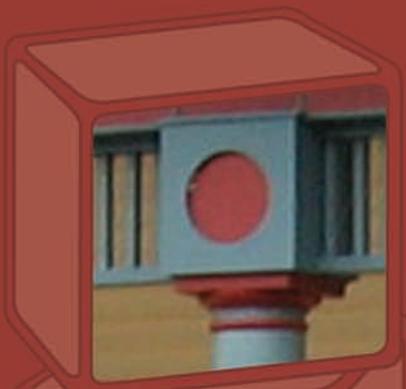


Building the Supply & Quality of Early Care & Education Facilities in Maine



Prepared by the Local
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Family Focus – Brunswick

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INTRODUCTION

Introduction

Early childhood facilities get little attention. Yet they are vital to the state's economic well-being and the healthy development of most of Maine's children. They are important because the availability and location of child care services profoundly affect child care supply. There is also growing evidence that well-designed child care space can have a dramatic impact on program quality as well as teacher morale and turnover. Nonetheless, early childhood programs have struggled with the high cost and complexity of creating and improving their physical environments. As Maine continues to build its system of early care and education, facility quality and supply and the financial and technical barriers to creating and improving facilities need to be explored. A number of other states have developed innovative policies and programs to help providers gain better access to financial and technical resources to create quality facilities, and lessons learned from these approaches can inform Maine's efforts.

To both determine needs here in Maine and to learn from the experience of other states, the Department of Health and Human Services' Office of Child Care and Head Start contracted with the Local Initiatives Support Corporation (LISC) to carry out an assessment to evaluate the adequacy of existing financial and technical resources to support facilities development for the state's center-

and home-based programs, and to formulate a set of recommendations for how the state can strengthen its early childhood facility financing and development infrastructure.

LISC is the largest community development organization in the country, with a long history of creating new affordable homes and commercial and community space. Through its national child care program, the Community Investment Collaborative for Kids (CICK), LISC has combined its real estate development and financing expertise with specific knowledge of the child care industry to help a growing number of cities and states improve the quality and supply of child care through investments in facilities.

To carry out this assessment, Amy Gillman (CICK's National Director) and Carl Sussman (CICK's National Technical Consultant) have interviewed more than 50 people representing a broad cross-section of practitioners, opinion leaders, policy makers, regulators, philanthropies, lenders, and others. They have also conducted additional research on child care supply and facilities-related issues in the state, and visited a number of recently developed centers and analyzed how they were financed and developed. A list of key informants can be found at Appendix A and a description of existing financing and technical assistance programs can be found at Appendix B.

CONTEXT & STRATEGIC SOLUTIONS

Context & Strategic Situation

The environmental scan carried out for this assessment revealed a number of challenges and constraints as well as many opportunities and assets available to address them:

Strengths

Public policies in Maine demonstrate a broad state government interest in early care and education, a focus on program quality, and some attention to facilities:

- The Children’s Cabinet, which brings the state’s senior administrative officials together, has an active Early Childhood Task Force that is focusing on child care facilities. The Attorney General, a member of the Task Force, has shown a personal interest in the facilities issue.
- The commissioner of the State Department of Education has shown strong support for universal access to pre-Kindergarten for four-year-olds. Districts receive reimbursement through the state’s school funding formula to provide these services.
- Maine has created a fertile environment for collaborative efforts in the early care and education arena. For example, most Head Start grantees are also state-contracted child care providers. In addition, roughly 20% of public school pre-kindergarten programs for four-year-olds operate in collaboration with Head Start or contracted community-based child care providers.
- Since Maine dispenses half of its Child Care and Development Fund subsidy resources in the form of contracts, some providers that might otherwise be struggling are more stable.
- The development and use of “Quality Certificates” provides access to four state financial incentives and reflects the state’s emphasis on quality: a double tax credit to parents which has encouraged providers to pursue programmatic quality; eligibility for Financing Authority of Maine (FAME) loans; an investment tax credit for proprietary child care programs, and eligibility for a 10% increase in the state’s subsidy rate.
- A number of prior reports about child care in Maine have identified facilities as an issue.
- The existence of a statewide community development finance institution, Coastal Enterprises Inc., with a history of supporting and lending to child care providers.
- While most center-based programs occupy space that was neither originally designed for nor substantially renovated to meet the special needs of young children, a small number of programs have managed to overcome the financial and technical barriers, building new facilities. In the process, these pioneers have helped build experience and know-how about how to develop facilities and showcase for others the difference well-planned facilities can make.
- Some family child care providers, especially homeowners, have demonstrated a willingness and ability to make capital investments in their homes because it both helps their business and builds equity. They are also more willing and able to borrow money to make improvements, often using home equity loans, as well as the “sweat equity” of members of the family to build the improvements.

Limitations and Challenges

Accreditation is a common proxy for assessing the extent to which child care programs reflect quality practices. Only 11% of centers are accredited and even fewer family child care homes (less than 1% or 45 out of roughly 1800). A well-designed and equipped facility is one factor identified as a barrier to accreditation in one survey.¹

The age, physical conditions, and lack of investment to adapt existing facilities for child care use creates many operating problems.

