Spend or Transfer, Federal or State?

Considerations in Using TANF and TANF-Related Dollars for Child Care

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Introduction

Under the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), states have broad discretion in using their Temporary Assistance for Needy Families (TANF) dollars and state maintenance of effort dollars. A state wishing to do so can use this discretion to expand the availability of child care assistance to low-income families. States have multiple options: a state can directly spend TANF dollars on child care; can transfer TANF funds to the Child Care and Development Fund; can transfer TANF funds to the Title XX Social Services Block Grant; can (to at least some extent) spend Welfare-to-Work grant dollars on child care; and can spend state "maintenance of effort" funds for child care. The array of options can sometimes be confusing because different consequences attach to each choice. This document summarizes the choices and their consequences.

In brief, the key conclusions are:

- **Direct Expenditure of TANF Funds:** A state can spend an unlimited amount of its TANF funds directly for child care assistance for needy families. However, there are significant disadvantages in taking this approach. First, under current HHS interpretations, most TANF funds directly spent for child care will count as TANF "assistance," meaning that a month of TANF-funded child care assistance will count against TANF time limits and that a family receiving TANF-funded child care assistance will be required to assign its child support to the state as a condition of receiving assistance. In addition, TANF funds directly spent for child care are not subject to the protections and other rules governing the Child Care and Development Fund[1].

- **Transfer of Funds:** A state can transfer up to 30% of its TANF funds to the Child Care and Development Fund and can also transfer up to 10% of its TANF funds to the Title XX Social Services Block Grant (provided, that the total amount transferred to CCDF and Title XX cannot exceed 30% of the state's TANF block grant.) One key virtue of transferring funds is that they will be subject to the rules of the block grant (CCDF or Title XX) and not be treated as TANF assistance. A key advantage of transferring to CCDF is the facilitation of integrated and coordinated state planning. The principal advantage of a transfer to Title XX would be in the very limited circumstances where a state wishes to expend funds for child care assistance in a manner that is restricted by CCDF rules.

[1] The U.S. Department of Health and Human Services has adopted the approach of referring to the multiple funding components comprising the Child Care and Development Block Grant (CCDBG) as "the Child Care and Development Fund."

- **Welfare-to-Work Grant Funds:** An entity may spend WtW grant funds on child care assistance for eligible individuals if the service is not "otherwise available." However, it is not clear how a determination is made as to when child care is "otherwise available."

- **Expenditure of State Funds:** If a state is considering expanding state funding for child care, it is necessary to distinguish between two distinct TANF maintenance of effort (MOE) requirements: the basic TANF MOE requirement and a separately determined requirement that must be satisfied in a year in which a state seeks access to the federal Contingency Fund. Under many (but not all) circumstances, spending of state funds for child care assistance to needy families will count toward basic TANF MOE requirements; however, expenditures on child care do not count toward Contingency Fund MOE requirements. Accordingly, it will be important to understand and weigh the Contingency Fund consequences when determining whether to commit additional state funding (as opposed to, for instance, transferring additional TANF funding to CCDF).

- **The TANF Caseload Reduction Credit:** Alternative methods of spending for child care have different consequences in determining whether the child care spending helps the state to qualify for (or qualify for a larger) TANF caseload reduction credit. The state can benefit if the TANF funds are transferred to another block grant or if state funds not counting toward TANF MOE are used; the state cannot benefit if TANF funds are directly used or WtW funds are used; and it is not yet clear if the state can benefit if state funds counting toward TANF MOE are used.

The following pages provide a considerably more detailed explanation of the alternatives and their pros and cons.

Before proceeding to the analysis, one cautionary note is needed. The following discussion is <u>not</u> intended to be suggesting that a state should reduce or restrict TANF assistance or otherwise curtail the availability of needed cash assistance and employment and training services for needy families in order to fund child care expansions. Rather, this discussion is written in the recognition that with continuing caseload declines, many states now face the question each year of how to best spend their "TANF surplus," and that expending some or all of that surplus on expanding child care could provide important assistance in helping low income parents enter or retain employment, while promoting the well-being of their children. In instances where a state has decided to spend TANF-related funds on child care, it is helpful to understand the implications of each alternative.

1. Spending TANF Block Grant funds Directly On Child Care Assistance

A state can spend TANF funds directly on child care for needy families. However, there are significant disadvantages in taking this approach. When the state spends TANF funds directly for child care, those funds will usually be considered "assistance," for TANF purposes, meaning among other things, that any month of TANF-funded child care assistance will count against the federal TANF time limit,

and that families will be required to assign their child support rights to the state (and the state will be required to turn over the federal share of that child support) as a condition of receiving the assistance. In light of these troubling consequences, it will usually be preferable for a state wishing to expand child care spending to use other approaches (discussed below) rather than directly spending TANF funds on child care assistance.

