughout the publicly funded and private market are undercompensated and have limited support to participate in continuing education and ongoing professional learning.
2. Low reimbursement rates result in an ECE teacher shortage and contribute to excessive turnover as ECE teachers leave the profession. These issues contribute to a limited supply of early education and care opportunities for children.
3. The SRR does not cover the true cost of providing care across different economic regions of the state. In all areas of the state, and some significantly more than others, the SRR is lower than the true cost of providing care (as measured by the RMR survey), further limiting access.[9]

[8] This graphic converts the January 1, 2018 weekly RMR reimbursement rate (LCC full-time preschool) to a daily rate by dividing by five. Starting with the weekly rate that is used by most providers results in a directly comparable daily rate. It should be noted, however, that the RMR Survey uses a different factor to arrive at the daily full-day preschool rate; when sampled center providers do not provide a daily preschool rate, the factor is .24 while for licensed homes it is .2363.

[9] The Regional Market Rate Survey collects the data necessary to determine the reimbursement ceilings for defined geographic areas throughout California. The survey is required by the Federal government every two years. While the

4. ECE programs serving babies, toddlers, and preschoolers—particularly family child care and private preschool providers—have limited access to the quality improvement incentives that exist through California's Quality Rating and Improvement System (Quality Counts California). Furthermore, the incentives that do exist are diffused across the system, and do not always translate to teacher incentives for improvement and ongoing professional development.
5. The current reimbursement rate system does not incentivize quality: preschools and ECE programs that are required to meet more rigorous educational standards (Title 5) in addition to licensing standards (Title 22) are reimbursed less than those that are only required to meet licensing standards (Title 22), creating no financial incentive to implement higher quality standards.
6. A complicated and bifurcated system makes it difficult to communicate with parents and families, community members, and policy-makers about the adequacy of the system and the need for funding for preschool and ECE services.
7. Over 70% of families in California pay for their own child care and preschool services in the market. The subsidy market, which represents 30% of the total child care market, is large enough to affect private rates. Increases in the subsidy can create market pressure on the full system. Many families are unable to pay more for the services they access. This must be considered when adjusting the state reimbursement.

3. Vision

California needs a single, regionalized state reimbursement rate system for child care, preschool, and early learning services that: 1) compensates all teachers and providers for the true cost of providing care by reimbursing them at rates that reflect the economic diversity of California, 2) recognizes the costs of meeting varying quality standards and regulations, and 3) strengthens the ability of the state's mixed delivery system to provide quality early learning options.[10]

This single, regionalized state reimbursement rates system for child care, preschool, and early learning services would help to ensure that:

1. California's diverse ECE teachers/providers are competitively compensated,
2. A tiered reimbursement rate system incentivizes quality by ensuring teachers, child care providers, and early learning programs have access to financial incentives to engage in continuing education and/or ongoing professional learning, quality improvement efforts, and/or the implementation of higher quality standards as a means of improving child outcomes, and
3. Policy-makers understand funding levels and needs, and parents and community members understand the differences in program content and the costs associated with providing high-quality child care, preschool, and early learning services.

Regional Market Rate Survey measures the prices charged for child care in regional markets across the state, many ECE stakeholders have suggested that the survey is assessing a market failure, and that the prices that providers charge are lower than the true costs of providing quality educational services for children. The result is very low wages for caregivers and teachers.

[10] More research is needed to understand the true cost of implementing high-quality early learning programs. The methodology for reimbursing for the cost of quality should be reviewed in light of new research and will need to be revisited once system reforms are implemented.

4. Assumptions: Bringing the Rates Systems Together

The stakeholder group that developed this document made the following assumptions that will impact the process by which a single state reimbursement rate system for child care and direct-contracted centers in California is achieved:

- Regional differences exist, and therefore California cannot have a single statewide SRR. For this reason, the group seeks changes to the current two-rate system to create a system that reimburses all providers in a way that accounts for regional cost differences.
- California does not have the finances to create broad systems reforms in a single year and a phasing-in approach will be required.
- Achieving the ideal single-rate reimbursement system will require interim steps for both the SRR and the RMR.[11]
- Although the RMR is imperfect and does not fully account for the actual cost of providing care or meeting increased quality standards, the RMR provides a mechanism for bringing both systems together as an interim step in a way that accounts for regional differences. Using the RMR also provides an anchor to better connect the California state system and the federal system for child care reimbursements under the federal Child Care and Development Block Grant (CCDBG). This is particularly important given the substantial federal investment that comes to California through CCDBG funding.[12]
- Though it serves as a mechanism for bringing the two systems together, comprehensive changes to the RMR are necessary, particularly a review of the methodology used to determine the rate and adjusting the RMR age categories.[13]

5. Guiding Principles: Regionalizing the Standard Reimbursement Rate

In an effort to make progress towards the shared vision outlined in section 4 and to address the problems specified above, system changes should be made to the Standard Reimbursement Rate system for Title 5 standard-based programs according to the following guiding principles:

6.1. **Comprehensive rate reform will require a multi-step process.** This first step is to bridge the two systems. Next steps in this process must include resolving issues with and exploring alternative methodologies to the RMR survey, and establishing processes and mechanisms to incentivize and reimburse programs within a mixed delivery system for meeting higher quality standards.