While some family child care providers seem to be doing well, others confront unique and widely disparate challenges complying with local zoning, overcoming landlord resistance to a home-based business operating on their property, securing liability insurance and resolving a variety of idiosyncratic health and safety impediments to state certification. Without a larger system of support to help prospective providers resolve these legal and regulatory impediments, some have difficulty navigating through the process.

Except for several strong niche child care markets in the state, there are significant financial barriers to facilities development:

- Most center-based child care programs operate on very tight financial margins and have few if any tangible net assets. This severely limits their capacity to secure and support debt to finance facility investments.
- To the limited extent that some providers might be able to borrow money, most are nonetheless debt-averse. This is characteristic of the child care industry nationally. However, some interviewees expressed the belief that the independent spirit that is part of Maine's culture exaggerates the reluctance to assume debt.
- Although USDA Rural Development's Community Facilities Loans provide the

most favorable source of debt financing for child care centers (discussed later in this report), this resource is not available in certain parts of the state and to certain categories of providers.

- Barriers are technical as well as financial: Child care providers in Maine, like those in other states, lack the knowledge and experience to effectively develop real estate. Therefore, in addition to the obvious need for capital, the state faces a less obvious but equally as serious shortage of real estate development capacity to build or renovate facilities. The need for capital and technical expertise are interdependent.
- The role of the physical environment in promoting quality has historically been overlooked. Perhaps because of the prohibitively high cost of addressing facilities issues, practitioners place a priority on other important quality components such as staff training and credentialing. Moreover, there is limited awareness of the quality benefits of well-designed space.
- The availability of existing school space to house public preschool programs presents special challenges.
- These programs may siphon preschool-aged children from other child care programs, undermining the financial viability of expensive infant and toddler classrooms that rely in part on preschool fees for their feasibility. So, paradoxically, the expansion of preschool supply may create a supply problem for younger children.
- While public school classrooms are increasingly becoming available for preschool use, the space is not ideal. Most classrooms lack sinks and bathrooms; cot and equipment storage, or appropriate playground fencing and equipment. The cost of converting the typical elementary school classroom to preschool use will be costly. Moreover, four-year-olds may be over-

whelmed by the size, scale and institutional character of elementary school buildings.

- Winning support for a public sector investment in child care facilities – regardless of whether they are school-, community- or home-based – will require a great deal of leadership and careful attention to messaging.
- Grant sources typically available in many other states – foundations and corporate grants – as well as fundraising leadership and organizations capable of mounting capital campaigns, are quite scarce in Maine. Even the Community Development Block Grant program, a public sector grant source commonly tapped for child care facilities development in other states, is especially competitive in Maine.

Opportunities

- The availability of classrooms in existing public schools provides access to physical space that could be adapted to offer more children a quality preschool experience. Some school districts have made vacant classrooms available to Head Start programs to augment preschool resources available in the district. This relieves the Head Start program of certain operating costs, such as heating and snow removal, and provides children with access to school resources, such as the gym for gross motor activity and music. Fully capitalizing on this opportunity will require overcoming some of the physical limitations of elementary school classrooms and buildings.
- Much of Maine is rural, consisting of communities with fewer than 20,000 people. Nonprofit child care programs in these communities are eligible for a variety of extremely favorable programs administered by the Rural Development program of the US Department of Agriculture. The Community Facilities specialists in the

state’s four USDA offices have been extremely helpful to those providers who have accessed these resources. The Maine office is particularly active in financing a very large number of projects and securing the additional financial resources from Washington to do so. It is the leading state in the number of community facility loans and is number two in the amount of money it invests for this purpose.

- Although it is only in the early stages of discussion, members of the Children’s Cabinet’s Early Childhood Task Force have shown an interest in the issuance of bonds to finance early childhood facilities in the state.
- Nonprofit and quasi-public affordable housing developers in Maine might be enlisted to partner with child care providers to develop new facilities. The child care industry lacks the kind of real estate development expertise these organizations possess.² If financing existed that made the development of child care facilities feasible, organizations like these might be interested in developing child care facilities on behalf of specific providers.

Key Issues

Maine, like every state, has its own set of conditions that support and impede the development of child care facilities and also shares some common industry-specific conditions. The early care and education industry invests very little in creating high-quality physical environments designed for young children. Some proprietary center-based programs have profitable business models based on niche markets that can, and, for their success often must, expend more than most child care programs on occupancy. However, for much of the center-based segment of the industry, programs are small, often organized as nonprofit corporations, and are neither able nor inclined to invest in facilities. Both capital and real

estate development expertise are barriers. These conditions result in a low level of capital investment which affects facility and program quality and has an impact on the supply of center-based care. This is the most obvious challenge facing the industry in Maine.