As an initial matter, it is clearly permissible for a state to expend TANF funds on child care assistance.[2] There is no statutory limit on the share of the TANF block grant that can be spent on child care assistance. In order to spend federal TANF funds directly on child care assistance, the assistance must be for "needy families" as defined in the state's TANF plan. There is no federal definition of "needy," so it appears that the state has broad discretion to set its own definition of "needy." While HHS has not addressed the question, it appears that a state could elect to set one income guideline for TANF child care assistance and a different (higher or lower) income guideline for TANF cash assistance.

If TANF funds are directly expended for child care (as opposed to transferred to CCDF or the state's Title XX Program), then they are subject to TANF rules rather than to the rules of CCDF or another block grant. Most significantly, most direct child care expenditures with TANF funds will be considered "assistance" for TANF purposes, according to proposed HHS regulations.[3] The preamble to the proposed rules explains:

> In the proposed rule, we are clarifying that child care, work subsidies, and allowances that cover living expenses for individuals in education or training are included within the definition of assistance. For this purpose, child care includes payments or vouchers for direct child care services, as well as the value of direct child care services provided under contract or a similar arrangement. It does not include child care services such as information and referral or counseling, or child care provided on a short-term, ad hoc basis.

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[2] There are two alternative bases on which the state can spend TANF funds on child care. First, states can spend TANF funds in any manner reasonably calculated to accomplish the purpose of TANF; one of the purposes of TANF is to "end the dependence of needy parents on government benefits by promoting job preparation, work, and marriage;" another purpose is to " provide assistance to needy families so that children may be cared for in their own homes or in the homes of relatives."

Second, a state may expend TANF funds in any manner that the State was authorized to use amounts received under Title IV-A of the Social Security on September 30, 1995, or, at state option, August 21, 1996; on either of those dates, Title IV-A included the AFDC Child Care, Transitional Child Care, and At-Risk Child Care Programs.

[3] [Proposed] 45 C.F.R. §270.30 , 62 Fed. Reg. 62182, defines "assistance for TANF purposes as follows: "Assistance means every form of support provided to families under TANF (including child care, work subsidies, and allowances to meet living expenses), except: services that have no direct monetary value to an individual family and that do not involve implicit or explicit income support, such as counseling, case management, peer support, and employment services that do not involve subsidies or other forms of income support; and one-time, short-term assistance (i.e., assistance paid within a 30-day period, no more than once in any twelve-month period, to meet needs that do not extend beyond a 90-day period, such as automobile repair to retain employment and avoid welfare receipt and appliance repair to maintain living arrangements)."

62 Fed. Reg. 62132. What are the consequences if child care is provided with a TANF dollar and treated as "assistance?"

- **Time Limits:** Any month in which a family that includes an adult receives child care assistance funded with a federal TANF dollar will count as a month of assistance for purposes of the federal sixty month limit (i.e., the prohibition on using federal TANF funds to provide assistance to a family that includes an adult that has received federally-funded TANF assistance for sixty months, subject to allowable exceptions for 20% of a state's cases).

- **Participation Rates:** For any month in which an individual receives TANF-funded child care assistance, the individual will count for purposes of federal TANF participation rates (i.e., the individual will be part of the universe from which the participation rate denominator is determined, and if the individual participates for a sufficient number of countable hours, she will count in the numerator in calculating the state's rate).

- **Child Support:** For any month in which an individual receives TANF-funded child care assistance, the family will be required to assign its child support to the state; the federal government will keep the federal share of child support collected, and the state can choose whether to pass on the state share of support to the family or retain the state share as reimbursement for assistance provided.

- **Other Federal Prohibitions:** In a number of instances, states are prohibited from using federal TANF funds to provide assistance to certain categories of families or individuals. These prohibitions include a set of restrictions on assistance to legal immigrants.[4] When child care falls within the definition of assistance, a state is prohibited from using federal TANF funds to provide that child care assistance to a family or individual subject to the prohibition.

- **TANF Reporting Requirements:** Assistance provided with TANF funds is subject to all of the TANF reporting requirements that apply to individuals and families receiving TANF assistance.

It has sometimes been suggested that a state might find it advantageous to use TANF funds to provide child care to working families, because those families would then count toward the state's TANF participation rate. However, if federal TANF funds are used, there is no way to have the families count toward the participation rates without also having a month count toward time limits and without also requiring a mandated assignment of child support. Moreover (as discussed in Section 5), if a family not otherwise receiving assistance is provided child care assistance with a TANF dollar, the family will

[4] For a complete listing of the TANF prohibitions, see Greenberg and Savner, **A Brief Summary of Key Features of the Temporary Assistance for Needy Families Block Grant** (CLASP, Rev. May 1997).

count as part of the state's TANF caseload for purposes of determining whether the state qualifies for the TANF caseload reduction credit.