6.2. **Hold all programs harmless.** Ensure that no program receives less than its current level of funding as a result of changes to the rate system.[14]

[11] This document outlines the first step in a multi-step process.
[12] Updates to the RMR survey methodology will be required and will need to move in tandem to efforts to bring the RMR and SRR systems together. California should also look to alternative methodologies to the RMR survey, allowable under the federal CCDBG.
[13] Necessary changes to the RMR will be discussed in more detail in a later proposal.
[14] This will be particularly important for Title 5 Infant/Toddler programs that, in most cases, due to recent SRR adjustment factor increases for Infants/Toddler, receive a considerably higher rate than providers that serve Infants in Title 22 settings.

6.3. **Reimburse all programs at a rate that considers regional economic cost drivers.** A single-rate system needs to combine the current two systems while preserving the regional cost considerations currently included in the RMR system.

6.4. **Maintain cost of living adjustments for all counties.** Ensure cost of living adjustments will not be impacted by changes to the SRR rate structure. When cost of living adjustments are allocated by the legislature, these will be distributed equally across counties as a percentage of the contractor's current rate, without being impacted by rate distribution recommendations.

6.5. **Ensure that the single-rate system incentivizes and compensates for quality.** The system should administer reimbursements in a way that incentivizes and compensates for quality by providing funding enhancements to licensed programs that meet higher quality standards, including incentives for offering full-time programs. In the future, any program that demonstrates that it is meeting higher quality standards, regardless of whether it is a Title 5 or a Title 22 program, should receive funding enhancements.[15] Setting an accurate reimbursement level to adequately compensate providers for meeting higher quality standards will necessitate additional research and should be revisited after system reforms are implemented.

6.6. **Allocate investments to close the gap between the current SRR and the RMR in each county over a number of years.** It will take a number of years of increasing state investments to bring the SRR to the RMR level in each county.

6.7. **Close gaps between the RMR and the SRR at a consistent rate across counties.** The gap between the SRR in each county and the RMR in that county should be closed at a constant percentage (ex: the deficit [RMR - SRR] for each county is reduced by 10%). This means that the SRR would increase more for counties with larger deficits ("equal speed deficit reduction").

6.8. **Evaluate changes to the system and identify necessary course corrections.** As policy changes are made to bring the two systems together and the RMR survey is updated, ongoing evaluation and research should be conducted to identify areas were additional changes or modifications to recommendations are necessary.

6. Recommendations

The stakeholder group makes the following recommendations as an initial step towards the vision outlined in section 4:

7.1. **Implement comprehensive rate reform through a multi-step process.** First, bridge the SRR and RMR (see recommendations below). This should be followed by reforms to the RMR survey methodology, exploration of alternative methodologies to the RMR survey, and creation of a tiered reimbursement system that can incentivize and reimburse for quality and quality improvement efforts across different program types. Throughout

[15] While this white paper is specific to regionalizing the SRR, the implications of other uses of a quality adjustment factor were recommended by the working group.

this multi-step process, all programs should be held harmless, ensuring that no program receives less than the current level of funding in the future.

7.2. Use the Regional Market Rate Survey to reimburse all counties at a rate that considers regional economic costs.[16] While the RMR survey is an imperfect assessment of actual costs, it does consider regional cost drivers, therefore, using the RMR to provide a base level of funding for all programs will result in a single system that accounts for regional differences.[17]

7.3. Redefine age groups in the RMR survey so they align across program standards. Revise the age groups in the RMR survey, particularly with regard to the age category in which two-year-olds fall, so that both Title 5 and Title 22 programs have age groups that are defined in the same way.

7.4. Reimburse all programs at the current Regional Market Rate ceiling of their county (Base Rate). Reimburse all providers within a county, at minimum, at the current Regional Market Rate ceiling of the county in which the child care, preschool, or early learning program is administered. (For the purpose of this proposal, reimbursement at the RMR ceiling will be the base rate—see 7.4 for additional explanation.)

7.5. Incentivize Quality:

a. **Provide funding enhancements (adjustment factors) for meeting higher quality standards and contracting burdens.** In addition to the base rate (the county RMR ceiling—see 7.3), provide a funding enhancement or adjustment factor for programs meeting higher Title 5 quality standards and contracting burdens. Use an adjustment factor of 1.23 for Title 5 preschool programs.[18] [19]
b. **Incentivize full-day programs.** Part time programs should be reimbursed at 50% of the Regional Market Rate for the county in which they are administered. This would be implemented at the end of the phase-in period, once programs have reached the maximum RMR ceiling in their county, in addition to the quality adjustment factor (see recommendations 7.6 and 7.7).[20] As described above, part

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[16] Using the RMR Survey would mean the target for reimbursement would change when a new survey is administered. If the RMR survey is administered regularly, these changes should be relatively incremental.