The low population density in large portions of the state makes home-based family child care businesses the most feasible way to deliver child care in some locales. The family child care business model is based on the provider's ability to use their home to accommodate child care demand without any significant capital investment. This characteristic has two important implications. First, family child care can adjust most quickly to changes in market conditions: As demand increases, providers can enter or re-enter the child care business without many barriers. Second, experts in early childhood facilities design emphasize the need for making centers appear non-institutional and incorporate residential design elements. Family child care takes place in a home, not a "home-like" environment. For all these reasons family child care's unique competitive advantage is its small group size and intimate and ready-made home setting. As a result, the capital needs in family child care are incidental as compared with those faced in the center- and school-based portions of the industry. This is not to imply that home-based child care businesses do not have issues. Reportedly, aspiring family child care providers occasionally encounter regulatory or legal barriers to opening or securing state certification and, moreover, program quality can be very uneven. Both of these problems are best addressed through technical assistance services and far more modest levels of financial resources than the sizeable capital investment needed to resolve center-based facility issues.

State-funded school-based pre-Kindergarten programs for four-year-olds are valuable com-

plements to the early care and education landscape. Moreover, school districts tend to have underutilized classroom space to house these new educational services. However, elementary school facilities may not provide the kind of physical environment needed to support quality early childhood programming without significant further investment. Elementary school classrooms and playgrounds often face the same adaptive reuse challenges that center-based providers encounter relocating to unimproved space designed for other uses. Many of these buildings may be inappropriate and a significant investment in classroom and playground renovations may be needed to support high quality programs for preschool children

This is also a period of change and exciting opportunity in Maine. State leaders have increasingly focused on "investing early" in comprehensive approaches and prevention strategies. This provides a favorable public policy environment to invest in quality child care. Early education and care is arguably the most widespread, intensive (in terms of hours children spend in out-of-home care) and preventative service available to the state's preschool-aged children. State education and human services policies reflect long-term trends evident across the country that will likely cause a steady increase in the number and proportion of young children attending preschool programs. To ensure that the state realizes the expected public return on this investment, the quality of early education programming must be high, there must be sufficient supply, and the supply must be located where parents are most likely to access the service. In short, policy makers and child care providers need to work together to ensure the supply, quality and location of early childhood facilities support efforts to build a healthy and robust early care and education system in Maine.



FACILITY SUPPLY & QUALITY ANALYSIS

Facility Supply and Quality Analysis

Early childhood facilities become public policy issues if the economics of early care and education create a supply bottleneck or impede the industry from achieving quality for the healthy development and education of young children. As a result, this analysis considers policy directions based on both a supply and quality perspective:

Supply

Child care supply and demand are difficult to determine. The supply side calculation appears relatively easy since most programs are required to be licensed or certified by the Department of Human Services. However, there are two problems. First, child care is a very local service, so while statewide or even regional supply in some locations may appear sufficient, the state still has critical shortages in specific geographic areas. Second, for economic, transportation, or personal reasons, parents choose to use or substitute informal care arrangements, relying on friends, family, neighbors or unlicensed or unregistered providers.

Demand can also be ambiguous. The need for child care may be high but, because of its cost, the effective demand – the ability of parents to afford high quality services provided by a licensed or registered provider – is low. For example, the state has a waiting list of economically-eligible families seeking subsidized child care. Presumably there is another group of families who based on their income are ineligible for state child care subsidies but who

earn too little to afford licensed or certified care. In the absence of more subsidy dollars, many children are unable to enroll in formal care arrangements. Hence there is a “need” but not effective “demand.”

Alex Hildebrand, the author of *The Economic Impact of the Child Care Industry in Maine* (June 2003,) used another methodology to estimate the harder to determine need for child care and afterschool care using demographic data and population projections. Currently 72% of Maine’s children between birth and 13 years of age “live in households where all parents present are in the labor force.” Moreover, there is a long-term trend of increasing labor force participation rates. Hildebrand estimates there is only one licensed space for every four children that need some sort of care although “it is impossible to determine how many parents would take advantage of licensed child care spaces if they were both available and affordable.”³

Given the inherent limitations on quantitative supply, demand and utilization data, key informant interviews provided supplemental qualitative data. The interviewees included individuals from different geographical areas (although interviewees were overwhelmingly from the more populous areas of the state), and with many state officials, lenders, business leaders, child care providers, Resource Development Centers (RDCs), academic researchers, and others. These interviews yielded consistent descriptions of the supply and demand landscape:

- The supply of regulated care is scarcer in rural areas. Interviewees speculated that lower incomes in rural portions of the state

translated into less effective demand. Also, because rural communities are more tightly knit than the more densely populated regions of the state, parents are more likely to use un-registered family child care or informal care arrangements with relatives, friends and neighbors.