It has also been suggested that, in light of the time limit problem, a state should only use TANF funds for child care when the family is already receiving TANF cash assistance, because then the month is already counting as a month for time limit purposes. A problem, however, may still arise in relation to child support. For example, suppose Ms. Smith is receiving $250 in TANF cash, and a $300 child care subsidy. If the child care is provided through CCDF, the amount of the child support assignment would not include her child care assistance; if the child care assistance is funded with a TANF dollar, it apparently would become subject to the child support assignment.[5]

There are several possible advantages in using TANF funds for child care assistance, though they are not likely to outweigh the disadvantages. First, TANF has a 15% administration cap, while CCDF has only a 5% administrative cap, though this analysis becomes complicated because the definition of "administration" under proposed CCDF rules is different from the definition under the proposed TANF rules.[6] Second, there may be some limited circumstances where a state wants to spend money for child care in a manner not subject to CCDF rules, e.g., if a child does not meet CCDF age eligibility requirements or if a non-protective services family does not meet the "working or attending a job training or educational program" requirement of CCDF. See [Proposed] 45 C.F.R. §98.20, 92 Fed. Reg. 39610, 39645 (July 23, 1997). Even in such instances, though, it would still be more advantageous to the family if the state were to use state funds (or perhaps, funds transferred to Title XX) rather than using TANF funds directly, because of the requirements attached to "TANF assistance." Thus, even though it is permissible to spend TANF funds directly for child care assistance, there are significant policy reasons why states should explore other alternatives.

2. Transferring TANF funds to other block grants for child care assistance

A state may transfer up to 30% of its TANF block grant to the Child Care and Development Fund for the provision of child care assistance. If the state wishes to shift TANF resources to child care, this approach offers significant advantages in facilitating coordination and integration of state child care policy. In limited instances where a state wishes to provide child care assistance and particular CCDF restrictions impair the ability to do so, the state can also consider the option to transfer up to 10% of its TANF block grant to its Title XX Program. However, given the risk that funds transferred to Title XX

[5] The language of the federal TANF statute says that family members must assign support rights to the state "not exceeding the amount of assistance so provided..." Sec. 408(a)(3)(A). It remains unclear whether HHS would interpret this language as allowing a state the discretion to make a child support assignment be for an amount less than the total assistance provided if, for instance, a state did not wish to extent the assignment to non-cash assistance.

[6] Compare [Proposed] 45 C.F.R. §273.0(b), 62 Fed. Reg. 62192 (definition of administration for TANF) with [Proposed] 45 C.F.R. §98.52, 62 Fed. Reg. 39648-49 (definition of administration for CCDF).

may simply supplant other state spending, it will generally be preferable to limit the Title XX transfer (if any) to instances where there is a clearly identified CCDF restriction that impairs addressing specific child care needs.

After corrective legislation in 1997, the rules governing transfer of TANF funds are now that:

- A state may transfer up to 30% of its TANF funds to other block grants.
- Up to 30% can be transferred to the Child Care and Development Fund (CCDF).
- Up to 10% can be transferred to the state's Title XX Program.
- The total amount transferred cannot exceed 30%, and so, for example, if the state transfers 10% to Title XX, then not more than 20% can be transferred to CCDF.[7]

The transfer option involves a significant amount of money. For example, in FY 97, 30% of TANF was approximately $4.9 billion, while the amount of the entire CCDF, if states drew down all available funds, was only $3 billion.

As compared to spending TANF funds directly for child care, one significant advantage of transferring funds to CCDF is that the funds become subject to CCDF rules rather than TANF rules, so that any assistance provided will not count as "assistance" for TANF purposes. A related potential advantage is that since the funds become subject to CCDF rules, they are subject to the same rules governing all other CCDF funds -- e.g., CCDF planning process requirements, consumer information requirements, health and safety requirements, parental choice requirements, etc. Thus, the funds can more easily be integrated into programs operated with other CCDF funds and there may be less risk of fragmentation in state child care policy if the funds are transferred to CCDF.

The federal CCDF income eligibility guideline for each state is set at 85% of state median income. This is likely to be a considerably higher income standard than is applicable to TANF. Some administrators and analysts may view the higher CCDF income limits as a positive feature of the transfer, because it allows for an expansion of child care to working families, and may allow, e.g., for a state to use a more gradually escalating sliding fee scale in its CCDF program. Other persons may be concerned that a result might be that funds previously targeted for very low-income families are shifted away from this

[7] Initially, as a result of what appeared to be a drafting error, the language of the PRWORA said that a state could only transfer funds to Title XX if at the same time, the state was also transferring funds to CCDF; the law provided that the state must transfer $2 to CCDF for every $1 transferred to Title XX. This situation was corrected in the Balanced Budget Act of 1997, which now clearly allows a state to transfer funds to Title XX without also transferring to CCDF.

group. In any case, if a transfer is being considered in a state, it is important to at least be aware that one consequence may be a shift from very-low income to less-low income families.

One potential disadvantage of a transfer of funds to CCDF concerns federal "expenditure" requirements. Under CCDF rules, funds received in a year must be expended in that year or in the following year. In contrast, a state can reserve its unspent TANF funds for future years without limitation. Thus, if a state determines to transfer funds to CCDF, it is important to ensure that they will be spent within the required period, or the state will risk losing them.