[17] See Part 2 of this document. The working developed an RMR overhaul white paper to follow this document as a policy companion. It considers changes related to age groups, special education factors, and extended hours rate factors among other issues. This document also reviews alternative methodologies that could be used instead of the RMR survey as allowable under federal CCDBG requirements.

[18] The proposed quality adjustment factor of 1.23 for Title 5 preschool programs is based on the cost of staffing to meet 1) lower ratios and increased demand on staff time to meet higher quality standards, and 2) contracting requirements. The adequacy of this adjustment factor should be revisited over time in light of new research. Adjustment factors for Infant/Toddler programs and School-Age care will have to be set separately.

[19] In the future, to incentivize all licensed programs to meet higher quality standards, Title 22 programs that demonstrate that they are meeting all Title 5 standards should receive a quality adjustment factor of 1.2. The proposed quality adjustment factor of 1.2 for Title 22 programs that meet Title 5 standards is based on the cost of staffing to meet lower ratios and increased demand on staff time to meeting higher quality standards. It is lower than the Title 5 adjustment factor because Title 22 programs do not have the same contracting burden of directly contracting with the California Department of Education. The adequacy of both the Title 5 and Title 22 adjustment factors should be revisited over time in light of new research and as implications related to incentivizing quality across program types is better understood.

[20] In this proposal, a full-day Center-Based program is defined as at least 6.5 hours per day, for 250 days per year. A half-

time Title 5 programs would still receive an adjustment factor of 1.23.[21] Furthermore, the hold harmless recommendation would still apply to part-time programs to ensure no program gets less than its current level of funding.

c. **Set a separate Title 5 infant/toddler adjustment factor.** As system changes are implemented and a new RMR survey is conducted, the state will need to conduct a review process to set the infant/toddler adjustment factor.
d. **Set a separate Title 5 school-age adjustment factor.** Similarly, a school-age adjustment factor will need to be set as system changes are implemented and a new RMR survey is conducted.

7.6. Set targets to allocate investments to close the gap between the current SRR and the RMR in each county over a number of years. Because this first step cannot be achieved in one budget year, an SRR "target" should be established for each county based on these two factors, and each year the state should bridge the deficit between the county's current SRR amount and the final county target by an equal percentage increase, after cost of living adjustment (see 7.7 below).

7.7. Close gaps between the SRR and these new county SRR targets at a consistent rate across counties each year with rate increases beyond cost of living adjustment increases. Allocate funding such that the gap between the SRR in each county and the RMR in that county closes by a constant percentage each year until the new SRR target is reached for each county, or "equal speed deficit reduction" (ex: the deficit [RMR - SRR] for each county is reduced by 10%). This will result in greater yearly increases to the SRR in counties with larger deficits.

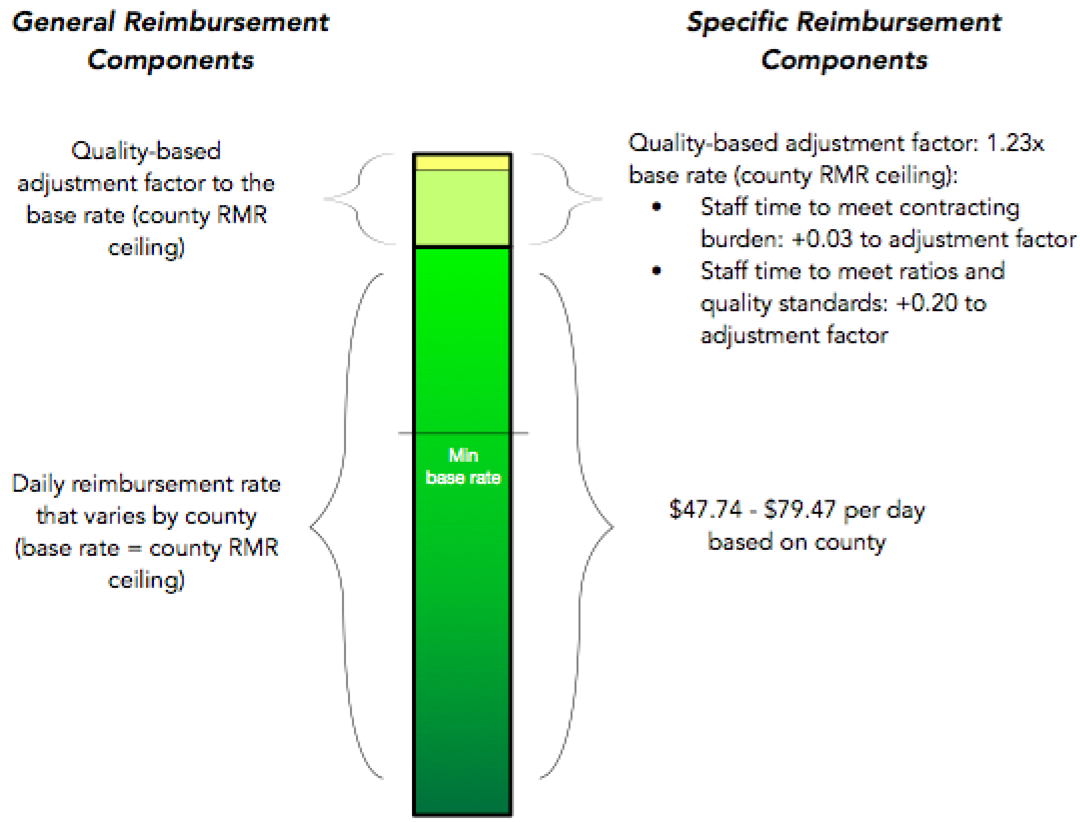
7.8. Conduct ongoing review of rate changes to understand their impacts on the system and make adjustments as needed. Review changes to the system, including changes related to the RMR methodology and new RMR survey results, to understand the impact of recent changes to the SRR Infant/Toddler rate and identify needed changes related to the School-Age rate. Course corrections and adjustments should be made according to the guiding principles outlined in this paper.