- Demand is sensitive to the economy: If parents or relatives are at home, the demand for child care declines.
- Demand is high in greater Portland because of population density and the strong regional economy.
- Local and state economic development officials “understand the connection between early childhood education and workforce availability.” They reported that a few large employers have offered on-site child care but that such care is becoming quite scarce. A few large employers reportedly offer child care subsidies to their workers. However, the issue of child care supply is a continuing matter of concern to new employers who routinely inquire about child care availability as they make locational decisions. Middle-class professionals are specifically interested in quality center-based programs.
- Because of the especially high cost of delivering it, RDCs report infant and toddler care is in chronically short supply. Afterschool care is insufficient although it is relatively more available than infant and toddler care but less available than slots for three- to five-year-olds.
- Small business technical assistance providers and RDC staff noted that program size influences center-based supply. Single-site child care centers licensed for 20-30 children are marginally feasible and especially vulnerable when demand is soft. As one key informant said, “There are relatively few comparatively large organizations that provide child care, and they do day care as an adjunct [to other activities].” The underlying problem is the economics of the child care business: Small providers cannot expand their capacity to support excess demand. Centers need to operate close to full enrollment to make ends meet. As a result, center-based child care supply is inelastic.
- Looking ahead to project future supply and demand, the Office of Child Care and Head Start recently sponsored research designed to project the need for child care. The researchers started with existing license and registration information to estimate supply. To estimate demand, the researchers again used current demographic data and assumed only a proportion of the children living in households where all the adults are in the workforce would need care. The researchers then mapped this data against economic growth projections to identify those counties most likely to face supply shortages in future years. According to this analysis Cumberland, Lincoln, Knox Waldo and Penobscot counties will in 2020 have the highest percentage increase in children ages 0-13 needing care as compared the percentage of the current population needing licensed care.
- Birth and fertility rates for women ages 15-44, which had declined statewide through the early 1990s, have remained relatively stable for the last ten years.⁴ However, growing workforce participation rates in specific regions are likely to generate a growing demand for child care. This is especially true of eight contiguous south coastal counties – York, Cumberland, Androscoggin, Sagadahoc, Lincoln, Kennebec, Knox and Waldo – that are also the most densely populated counties in Maine.⁵ Androscoggin County’s birthrate

has grown by 17.9% between 2000 and 2005, more than twice the rate of any of the other counties that have experienced an upward trend in births. Thus, the economic growth, greater affluence, growing workforce participation rates, population density and, to a lesser extent birthrates, will fuel a gradual increase in child care demand. This portion of the state can support and will need a growing supply of both home- and center-based care. The balance of the state will likely rely more heavily on family child care.

Key Findings With Respect To Supply

There is a statewide shortage of infant and toddler care. Infant and toddler care is in short supply statewide because higher adult-child ratios make the economics of delivering care to younger children prohibitively expensive.

There are weaker indications that demand for afterschool child care also exceeds supply. However, it is not clear how important, or even whether, facilities may be a factor contributing to short supply.

Center-based supply will lag behind demand in certain locations. A number of factors cause center-based supply to lag behind demand in areas where a strong economy and population growth create a need for more care:

- Building or renovating new child care facilities – structures that incorporate the unique design elements that support program quality – takes many months or even years.⁶ Unlike purchasing a home or even typical commercial categories of real estate, existing child care centers are unlikely to be on the market. The space must be created.
- Since most center-based programs operate on narrow margins, they need to operate

at or near capacity to break even. That is sufficient reason for center directors to be risk-averse. If expansion means absorbing higher fixed facility costs, the risk is still higher.

The need for supply-building is uneven and localized. At the moment, economic and population growth is concentrated in portions of southern coastal Maine. There has been some growth of proprietary center-based programs, but non-profit centers serving mostly lower-income families are especially reticent about expansion for the reasons mentioned above.

Home-based family child care supply responds more quickly to changes in demand. Although the time and expense involved in facilities development limits the ability of center-based programs to expand quickly, there are relatively few barriers to entry or exit from family child care. Because family child care businesses operate out of existing housing, the supply is more elastic.

Home-based child care programs face their own challenges: Some family child care providers report that insurance companies have discontinued homeowner policies because the home is used as a business; zoning barriers prevent them from operating a home-based child care business; landlords are resistant to a child care business operating in a rental property, and there are conflicts with inspectors over the interpretation of regulations. Although such problems do not appear to be widespread, prospective family child care providers need access to advocates knowledgeable about real estate, insurance and regulatory issues to help resolve these barriers. Where a health and safety violation exists, a provider may need access to either micro-business loans or small grants.

Population density influences the mix of center and home-based care. Center-based programs become increasingly less viable in more rural areas of the state where the popu-

lation density is lowest. Rural communities will need to rely more heavily on home-based child care. The only exception to that is in school districts that operate state-funded preschool classrooms. In effect school-based programs are like centers in terms of group size, but because of the education funding available, school districts are spared some of the financial and program-size related constraints that face other child care centers. On the other hand, school-based programs, while providing a valuable pre-Kindergarten curriculum, are rarely a substitute for the full-day child care working parents also need. Therefore, even in rural areas with school-based programs, home-based family child care will continue to play an important role caring for children during the balance of the work day.