If funds are transferred to Title XX, they become subject to Title XX rules rather than TANF rules. However, there are very few Title XX rules. The TANF statute requires that funds transferred to Title XX must be used for children and their families with incomes below 200% of poverty. (As with CCDF, the issue of shifting resources from very-low income to less-low income individuals potentially arises with a transfer). While child care is an allowable use of Title XX funding, the funds expended under Title XX are not subject to CCDF requirements.

While there may be legitimate reasons for a transfer to Title XX, advocates and budget-watchers in a state should closely review any state transfer of funds to Title XX to be sure that the funds actually go to expand services for low-income families. The reason for this concern is that there are no federal "maintenance of effort" or "non-supplantation" requirements affecting how a state spends its federal or state funds when TANF funds are transferred to Title XX. Thus, a state wishing to redirect funds away from low-income assistance can easily make use of a transfer of TANF funds to Title XX, followed by a corresponding freeing up of state funds that had previously been directed to the services. As a result, a transfer to Title XX may or may not result in increased expenditure of funds for low-income families; it may simply be a means by which the state shifts funds away from low-income assistance.[8]

Accordingly, in instances where it is proposed to transfer TANF funds to Title XX for child care assistance, there should be a clear and careful analysis of what, if any, advantages such a transfer has over a transfer to CCDF. Unless it is possible to identify specific CCDF restrictions that impair the state's ability to provide needed child care, it may be more appropriate to transfer to CCDF rather than Title XX.

3. Spending of Welfare-to-Work Grant Funds on Child Care

[8] The same shifting of funds away from low-income assistance could occur when funds are transferred to CCDF, if the state is one that previously was spending state funds on child care in excess of the CCDF maintenance of effort and match levels. In such a situation, the transferred TANF funds could simply be used to free up state funds previously invested in child care. Accordingly, in any instance where a transfer occurs, interested persons will wish to ensure that it actually results in a new level of child care investment.

The Balanced Budget Act of 1997 provides for a total of $3 billion for Welfare to-Work (WtW) grants for FY 98 and FY 99. Generally, a state's share of funding must be expended on certain "allowable activities" for a population of "hard-to-employ individuals" and "individuals with long-term welfare dependence characteristics." Child care assistance for such individuals is one of the allowable activities, though only when the service is "not otherwise available" to the participant..

Under the WtW rules, after certain set-asides, 75% of the funds are available in formula grants to states and 25% of the funds will be disbursed through competitive grants. Each state is eligible for its share of the formula grants; in order to qualify, the state must meet TANF maintenance of effort requirements and make additional state expenditures for allowable activities[9]. Under interim final regulations, a state is eligible to receive federal funding up to the amount available for allotment to the state, based on a 2:1 match structure, i.e., $2 of federal funding will be available for every $1 of state match expenditures; the interim regulations provide that only costs that would be allowable if paid for with WtW grant funds will be accepted as match. See 20 C.F.R. §645.300(a),(b)(1), 62 Fed. Reg. 61588, 61609 (November 18, 1997). The regulations also provide that up to one-half of the match may be in the form of third party in-kind contributions. 20 C.F.R. §645.300(b)(3).

Within a state, at least 85% of the formula grant funds will be administered by Private Industry Councils (or alternative agencies designated by the Governor) with the remainder to be distributed by the Governor to projects that appear likely to help long-term TANF/AFDC recipients. The Department of Labor will award competitive grants, without requiring a matching share: eligible applicants must be private industry councils, political subdivisions, or private entities applying in conjunction with a private industry council or political subdivision.

Both formula grants and competitive grants must be expended on "hard-to-employ individuals" and "individuals with long-term dependence characteristics" (defined in 20 C.F.R. §645.212 and §645.213) and used for "allowable activities" (defined in 20 C.F.R. §645.220). The regulations provide that allowable activities include a defined list of job readiness activities, employment activities, job placement services, post-employment services, job retention services and support services, and individual development accounts. The regulations expressly identify child care assistance as one permissible job retention and support service; however the following conditions apply to any job retention service or support service:

- the service must be provided after an individual is placed in a job readiness activity, an employment activity, or in any other subsidized or unsubsidized job; and

- the service can be provided with WtW funds only if not otherwise available to the participant.

[9] See generally **Welfare-to Work Grants and Other TANF-Related Provisions in the Balanced Budget Act of 1997** (CLASP, August 1997).

20 C.F.R. §645.220(e)(3). The preamble expressly notes: "For example, in the area of child care, the operating entity should ensure that WtW funds are not substituted for child care services available from the Child Care and Development Block Grant, TANF funds, and other State and local funds." 62 Fed. Reg. 61594. The regulations also expressly require coordination of resources between WtW, TANF, and CCDF. 20 C.F.R. §645.225. The regulation and preamble do not otherwise clarify how an entity determines whether the service is "otherwise available" to the participant.