The results of implementing these guiding principles are visually displayed in **Figure 3** below:

day program is at least 3 hours per day, for 180 days per year.

[21] In the future, any part-time Title 22 programs that demonstrably meet Title 5 standards would also be reimbursed at 50% of the Regional Market Rate for the county in which they are administered and would receive a quality adjustment factor of 1.2.

Figure 3



7. Conclusion

California must create a single-rate system that accounts for regional cost drivers and the cost of providing quality child care and preschool services. As a necessary first step, the state's SRR must be aligned in each county to the regional costs of care, as currently defined by the Regional Market Rate system, and then adjusted for additional Title 5 costs for quality standards and program administration. Because this first step cannot be achieved in one budget year, an SRR "target" should be established for each county based on these two factors. Each year, the state should bridge the deficit between the county's current SRR amount and the final county target by an equal percentage increase, after cost of living adjustment.

These reforms should be quickly followed with necessary revisions to the RMR survey. Ultimately, a revised RMR can then be used in every county to establish a baseline for reimbursing providers for Title 22 standards. Providers serving children under Title 5 standards will be funded at the RMR plus the Title 5 adjustment factor. Finally, this new system must carefully consider the true cost of operating high-quality programs and participating in quality improvement efforts. The rate system should then be revised as necessary to ensure program quality.

Part 2: Developing a Single-Rate System Reimbursement Structure for California

Guiding Principles and Recommendations to Revise the Regional Market Rate-Setting Methodology

1. Reassessing Revising the Regional Market Rate Survey: Introduction

California has a bifurcated system for reimbursing early learning services. Child care that meets Title 22 standards is reimbursed through the Regional Market Rate (RMR), while state-contracted child care that meets Title 5 standards is reimbursed at the flat Standardized Reimbursement Rate (SRR).

Specifically, the RMR system is governed by the Federal Child Care and Development Block Grant (CCDBG) Act and Child Care Development Fund (CCDF) Final Rule.[22] CCDBG requires regional market rates to be set through a survey developed and administered by individual states.[23] In California, the RMR survey collects the data necessary to determine the reimbursement ceilings for defined geographic areas. The survey began in 1992 and the current methodology (described in 1.1 below) was established in 2005. Regulations require the state to use the most recent survey in determining reimbursement ceilings, but the legislature sets the percentiles for reimbursement ceilings.[24]

The process described in section 1.1 produces reimbursement ceilings, which are used to set the rates for all CalWORKs child care programs—Stage 1, which is administered by the California Department of Social Services, and Stages 2 and 3, which are administered by the California Department of Education (CDE).[25] The rate ceilings are set by care settings, age, and times of service. The types of care include Licensed Child Care Centers (LCCs), Licensed Family Child Care Homes (LFCHs), and License-exempt Family, Friend, and Neighbor (FFN) providers. The categories for children's age include infants under two years of age, preschoolers age two through five, and school-age children six years and older. Times of service include hourly, daily, part-time weekly, full-time weekly, part-time monthly, and full-time monthly care.

Each RMR survey gives results by percentiles, any of which the legislature can choose to implement. Since January 2017, the California legislature has set the RMR at the 75th percentile.[26]

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[22] Child Care and Development Block Grant Act of 2014, 2016 Child Care Development Fund Final Rule https://www.acf.hhs.gov/occ/resource/ccdf-final-regulations

[23] From the CCDF Final Rule: "The reauthorized Act requires the market rate survey to be conducted every three years." https://www.gpo.gov/fdsys/pkg/FR-2016-09-30/pdf/2016-22986.pdf

[24] The RMR survey is currently completed by the contractor ICF Macro. CDE is currently preparing for the 2020 RMR survey. CDE is creating the Request for Proposals (RFP) that will be released in 2018 for bid, according to the established process.