Inadequate supply and slow market response to increases in demand can slow economic growth. Child care supply is inextricably linked to economic development and employment growth. Its availability is a factor influencing business location and expansion decision making. As noted in *The Economic Impact of the Child Care Industry in Maine*: “Targeted investment in child care supply-building can contribute to labor force participation gains among lower- and middle-income families in Maine. Such gains would directly increase output, personal income, business formation, and property and sales tax revenue.”⁷

If quality of care is factored into the supply and demand equation, demand would be greater for all age groups. Key informants from within the child care industry, especially those in intermediary organizations, expressed the belief that the demand figures under- represent the need because families seeking high quality care are often forced to accept lower quality because of the limited options available in the market.

Quality

The specific link researchers consistently find between high quality early care and education and positive child outcomes is having a profound impact on the industry and on public policy. This link is a central factor in the growing public policy commitment to expanded access to child care and to a system that promotes quality. It has also been a potent force within the early childhood industry where professional development, credentialing and accreditation are increasingly embraced by practitioners.

As with the issue of supply, there is a dearth of systematically collected and analyzed data on facility quality. While there are tools that provide evidence of program quality⁸, no equivalent process or tool exists to rate facilities quality or to gauge how the physical environment of a center or home impacts program quality. However, experts in early care and education believe that how a facility is designed, configured and equipped can significantly boost program quality. In addition, the key informant interviews, plus a variety of reports on cost and quality, capture a range of problems related to the physical environment of early childhood programs, from day-to-day operating inconveniences and minor health and safety issues to major impediments to the achievement of program quality. One key informant estimated that 80% of the technical assistance requests she handles to address behavior problems in child care centers and homes turn out to be caused by problems with the physical environment. This is consistent with research indicating that “Tired or irritable teachers; apathetic hyperactive, or uninterested children; high noise level; large amounts of time spent in routine management; and excessive use of teacher-directed activity all have a high likelihood of being spatially induced.”⁹

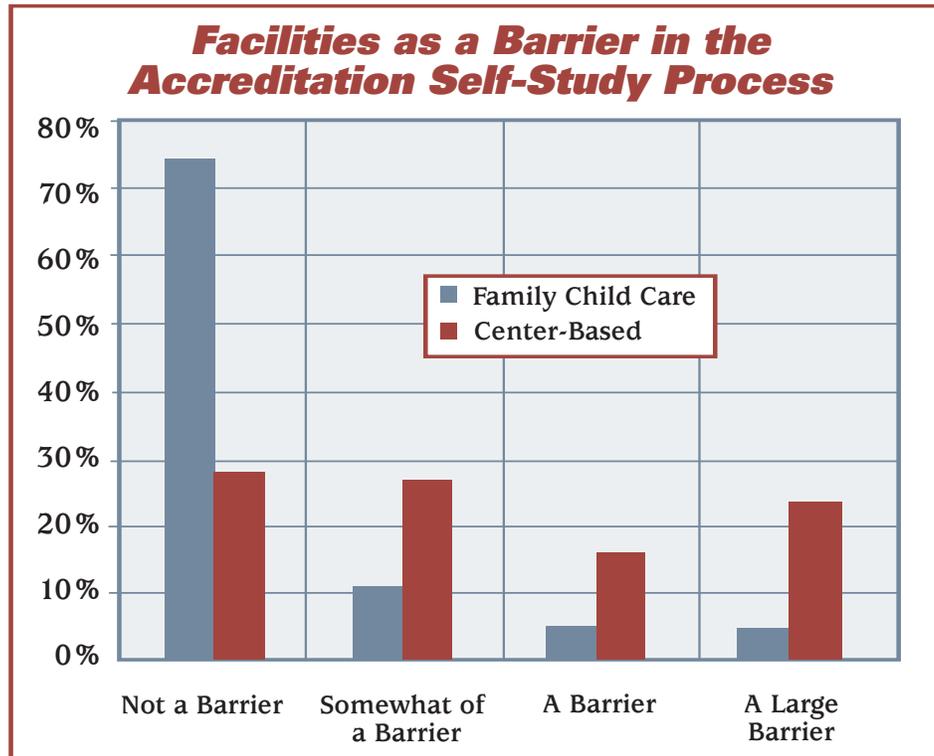
An inclusive list of facility quality issues identified by interviewees can be found in Appendix C. Some of the most critical and common facility deficits are summarized below. These challenges are not unique to Maine. They are found in every other state in which the authors of this report have conducted research. In almost every case, barriers to facility quality are rooted in the economics of child care delivery, and the lack of access to appropriate financial and technical support.

- **Adequate Classroom Square Footage.** Because of the high cost of capital for facilities, minimum state licensing regulations become the standard to which providers often design facilities. State licensing requires 35 square feet of useable classroom space per child. Those who have studied early childhood space recommend classrooms containing 45 to 50 square feet of useable classroom activity space.
- **Appropriate Non-Classroom Spaces.** In an effort to keep occupancy costs low, many centers don't include the type of ancillary spaces needed to support a good program, such as a teacher break room; teacher work space to prepare lesson plans and activities; private space (rather than a "staircase landing") for parent-teacher conferences; indoor gross-motor or multi-purpose space; and sufficient administrative offices.
- **Scarcity of Appropriate Buildings.** The high cost of real estate combined with the child care industry's limited capacity to compete for more desirable properties means that appropriate child care space is unavailable in some communities. Programs most often decide where to locate based on the cost, leading centers to be inappropriately housed in inconvenient

locations or buildings that were designed for other purposes.