If WtW funds are used for non-cash assistance (such as child care), the assistance will not be considered "assistance" for purposes of TANF time limits, but will be considered "assistance" for all other TANF purposes, e.g., child support assignment, other TANF prohibitions, TANF work and participation requirements, TANF data collection requirements. [Proposed] 45 C.F.R. §274.1(a)(2),(b)(3).

4. Spending State Funds for Child Care Assistance

A state is free to spend as much state funding on child care as it wishes. However, there are two important TANF-related consequences to keep in mind. There are two TANF "maintenance of effort" requirements: the basic TANF MOE requirement, and the separate MOE requirement for a state wishing access to the federal contingency fund in times of economic downturn. Under current law:

- Under many circumstances, state spending on child care can count toward satisfying the basic TANF maintenance of effort requirements.

- In contrast, state spending for child care will not count toward satisfying the contingency fund MOE requirement.

As a result, a state wishing to significantly expand state spending for child care may face a difficult choice if the state also needs to count the spending toward TANF-related requirements. In many cases, states may conclude that, given the numerous problems in the current design of the Contingency Fund, a state's broader social policy decisions should not be driven by contingency fund rules; however, this is not an easy issue, and it is important to at least be aware of the applicable rules.

The rest of this section first explains when state MOE dollars count toward TANF MOE requirements and then explains why state child care spending does not count toward Contingency Fund MOE.

a. State Child Care Expenditures and TANF MOE Requirements

Certain state child care expenditures can count toward satisfying a state's TANF maintenance of effort requirements. The short summary is that a state can count expenditures of state funds for child care assistance, whether expended in the TANF program or in a separate state program, if:

- the expenditures are for "eligible families," defined as including citizen families and most immigrant families with children, so long as the families meet the state's TANF income and resource standards;

- the expenditures must not be expenditures that the state is counting as matching expenditures for purposes of CCDF; and

- if the expenditures are in a state or local program, the expenditures must be above the FY 95 level of spending for that program, with one exception: the state can count expenditures in a separate state program (e.g., an At-Risk child care program) to the extent that those expenditures were ones which matched federal funding for that program in FY 95.

The rest of this section explains in more detail when child care expenditures can count toward TANF MOE and highlights some of the most significant implications of the federal rules.

To receive a full TANF block grant, a state must satisfy a TANF maintenance of effort (MOE) requirement. The requirement is that qualified state expenditures reach at least 80% (or 75% if the state meets TANF participation rates) of an "historic state expenditure" level. In general, the historic state expenditure level is the level of non-federal spending which was needed to match the state's federal spending for a set of programs (AFDC, JOBS, Emergency Assistance, AFDC Child Care, Transitional Child Care, and At-Risk Child Care) in FY 94.

A state must satisfy its MOE requirement by making certain allowable expenditures for needy families, but MOE funds need not be spent in the TANF Program; a state can also choose to spend them in other state programs. Expenditures can count toward TANF MOE whether they are made in the state's TANF program or in a separate state program if they are for "eligible families" for child care or for a set of other permissible purposes.[10]

Under proposed regulations, an "eligible family" as defined by the State, must:

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[10] The other allowable purposes are:

- Cash assistance;
- Educational activities designed to increase self-sufficiency, job training, and work, excluding any expenditure for public education in the state except expenditures which involve the provision of services or assistance to a member of an eligible family which is not generally available to persons who are not members of an eligible family;
- Administrative costs in connection with the above expenditures, but only to the extent that such costs do not exceed 15% of the total amount of qualified state expenditures for the fiscal year; and
- Any other use of funds not prohibited by the block grant and reasonably calculated to accomplish the purpose of TANF. See Section 409(a)(7)(B); [Proposed] 45 C.F.R. §273.2, 62 Fed. Reg. 62192-93.

- be comprised of citizens, qualified aliens, non-immigrants under the Immigration and Nationality Act, aliens paroled into the U.S. for less than one year, or, in the case of aliens not lawfully present in the U.S., provided that the State enacted a law after August 22, 1996, that "affirmatively provides" for such services; and

- include a child living with a custodial parent or other adult caretaker relative (or consist of a pregnant individual); and

- be financially eligible according to the TANF income and resource standards established by the State under its TANF plan.

[Proposed] 45 C.F.R. §273.2(b)(1), 62 Fed. Reg. 62193. Thus, if a family meets the state's TANF income and resource standards, then child care assistance for the family can count toward TANF MOE requirements even if the family is not eligible for federally-funded TANF assistance. For example, certain immigrant families will be ineligible for federally-funded TANF assistance because they are in the midst of the five-year ineligibility period after having entered the United States. However, if they fall within one of the above listings, then the state may use state funds to provide child care assistance (or other forms of assistance that meet the definition of "qualified state expenditures"), and have those funds count toward the state's TANF MOE requirement. In addition, a consideration that may be relevant in later years is that a state may count toward MOE its expenditures for families that have reached and exceeded the TANF time limit.