[25] California Health and Human Services Agency, Department of Social Services, December 15, 2014. http://www.cdss.ca.gov/lettersnotices/EntRes/getinfo/acl/2014/14-94.pdf

[26] Child Care Programs – Analysis of Governor's Hold Harmless Rate Proposal, March 19, 2018, Legislative Analyst's

[27] The resulting RMR ceilings are published on the CDE website as approved by the annual budget act.

Per CCDBG, the goal of the rate-setting methodology is to ensure equal access to child care. While states can choose what type of child care providers to survey, the method of data collection, and the procedures for determining a market rate estimate, the RMR must be based on market conditions and comparable to rates paid by non-subsidized families.[28] The RMR must: 1) ensure base payment rates for meeting health and safety standards, 2) take quality of programs into account, 3) ensure providers only charge an affordable amount above the parent co-pay, and 4) ensure reimbursement to providers. The requirement that states include a cost estimate of the costs associated with health, safety, and quality is a new requirement.

One of the benefits of the RMR survey is that it is regularly updated, meaning reimbursement ceilings may be adjusted based on recent data. In addition, the survey is responsive to regional cost differences. Data collection across different geographies is a strength of the survey, because it accounts for the wide variance in cost of living across the state of California. As noted above, the RMR survey captures different prices for different types of care, by age, and by length of time.

However, the current RMR survey has several weaknesses. The survey assesses what rates providers are charging but not the cost of living in each region. For example, in the 2016 survey the highest RMR was Marin, but the county with the highest cost to live self-sufficiently was Santa Clara. San Bernardino showed one of the lowest RMRs but is mid-range in terms of self-sufficiency.

As explained in section 1.1, the RMR survey methodology uses Market Profiles to sample areas; however, Market Profiles also do not consider cost of living. Counties are made up of a set of Market Profiles. Standardized rates are computed for each Market Profile, and the county rate is the composite of the weighted average of Market Profile rates. Market Profiles are developed by considering variables like median income and demographics in an area. As a result, their use in the survey methodology institutionalizes inequitable payment rates: child care providers in those areas charge lower rates to reflect the price that parents they serve can afford to pay.

The existing RMR survey only includes providers that serve the fee-paying market. The current survey does not ask about quality of child care or consider how rates change based on quality. Furthermore, in its current form, the RMR survey looks at the price of child care but not the actual costs. In reality, there is a market failure throughout the state as families struggle—and fail—to afford the actual costs of providing child care.

1.1 Methodology[29]

Fielding for the 2016 Market Rate Survey began in April 2016 and continued into June 2016. The

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Office. https://lao.ca.gov/Publications/Report/3787

[27] From the CCDF Final Rule: "We reaffirm our long-standing position that setting payment rates at the 75th percentile of a recent market rate survey remains an important benchmark for gauging equal access." https://www.gpo.gov/fdsys/pkg/FR-2016-09-30/pdf/2016-22986.pdf

[28] 2016 Regional Market Rate Survey of California Child Care Providers: Final Report, April 14, 2017, ICF Macro.

[29] All information in this section is drawn from the 2016 Regional Market Rate Survey of California Child Care Providers: Final Report, April 14, 2017, ICF Macro.

2016 Market Rate Survey used established sampling and analysis methods used in previous surveys since 2005. The contractor, ICF Macro, employed a mixed-mode data collection strategy using mail, web, and telephone modes. LCCs received the survey packet in English only, while LFCHs received the packet in English and Spanish and were required to contact ICF for surveys in any other non-English language. Using the most conservative American Association for Public Opinion Research (AAPOR) methods for calculating survey outcomes, LCCs had a 40% response rate and LFCHs had a 38% response rate. There were no statistically significant changes from the 2014 survey. Programs are surveyed for any rates they charge distinguished by type of care, age of child, and times of service. LCCs and LCFHs that only serve subsidized children are not included in the survey population, despite approximately 30% of the child care market being subsidized.

Analysis methods included sampling and estimation based on statistical socioeconomic modeling of California's ZIP codes, sourcing provider information from the Community Care Licensing database, sampling LCCs and LFCHs based on the physical locations' ZIP code, and estimating weighted averages of Market Profile reimbursement ceilings. Market Profiles serve two functions: defining sampling strata and setting rates within similar areas (the Market Profile) before rolling up these areas to a weighted county-level rate. County-level rates are based on aggregates of standardized rates computed at the Market Profile level.

Market Profiles are created by first grouping ZIP codes into profiles that share similar socioeconomic and demographic characteristics. The methodology uses characteristics that are determined to have the greatest correlation to child care rates, using regression analysis to predict child care rates for each market profile. Socioeconomic factors that were used to determine Market Profiles include housing unit density, percentage rural population, median home value, percentage of employees with health insurance coverage, percentage family households, percentage of population aged 18 or older with a bachelor's degree or higher, and others. Market Profiles include ZIP codes with similar population sizes. There were nine Market Profiles in the 2016 survey.