- **Buildings that Cannot Easily Be Adapted for Child Care.** Many centers are located in buildings with difficult-to-change structural attributes such as having to walk through one classroom to reach another, which is disruptive and prevents optimal use of the space; lack of sinks and bathrooms either in or directly adjacent to and accessible from classrooms; and windows at heights that limit natural light and prevent children watching the world outside their classrooms.¹⁰

While the key informant interviews spotlighted isolated regulatory factors that either limited the supply or quality of center- or home-based child care, the most prominent barriers are associated with the unsupportable financial cost of creating quality early childhood environments. These problems disproportionately affect center-based programs. The growing interest in national accreditation for child care programs has made evident a few facility deficiencies that were not previously recognized. A survey conducted by Glenwood Research as part of its 2005 evaluation of Maine Roads to Quality's accreditation facilitation program indicated that center-based programs were far more likely than home-based caregivers to identify facility issues as barriers to accreditation (see following graph).¹¹ For example, in the course of conducting the self-study phase of the accreditation process, one child care director realized that the center's playground offered no shade, as expected by accreditation guidelines. Similarly the accreditation process has led some centers to recognize shortcomings in their physical facilities. The Glenwood survey only included providers seeking national accreditation.



Key Findings With Respect To Quality

Most center-based programs operate in physical space that is a barrier to program quality. The economics of child care dictate that most programs secure low-cost space; forego extensive renovations to adapt the building to meet the needs of programs serving young children, and force providers to minimize the amount of space they rent or buy. These problems are most acute for programs serving low-income children.

Capital needs are less frequently a barrier to quality in family child care. With the exception of family child care providers occupying substandard or poorly maintained housing, training and professional commitment, not significant capital needs, are most likely to result in programmatic quality. Some providers do seek to create dedicated space for the child care program, and have tapped into existing public and private resources to do this, including FAME’s childcare revolving

loan program, and home equity loans and child care investment tax credits.

School-based programs have capital needs that are not well recognized. Typical elementary school space is designed for older school-aged children with different developmental needs. Many classrooms, playgrounds and other areas of the school need to be modified to support quality programming. If schools are used for full-day programming through wrap-around services, which would be desirable for many families, appropriately modifying these spaces becomes a more urgent concern.

Facility quality is a more urgent need in Maine than supply-building. This report confirms some immediate and longer term supply-building challenges. However, the scale of the supply-building challenge is dwarfed by the need to improve the quality of center- and school-based facilities.



Family Focus – Brunswick

POLICY PRIORITIES

Policy Priorities

Any state effort to invest new resources in technical or financial support for facilities development should give priority to the following five factors:

Programmatic Quality – Any program receiving assistance should deliver high quality early childhood programming. Poor quality facilities prevent such programs from achieving their full potential but cannot substitute for well-trained and experienced teachers, positive adult interactions with children, appropriate teacher:child ratios, a sound curriculum, and effective supervision.

Facility Quality – Since supply building is not an urgent need in some geographic areas, more emphasis should be placed on creating high-quality learning environments than on securing space quickly. Moreover, it may be a poor investment to make large capital outlays to replace major building systems such as the roof or heating system in a facility that has not been adapted for use by young children and therefore fails to contribute to improvements

in programmatic quality. Programs occupying that kind of space should explore relocation to a facility that both has well-functioning building systems and has been adapted to support quality early childhood programming.

Low-Income Children – Public resources should focus on improving outcomes for low-income children by ensuring their access to high-quality programs and facilities.

Infant-Toddler Care – Priority should be given to programs that expand the supply of care for 0-3 year-olds in high need areas.

Collaboration – State investments in facilities should support the co-location of family services and supports, and the delivery of these services in a complementary manner. Similarly, part-day Head Start or school-based programs might collaborate with another provider to deliver wrap-around care in the same space to avoid transportation and disruption for young children.

RECOMMENDATIONS

Recommendations

Create an Advisory Panel

For decades the child care industry has undervalued the importance of the physical environment as an essential component of a high quality system of early care and education. As a result, the state has little infrastructure upon which to build institutional capacity. To elevate the importance of early childhood facilities for the industry and on the public policy agenda, Maine should convene a group of people with a stake in the industry's future to assume responsibility for guiding public and private efforts to address the need to invest more heavily and more thoughtfully in center- and school-based facilities, especially those serving low-income children. This group might take the form of a newly-created advisory panel to the Office of Child Care and Head Start or an existing entity, such as a task force to the Children's Cabinet or a subcommittee of one of its task forces. Its membership should include a diverse group of opinion leaders from government, education, child care, Head Start, and business to provide leadership in formulating strategies for improving early childhood facilities in Maine.