To qualify as an eligible family, the family must meet the state's TANF income and resource standards. There are some important unresolved questions about what this requirement means. There are no specified federal standards, so it appears that the state has broad discretion in establishing its own standards. However:

- It is not clear if, for example, a state could set a definition of "eligible families" for MOE purposes that makes use of higher income eligibility guideline used in determining eligibility for TANF cash assistance.

- Similarly, it is not clear whether the proposed regulations are intended to require that states must apply resource standards, or whether the meaning is just that if the state elects to use resource standards for TANF eligibility, it must also apply those standards for MOE "eligible families" determinations. It is also unclear whether a state could elect to apply resource standards for some forms of assistance (e.g., cash) and not for others (e.g., child care).

- A state may or may not have different definitions or count income differently for its child care programs than for its TANF Program, and it is unclear whether the implication of this proposed rule is that the state must, for example, determine the family's eligibility under the TANF income rules to resolve whether the expenditure for the family would count toward TANF MOE

requirements, i.e., is it sufficient to apply the TANF income standards, or is it also necessary to apply the TANF income methodologies.

Note that there is no requirement that the child care expenditures be necessary for employment. Accordingly, a state could, for example, fund child care expenditures for education and training programs for needy families, and have them count toward maintenance of effort. It appears that the state could also count other kinds of child care expenditures for needy families, e.g., respite care, protective services care (keeping in mind that a child must be residing in the home for the family to meet the definition of eligible family.)

Note, however, that some state child care expenditures for "eligible families" do not count toward the TANF MOE requirement. To understand which state child care expenditures count, a brief review of the CCDF funding structure may be helpful:

- Under CCDF rules, every state receives a block grant of federal funds (of which some of the funds, in federal budget terms, are "mandatory" and some are "discretionary"). This block grant approximately represents the state's federal funding for a set of child care programs from the higher of 1994, 1995 or the 1992-94 average. The state qualifies for this block grant without any requirement to expend state funds.

- Additional federal matching funds are available to the state above the level of its discretionary and mandatory funding. However, these matching funds are only available to the state if: 1) the state meets a CCDF maintenance of effort requirement, set at the higher of 1994 or 1995 level of state funding that represented the non-Federal share for the then-existing IV-A child care programs (i.e., AFDC Child Care, Transitional Child Care, At-Risk Child Care); and 2) the state commits additional state funds to match the federal matching funds.

In light of this structure, one can think of state child care spending as having three components:

- first, the state must meet CCDF MOE requirements if it wishes to qualify for federal matching funds;

- then, the state must provide state match to receive the available federal matching funds; and

- then, if a wishes to do so, it can expend state funding for child care above the level of CCDF MOE and the match for federal funding.

In this structure:

- the state expenditures that count toward CCDF MOE can also count toward TANF MOE so long as they meet the other TANF MOE requirements (i.e., for eligible families);

- the state expenditures that match federal child care funding cannot count toward TANF MOE, because there is a prohibition against counting state funds that are used to match federal funds for MOE purposes; and .

- if a state has state spending above the CCDF MOE and CCDF match level, that state spending can count toward TANF MOE, so long as it meets other TANF MOE requirements.

There is only one more potential qualification to keep in mind. TANF MOE rules also provide that if the state previously had expenditures under a state or local program that meet the definition of a qualified purpose, e.g., cash assistance for families, child care, etc., the state may count spending under that program only to the extent that it represents a higher level of spending than the FY 95 level. The state cannot, for example, simply identify pre-existing state or local programs for the allowable purposes (e.g., cash assistance, child care assistance, etc.) and claim those expenses as part of maintenance of effort. This would seem to mean, for example, that if a state had an existing state child care program in FY 95, and that program was not matching federal funds, and the state continues to operate that program now, then only the level of spending for the program above the FY 95 level can count toward TANF MOE requirements.

While the rules governing child care and TANF MOE may sometimes be complex, the basic conclusion is clear: increased state spending for child care for low-income families can often count toward TANF MOE requirements. Particularly in those cases where a state's TANF caseload is declining, and the state is seeking to determine how it can ensure that it continues to comply with TANF MOE requirements, the expenditure of funds on child care is one means to both reduce the need for TANF assistance and to meet MOE requirements.

b. State Child Care Spending and TANF Contingency Fund Maintenance of Effort Requirements

A very different set of rules concern the TANF "contingency fund." Child care expenditures do not count toward the maintenance of effort requirement for the contingency fund. Accordingly, a state concerned about assuring that it qualifies for the Contingency Fund in times of need will need to carefully attend to which expenditures do and do not count toward the contingency fund requirements.

The Contingency Fund is a $2 billion federal fund, generally intended to be available to states to provide matching federal funds for certain expenses during periods of economic downturn. In order to be eligible to receive contingency funds, there are two principal requirements: first, the state must meet an economic trigger (based on either unemployment increases or increases in the numbers of families receiving food stamps); and second, the state must satisfy a Contingency Fund MOE requirement.