The Market Profile estimation strategy is rooted in the belief that the geographic location of a child care provider is less predictive of child care rates than are the socioeconomic and demographic characteristics of the area. ICF Macro argues that this method allows for improved market rate estimates and better allocation of available funds.

2. Opportunity

Recent changes in the federal Child Care and Development Block Grant (CCDBG) require states to analyze the estimated cost of care (including any relevant variation by geographic location, category of provider, or age of child) related to the cost of child care providers' implementation of health, safety, quality, and staffing requirements and the cost of higher-quality care. Furthermore, the final CCDBG rule gives states more flexibility in the methodology they use to identify rates. Market rate surveys and cost-based alternative methodologies can both be used to inform provider payment rate-setting with the goal of supporting access to high-quality child care for families receiving subsidies. With either approach, the data must be current and complete, and the data collection and research methods must be statistically valid and reliable. States and territories can use a market rate or price survey (as is used currently in California), a cost survey, a cost model or calculator, or a hybrid approach.

Given this new flexibility, the time is right to examine current practices in California and review the current RMR survey methodology.

3. Guiding Principles

In an effort to address the problems with the existing Regional Market Rate rate-setting process and survey, system changes should be made according to the following guiding principles:

3.1 **Support efforts underway to create a single reimbursement rate system in California.** This first step towards the vision outlined in Part 1: An Initial Step Towards Developing a Single-Rate System Reimbursement Structure is to bridge the SRR and RMR systems. California must implement a sequenced process of reimbursement rate reform to move the SRR and RMR toward a unified reimbursement system for all California ECE programs. This will amplify the importance and impact of the RMR survey and the rate-setting process. Any process for setting the RMR, whether through the existing RMR survey methodology or through another model, should work towards bridging these two reimbursement rate systems.

3.2 **Incorporate a cost analysis into the rate-setting methodology.** California needs a single, regionalized state reimbursement rates system for child care, preschool, and early learning services that: 1) compensates all teachers and providers for the true cost of providing care by reimbursing them at rates that reflect the economic diversity of California, 2) recognizes the costs of meeting varying quality standards and regulations, and 3) strengthens the ability of the state's mixed delivery system to provide quality early learning options. To achieve that vision, information on the true cost of providing child care, preschool, and early learning services must be collected and analyzed. This cost analysis must consider the true cost of offering services, including the cost of providing early educators with wages and benefits comparable to teachers in TK-12 settings. An analysis of true costs must be considered in the RMR rate-setting methodology.[30]

3.3 **Ensure equity in Regional Market Rate-setting methodology.** As described in section 1.1, the current Regional Market Survey conducts its sampling using Market Profiles, or groupings of ZIP codes that have similar socioeconomic characteristics (ex: similar housing costs, population density, and employment rates). County rate estimates are then calculated as a weighted average of the estimates of the Market Profiles within that county. Because the fees that providers are able to charge families for child care are directly related to the economic conditions of the families that provider serves, setting rates based on cost differences in regional Market Profiles exacerbates inequality and institutionalizes low reimbursement rates for providers that serve children and families in low-income counties. Using the Market Profiles to set a weighted county average within a county sets a rate ceiling that does not reflect the price of care across the county. Finally,

[30] The National Academies of Sciences, Engineering and Medicine's recently released report, "*Transforming the Financing of Early Care and Education*" defines true costs of high quality early care and education, as the costs inclusive of resources for improving the quality and availability of professional learning during ongoing practice and supporting well-qualified educators and administrators with adequate compensation through complete wage and benefit packages that are comparable across settings and children's ages. National Academies of Sciences, Engineering, and Medicine. (2018). *Transforming the Financing of Early Care and Education*. National Academies Press.

because the RMR survey and rate-setting methodology set rate ceilings, providers that charge less than the ceiling to accommodate low-income families are made to accept that lower rate for all subsidized children. This limits the ability of the system to serve children in need. The RMR survey or rate-setting methodology must incorporate a process to more equitably set reimbursement rates.

3.4 **Maintain simplicity and pursue data systems that result in new opportunities and efficiencies.** Every effort should be made to ensure that important information is collected from provider surveys while ensuring relative simplicity of the survey and keeping the time to complete the survey low. The coming years will bring opportunities to use new data systems to gather real-time information related the cost of providing care, the rate parents are charged, and the quality of different providers. Use of these data systems may provide the necessary information to set reimbursement rates, making the Regional Market Survey obsolete. California must assess how new data systems, including cost models and survey tools, might support efforts underway to create a unified Reimbursement Rate system and impact the need for an RMR survey.