Create a Facilities Development Intermediary

To provide the real estate development expertise and infrastructure to enable child care organizations to develop real estate, Maine will need to support an entity that can provide early planning funds; build the capacity of providers and architects to incorporate best design practices into their plans, and serve as a disinterested but well-informed third-party advisor to help providers work with develop-

ment consultants or real estate development firms. This intermediary would include:

1. **staff and/or consultants** with real estate finance and development expertise and familiarity with the special needs of the child care industry to help center directors hire and manage a team of professionals; understand best practices in facility design; and make legal arrangements, negotiate regulatory reviews, raise capital, etc. The intermediary should also provide advice, and where appropriate, advocacy to family child care providers who are prevented from operating because of zoning, landlord-tenant, environmental, inspectional or insurance issues.
2. **low-interest or interest-free “predevelopment” resources** to enable providers to access a team of third-party development professionals upfront in the planning process. Predevelopment resources are advanced and placed entirely at-risk during the planning phase to pay professional fees of architects, lawyers and others, and to secure site control, perform environmental testing or other site review. The intermediary would need to be able to offer an unsecured predevelopment loan product: with interest and principal deferred until the project raises all the funds needed to proceed.¹²

The intermediary's operating costs might be supported with a combination of appropriated state funds, Child Care Development Fund 4% quality set-aside, and perhaps other appropriated state funds.

In other states the intermediary function is commonly performed by a nonprofit community development intermediary experienced



in working with community-based developers, has the staff expertise (or can acquire it) to advise providers on real estate development issues, not just finance ones, and has specific knowledge about the child care industry. The state might prepare an RFP to determine which organizations might be able to expand and diversify their expertise and program offerings to meet the state's needs. Some joint ventures may be organized in response to the RFP.

Coastal Enterprises, Inc. (CEI) is the state's most active private child care lender, having made 157 loans to child care centers and homes over the last 20 years. CEI makes relatively small loans averaging \$50,000. However, its child care loans range from a low of \$1,500 to a high of \$406,000. Cumulatively it has lent almost \$1.4 million to its largest borrower in six transactions. It uses a variety of capital sources to fund its loans. CEI was a pioneer in child care finance nationally and previously had a full-time staff person to work with child care providers. Because the grant funding for that position is no longer available, CEI has been unable to provide the same level of technical assistance. However, it now uses an outside contractor to assess the programmatic quality of its prospective child care borrowers. This focus on programmatic quality is unusual in a lender and reflects the organization's historic commitment to the child care sector.

Establish a Deep Capital Subsidy Program

Parent fees and state operating subsidies are insufficient to cover the cost of quality early childhood facilities. To make construction or thorough renovation of high quality nonprofit child care centers possible requires a deep capital subsidy equal to roughly two-thirds of the cost.¹⁵ Centers can be expected to repay a portion of the cost over time, however, the State of Maine would need to cover a signifi-

cant proportion of the debt service. This subsidy mechanism is described in detail in Appendix D.

The level of state subsidy required for any specific project will depend on the type of financing used. Fortunately, many areas in the state of Maine are eligible for USDA Rural Development Community Facility Loans which offer generous 40-year loan repayment schedules and an interest rate subsidy that is currently 4.25% for centers located in low-income communities. In communities that are ineligible for the USDA financing, the state could help providers secure the next most favorable financing – tax-exempt nonprofit revenue bonds. These bonds can be structured with long repayment periods and take advantage of favorable tax-exempt interest rates, although the combination is not as favorable as USDA's.

Illinois and Connecticut, two states that have used tax-exempt revenue bonds to finance nonprofit child care facilities, have entered into contracts with providers to pay a fixed percentage of the debt service each year as it becomes due. This spreads the state's cost, minimizing the budgetary impact on a specific fiscal year. This subsidy fills the gap between the amount of debt service the provider can afford and the total monthly or annual loan repayment. As an example, an annual state appropriation of \$750,000 for this purpose would be sufficient to finance 20 child care centers serving 1,000 children (whereas the upfront cost of financing 20 centers through grant or equity sources would be approximately \$20 million).

Current political will and fiscal capacity will likely limit the scale of this program. However, a modest state capital subsidy program relying on an annual appropriation of \$500,000 to \$1 million per year to meet current and future debt service repayment commitments would be sufficient to finance a number of model

early childhood facilities, especially if they are geographically targeted to areas of high need and involve interesting collaborations. For example, the recent report for the Task Force on Early Childhood proposed the creation of family service “HUBs” where various child and family services would co-locate or offer a broader request for innovative child care facility proposals that involve model service integration collaborations. In addition to child and family service HUBs, responses might include proposals to develop a partnership between a school system and a child care center to deliver state financed preschool services, wrap-around care, and infant and toddler child care in a shared facility, among other ideas.

Organizations sponsoring such projects should consider partnering with one of the state’s nonprofit affordable housing developers, such as Coastal Enterprises Inc., Avesta, local housing authorities and a number of community action programs – Community Concepts, Penquis Community Action and People’s Regional Opportunity Program among them. Nonprofit housing development organizations are more likely than the other participating human service groups involved in these partnership projects to have the technical real estate development finance and construction expertise needed to turn a capital subsidy into a successfully developed community facility.