The Contingency Fund MOE requirement is different from the TANF MOE requirement in a number of ways:

- The TANF MOE requirement must be satisfied every year in order to avoid a federal penalty; the Contingency Fund MOE requirement need only be satisfied in the year in which the state is seeking access to the Contingency Fund;

- The TANF MOE requirement is based on having state expenditures of 80% (or if the state meets TANF participation rates, 75%) of a historic state expenditure level. The Contingency Fund requirement is based on having state expenditures of 100% of a historic expenditure level. However, the levels used are different for the two provisions. The TANF MOE historic state expenditure level is based on the higher of 1994 or 1995 spending for AFDC, AFDC Administration, the JOBS Program, Emergency Assistance, and the former IV-A Child Care programs (AFDC Child Care, Transitional Child Care, At-Risk Child Care). The Contingency Fund MOE requirement begins from the TANF definition, but then subtracts out the spending for the IV-A child care programs. Thus, it is a higher standard (100%) but using a lower base (1994 or 1995 IV-A spending excluding IV-A child care spending).

- While state spending for child care can count toward TANF MOE requirements (subject to the qualifications described in the preceding section), spending for child care assistance may <u>not</u> count toward satisfying contingency fund MOE requirements.

- In addition, while expenditures in separate state programs can count toward TANF MOE requirements, expenditures in separate state programs cannot count toward Contingency Fund MOE requirements, i.e., the expenditures must be state expenditures within the TANF Program.

What are the practical implications of this difference in MOE rules? The principal implication is that a state that satisfies its TANF MOE obligation, even in part, through child care spending may have a more difficult time in meeting Contingency Fund MOE requirements than a state that meets its TANF MOE obligations through non-child care spending within its TANF program. An example demonstrates the problem. Consider a hypothetical state, with a TANF MOE historic expenditure level of $100, and a corresponding TANF MOE level of $80. Further assume that the share of historic state spending attributable to IV-A child care was $10; thus the Contingency Fund historic expenditure level and MOE level will be $90. In this example, if the state is only concerned with meeting the TANF MOE requirements, it only needs spending of $80, of which any amount could be for child care, and any amount could be spent in one or more separate state programs. However, the part of the spending attributable to separate state programs, and the part attributable to child care (whether spent in TANF, spent in a separate state program, or even if spent commingled with CCDF funds) will not count toward Contingency Fund MOE. Thus, if the state is also concerned about meeting Contingency Fund MOE requirements, the state will need to have state spending of $90, exclusive of child care, in its

TANF Program. Accordingly, the perhaps-unintended effect of the Contingency Fund MOE rules is to place a state at greater risk of being unable to meet Contingency Fund MOE requirements if the state elects to meet a substantial share of its TANF MOE requirements through child care spending.

How should a state structure policies in light of this difficulty? A threshold question for a state is whether it wishes to maintain at least the chance of qualifying for Contingency Fund eligibility. Recall that a state does not need to meet 100% of the historic state expenditure level every year, so long as the state reaches that level in the year in which it qualifies. However, as a practical matter, if a state's spending falls (or has already fallen) very far below the 100% level, it may not realistically have the capacity to be eligible for the Contingency Fund, and the question of whether particular expenditures will count toward Contingency Fund MOE may not be very important. Due to declining state spending based on caseload declines in recent years, a number of states may already be in this position.

Second, there are a number of other problems with the Contingency Fund beyond the MOE difficulty described above, and these difficulties may make the Contingency Fund sufficiently problematic that the state concludes that state policy should not be driven by efforts to remain eligible for the Contingency Fund. The most significant other problem in Contingency Fund design is its annual "reconciliation process;" under reconciliation, a qualifying state will be eligible for federal matching funds, but its actual match rate for the year will not be known until the end of the year, and even then, its effective match rate will be less favorable than the Medicaid match rate unless it qualifies for Contingency Fund eligibility in every single month in the fiscal year; if the state only qualifies in a few months, its effective match rate may be extremely unattractive.[11]

In summary, child care expenditures, whether within or outside of TANF, do not count toward contingency fund MOE. As a result, any state using at least some child care expenditures to count toward TANF MOE (which is likely to be the case for all states) needs to review the current composition of spending to determine if any policy adjustments are needed. In the long run, the best resolution would be for Congress to revisit and restructure the Contingency Fund requirements, both to ensure that child care expenditures were countable and to address the problems in the reconciliation process.

[11] For example, if a state's Medicaid matching rate is 50%, but it only qualifies for contingency funding for six months of the year, its effective match rate will be 75% state, 25% federal; if the state only qualifies for three months of the year, its effective match rate will be 87.5% state, 12.5% federal. For a more extended discussion of the problem, see discussion in **Welfare-to Work Grants and Other TANF-Related Provisions in the Balanced Budget Act of 1997** (CLASP, August 1997).