4. Recommendations

The stakeholder group that developed this document makes the following recommendations as an initial step to responding to the problems described in section 1 and to support the Guiding Principles detailed in section 3:

4.1. **Ensure that the next iteration of the RMR survey methodology supports efforts to bring together the two existing reimbursement systems.**

a. Set age ranges in the RMR survey methodology so they align with age ranges in the SRR. Use Title 5 age ranges to set Regional Market Rates (birth to 18-month, 18-36 months, 36 months to kindergarten enrollment, school-aged) so the two systems can be brought together.
b. Modify statute to set common times of care that align the two systems.

4.2. **Incorporate a cost analysis in future iterations of the RMR survey methodology and move forward a more robust incorporation of true cost in future rate-setting methodologies.**

a. Meet federal cost analysis requirements by gathering cost information in the next iteration of the RMR survey. According to recent changes in the federal CCDBG, regardless of whether Lead Agencies conduct a market rate survey or use an alternative methodology, they are required to analyze the estimated cost of care (including any relevant variation by geographic location, category of provider, or age of child) related to the cost of child care providers' implementation of health, safety, quality, and staffing requirements and the cost of higher-quality care. The final CCDBG rule allows for the development of a cost-model. The next iteration of the RMR survey and rate-setting methodology should include a true cost analysis, the findings of which should be confirmed and/or informed by cost questions in a survey. Cost-related questions in the survey should examine both costs related to what is being provided (ex: diapers, food, etc.), and costs related to quality.
b. Move towards a heavier emphasis on the true cost of providing quality child care, preschool, and early learning experiences by considering the implementation of a

true cost survey, development of a cost model or calculator, or implementation of another hybrid approach. This cost analysis should consider costs for adequate and competitive staff salaries, training and professional development, curriculum and supplies, group size and staff ratios, enrollment levels and program size, facilities costs, and variations in these costs related to provider type, age of children served, and geography.

4.3. Refine the RMR survey and future rate-setting methodologies to address equity issues.

a. Review the Market Profile methodology and incorporate methods to address the structural impacts of using socio-demographic characteristics to set rates. As noted above, fees providers charge for child care are directly related to the economic conditions of the families that provider serves. Using socio-demographic characteristics to set rates through Market Profiles exacerbates inequality and institutionalizes low reimbursement rates for providers that serve children and families in low-income counties. This could be addressed by adjusting the Market Profile price distribution to remove the lowest prices charged in various Market Profiles. The amount of low-price data "trimmed" from each Market Profile could vary based on poverty rate or other identified factors. This recommendation must be coupled with recommendation 4.3.b below in order to have the desired effect.
b. Use California's reimbursement rate system to maximize access to early childhood learning opportunities for children in poverty and maximize public benefit. To do this, providers must be allowed to charge less than the reimbursement rate ceiling as needed. This, coupled with implementation of recommendation 4.3.a would allow providers to receive a higher reimbursement rate for subsidized children while charging lower rates, as needed, to ensure families not receiving a subsidy (private-pay families) can afford care.
c. Move away from the use of Market Profiles and the inherent structural inequality they create in future iterations of the RMR rate-setting methodology.

4.4. Ensure that future iterations of the rate survey or alternative rate-setting process prioritize simplicity and use of real-time data.

a. Incorporate changes and additions to the current RMR survey methodology (to collect information on cost, to align age groups, etc.) that do not extensively add to the burden on providers to complete the survey.
b. Move towards the use of new data systems to assess prices and costs, eliminating the need for an RMR survey.

Part 3: Developing a Single-Rate System Reimbursement Structure for California

Guiding Principles to Incentivize and Compensation for Quality

1. Introduction

Reimbursement rates impact the ability of child care, preschool, and early learning services to achieve higher levels of quality. Funding rates impact the ability to meet elements of quality such as lower adult-child ratios, higher levels of staffing qualifications, and the ability to retain a qualified workforce. California needs a single, regionalized state reimbursement rates system for child care, preschool, and early learning services that: 1) compensates all teachers and providers for the true cost of providing care by reimbursing them at rates that reflect the economic diversity of California, 2) recognizes the costs of meeting varying quality standards and regulations, and 3) strengthens the ability of the state's mixed delivery system to provide quality early learning options.

California's current mixed delivery system provides child care, preschool, and early learning services for the state's youngest learners.[31] The state reimburses providers of early learning services through a bifurcated system that follows two approaches: child care that meets Title 22 standards is reimbursed through the Regional Market Rate (RMR), and state-contracted child care that meets both Title 5 and Title 22 standards is reimbursed at the flat Standard Reimbursement Rate (SRR). This two-approach system fails to serve child care providers, families, and the state's youngest children by limiting access to early care and education, missing opportunities to maximize program quality, and forcing many child care providers out of business in areas of the state with a high cost of living.

Research clearly demonstrates that the quality of early learning experiences has a major impact on child outcomes. Furthermore, high-quality learning environments are a two-generational strategy to positively impact the lives of both the developing child and their working parent.[32] Streamlining California's dual system for early learning into a single, regionalized reimbursement rates system will positively impact program quality by recognizing the costs of meeting varying quality standards and regulations, and strengthening the ability of the state's mixed delivery system to provide quality early learning options. Any program that demonstrates that it is meeting higher quality standards, regardless of program type, should receive quality funding enhancements.