5. Child Care and the TANF Caseload Reduction Credit

In deciding how to structure child care spending, one additional consideration for some states may be the relation between expanding child care availability and the TANF "caseload reduction credit." Generally, a state that is able to reduce the number of families receiving TANF assistance may find that doing so also assists the state in meeting its TANF participation rates. The reason is that certain forms of caseload reduction reduce a state's required TANF participation rate; as a result, expanding the availability of non-TANF child care (or other forms of non-TANF assistance to working poor families) may be an effective strategy in helping a state meet its TANF participation rates. However, the form of the child care spending will affect whether the state can benefit from TANF's "caseload reduction credit."

Under TANF rules, many states may face actual participation rates that are significantly below the listed participation rates in the statute. Generally, the statute required HHS to prescribe regulations for reducing a state's participation rate based on the state's caseload reduction. The participation rate reduction for a year will be the number of percentage points equal to the number of percentage points by which the number of families receiving assistance under the TANF Program during the immediately preceding fiscal year is less than the number of families that received aid in FY 95, subject to two exceptions: The rate shall not be reduced to the extent that:

- HHS determines that the reduction in the number of families receiving assistance had been required by federal law; or

- HHS proves that the families were diverted from receiving TANF assistance as a direct result of differences in state eligibility criteria from the criteria in effect on September 30, 1995.

For example, suppose that the state has had no relevant changes in eligibility since FY 95, and that its FY 97 caseload is 15% lower than its FY 95 caseload. In such a situation, the FY 98 participation rate would be adjusted downward by 15 percentage points, i.e., the rate will be reduced from 30% down to 15%. Thus, caseload reduction becomes a significant strategy for helping a state to meet its TANF participation rates.

HHS' proposed rules to implement the caseload reduction credit are located at [Proposed] 45 C.F.R. §271.40-44. Generally, the rules require that any state seeking the caseload reduction credit must submit a listing of changes in state eligibility rules since FY 95, along with estimates of the extent to which those rules affected caseload and an explanation of the methodology used. HHS will review the state reporting in determining the extent, if any, to which a state qualifies for the caseload reduction credit.

How do child care expenditures affect the extent to which a state benefits from the caseload reduction credit? It depends on whether the family receives other forms of TANF assistance and on how the child care assistance is provided. If a family is still receiving even $1 of TANF assistance, then the TANF caseload will not have declined, even if the extent of the family's assistance is substantially reduced. Suppose, however, that the family is no longer receiving any other form of TANF assistance. In such a case, the impact on the caseload reduction credit depends on how the child care assistance is structured:

- **If TANF funds are directly used** for the child care assistance, the state will not benefit from the caseload reduction credit, because the family will still be receiving TANF assistance.

- **If the TANF funds are transferred to CCDF or Title XX** to be used for child care assistance, the state can benefit from the caseload reduction credit, because the family is no longer receiving TANF assistance.

- **If Welfare-to-Work grant funds are used,** the families receiving the child care assistance will still be considered a part of the TANF caseload (because WtW funds used for child care will be considered assistance for all TANF purposes other than time limits), so the state will not get the benefit of the caseload reduction credit for such families.

- **If state TANF maintenance of effort funds are used** to provide child care assistance, it is unclear whether the state will qualify for the credit. Under proposed regulations, HHS says that it will normally count cases assisted in a separate state program that counts toward TANF MOE requirements when calculating a state's eligibility for the caseload reduction credit; however, HHS indicates that it will "consider" excluding cases in such separate state programs if they "are cases that are receiving only State earned income tax credits, child care, transportation subsidies or benefits for working families that are not directed at their basic needs." [Proposed] 45 C.F.R. §271.42(c). In the proposed regulations and preamble, it is not clear what factors HHS will take into account when it makes this consideration.

- **If the state uses state funds which are not counting toward TANF MOE** to provide child care assistance, and the effect of the child care assistance is to reduce the number of families receiving TANF, then the state can benefit from the caseload reduction credit for such cases. The HHS scrutiny and counting of cases in separate state programs will only be applicable to those cases in separate state programs that count toward TANF MOE requirements.

Thus, if a state decides to commit additional resources to child care, the manner in which the spending is structured can (among the many other factors already noted) also affect whether the state qualifies for the TANF caseload reduction credit, and whether there will be a corresponding reduction in the state's TANF participation rates.

Conclusion

A state wishing to expand child care spending faces multiple choices, based on the competing claims for alternative use of dollars and based on the differing consequences of differing choices. The clearest conclusion that emerges from the above analysis is that if a state wishes to expand child care funding, the least attractive way to do so is by expending a TANF dollar directly. Doing so has adverse consequences for families (e.g., time limits, child support requirements) and adverse requirements for the state (additional requirements to turn over child support to the federal government, an increased TANF caseload when calculating the TANF caseload reduction credit). The option to transfer to CCDF will often be the most straightforward and advantageous for both states and families. The decision to expand state spending (if that spending is needed to count toward TANF MOE) necessarily forces the state to consider the impact on Contingency Fund eligibility: for some states, this may not be a difficult issue but for others, it may pose troubling trade-offs.

It is hoped that this discussion of the alternatives and their consequences can enhance thoughtful decision-making as states explore means of expanding child care assistance for needy families.