2. Opportunity

In order to create more high-quality early learning opportunities for California's youngest

[31] These services currently include licensed family child care, center-based infant/toddler and preschool programs, and friend and family care that meet either Education Code Title 5, Title 22, or health and safety requirements.
[32] Gencer, A. (2014). Creating Opportunity for Families: A Two-Generation Approach. KIDS COUNT Policy Report. Annie E. Casey Foundation.

learners, the state needs: 1) a reimbursement rate system that incentivizes quality, and 2) a further-developed system of quality improvement and assessment. California should incentivize quality early learning settings by providing additional funding (funding enhancements) for meeting higher quality standards.

California has an opportunity to examine the way its rate system incentivizes and compensates for high-quality early learning settings. Recent changes in the federal Child Care and Development Block Grant (CCDBG) require states to analyze the estimated cost of care (including any relevant variation by geographic location, category of provider, or age of child) related to the cost of child care providers' implementation of health, safety, quality, and staffing requirements and the cost of higher-quality care. Furthermore, California made recent changes to its quality rating and improvement system (QRIS), Quality Counts California, that move the state in the direction of a single, statewide system of quality improvement supports.

Implementing system reforms to establish different levels of funding for programs meeting higher standards of quality will require a multi-year transition process. As part of this process, key stakeholders, especially parents and providers, will need to be engaged. It will be critical for California to create a system of incentivizing and compensating for quality in which the needs of all stakeholders are addressed.

3. Guiding Principles: Developing a Single-Rate System to Promote Quality

California must incorporate a process for incentivizing and improving the quality of state-supported early learning opportunities through a single-rate system. As the state develops a single-rate system, policies around incentivizing and compensating for quality should be made according to the following guiding principles:

3.1 **Incentivize and compensate for quality through funding enhancements.** As noted in section 1, California's system should administer reimbursements in a way that incentivizes and compensates for quality by providing funding enhancements to licensed programs that meet higher quality standards. In the future, any program or caregiver that demonstrates meeting higher standards of quality, regardless of program type (ex: Title 5, Title 22) should receive funding enhancements.

3.2 **Establish and adhere to consistent measures of quality.** Research demonstrates that the quality of early learning experiences has a major impact on child development and later-in-life outcomes. Families should be able to identify and select high-quality learning options for their children. There must be a consistent, research-based definition of quality and a way to reliably assess standards of quality across the state and across all care settings.

3.3 **Clearly and transparently engage and communicate with parents and providers about quality.** Quality must be embedded in the structure of the reimbursement rate system, and parents and providers must be included in conversations about quality. There are multiple aspects of quality that matter to parents and providers; engagement with these groups should seek to ensure that parents' and providers' needs are reflected in the system.

3.4 **Build infrastructure for quality improvement and quality assessment.** Providing different levels of compensation for meeting higher standards of quality requires robust institutional infrastructure to support quality improvement efforts and quality assessment efforts at scale. Quality assessment, or rating, must be separate from quality improvement services. The offices that support quality improvements should not the same ones that rate the program and determine providers' compensation.

3.5 **Ensure all providers and early childhood programs have access to quality improvement and quality assessment opportunities and infrastructure.** As the early learning system compensates providers at different levels based on differing quality, the potential for quality improvement and continuous improvement must be accessible to everyone. If California's reimbursement rate system is going to compensate providers at different rates for increasing levels of quality, quality improvement supports and opportunities for quality assessments must be available to all providers across all care settings in a consistent statewide structure. This requires accessible infrastructure and systemic and differentiated supports.

3.6 **Ensure raters are reliable and certified, and that raters do not have conflicts of interest.** The raters who assess quality must be well-trained and consistent. Ensuring that raters adhere to certification requirements will promote inter-rater reliability and increase providers' trust in raters and in the reimbursement rate system. Additionally, to have the trust of providers, it is important to have state-level raters, so no programs or providers rely on peer agencies for their ratings.

3.7 **Build on the state's quality rating and improvement system (QRIS) progress and systems.** California must affirm the lessons it learned through the development and implementation of a regional QRIS system by separating the rating process from the quality improvement systems. California should build upon the state's progress where appropriate.

3.8 **Develop a sustainable and scalable statewide system.** Quality assessments, or ratings, must be completed in a cost-effective way that does not put additional burden on early learning providers and programs. Ratings and assessments should be developed and administered at the state-level.

4. Recommendation

The early learning stakeholder group recommends an examination of how the guiding principles above would translate to policy and practice across all care settings and statewide, what they would cost the early learning and care system, and how they should be administered within an evolving early learning landscape.

Appendix

Workgroup List

Thank you to the following individuals who served on the Reimbursement Rate Workgroup:

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