Provide Technical Assistance and Access to Debt Capital for Modest Renovations to Existing Centers

While there is a need to provide deep capital subsidies to enable providers to build new facilities or substantially renovate existing facilities, it is unrealistic to expect the supply of subsidy to match the need. Therefore, an important role for the child care facilities intermediary is to provide technical assistance to providers in planning and arranging financing for more modest renovation projects. Even

relatively small investments, if they are made strategically to make the space function more effectively for children, teachers and parents, can pay significant dividends in the form of improved quality.

Create a Family Child Care Forgivable Loan Program to Address Health and Safety Issues and Encourage Quality Improvements

In the past, Maine has offered small capital grants to family child care providers. The state should create a similar program to cover the cost of resolving health and safety issues. Interest-free loans of up to \$2,000 should be available to quality providers with the principal balance being forgiven over a period of perhaps three, four or five years, as long as the family child care home continues to operate and meet appropriate public purpose objectives. If the provider discontinues operations before the full amount has been forgiven, the provider will be obligated to repay the remaining principal balance.

The use of these funds could also be extended beyond health and safety requirements to address quality issues, such as the purchase of age-appropriate furnishings and equipment for indoor or outdoor use. This would be most effective if offered through an existing family child care support system – Maine Roads to Quality, an RDC, or the child care facilities intermediary – which could offer related technical assistance on how to make meaningful quality improvements.

Fund a Family Child Care Certification Advisor to Help Providers Resolve Regulatory Issues

Interviewees reported instances where family child care providers encountered regulatory or legal barriers to opening or securing state certification. Although there was no evidence that

such problems are widespread, providers should be able to seek the advice of someone familiar with zoning, environmental, and health and safety issues. As with the forgivable loan program for family child care providers described above, this type of advisor could be affiliated with Maine Roads to Quality, an RDC, or the child care facilities intermediary, and have statewide responsibility to help prospective family child care providers gather information to understand and navigate difficult regulatory obstacles.

Explore the Feasibility of an Individual Asset Building Program for Low-Income Family Child Care Providers

One strategy to assist lower-income home-based caregivers, especially renters, is to integrate “individual asset building” into child care policies and encourage other organizations pursuing individual asset building as a strategy to add child care to their programs. Individual development accounts (IDAs) match a low-income individual’s savings in an account restricted to specific purposes such as a down-payment on a home and further education. This program might be linked with other asset building strategies, such as first-time homebuyer programs. CEI, for example, has a Lease-Purchase Program designed for individuals with insufficient savings to make a down payment or cover closing costs; with previous credit problems that they have taken steps to remedy; or who do not qualify for a mortgage because of self-employment. IDAs, homeowner education and business counseling are common features of individual asset building programs. Home-based child care providers who have earned a quality certificate and have shown a commitment to maintain their family child care business would be good candidates for this type of strategy for stabilizing their home-based business.

Engage School-Based Preschool Programs in Early Childhood Facility Planning and Development

Prekindergarten is becoming an essential bridge young children cross on their developmental journey into the formal public educational system. But preschool is part of a mixed, public-private system that has two critical missions: to provide early education that prepares young children for academic success and to provide high quality, nurturing and developmentally appropriate care for the children of working parents. Both private child care and public prekindergarten are part of the same value chain and both should use their unique strengths to complement the other.

School buildings with available space offer an opportunity for additional early care and education services in the community, but quite frequently school buildings, classrooms and playgrounds need to be adapted to create good learning environments for young children. Public schools that create or allocate space for preschool programs will need access to the type of early childhood design resources that the facilities development intermediary will be developing and disseminating, and should be included in any provision of technical assistance and training on this topic. In addition, the state should consider using its deep capital subsidy program to encourage joint planning for facilities between the school system and early childhood providers, and to finance public school improvements to prekindergarten classrooms if such renovations are part of a plan to strengthen the overall fabric of education and care for children birth to five.



Toddle Inn



Appendix A:

List of Key Informant Interviewees

Jane Adams, Waldo County Head Start/ Maine Head Start Directors Assoc.

Richard Aronson, Medical Director, Maternal and Child Health, DHHS

Lisa Ayotte, So. Kennebec Child Development Corporation

Debbie Bellemare, Family child care provider

Bruce Berkowitz, Region 1 ACF, US Department of Health and Human Services

Janine Blatt, State Department of Education

Helen Brimigion, Small Business Administration

Blake Brown, Coastal Enterprise Inc

Scott Brown, Director of Facilities, Department of Education

Cheryl Carrier, Toddle Inn

Sue Chevalier, Center for Community Inclusion and Disability Studies

Deborah Cole, Finance Authority of Maine

Dana Connors, Maine Chamber of Commerce

Brian Dancause, Department of Community and Economic Development

Carolyn Drugge, DHHS–Early Childhood Division

Linda Elias, Child Care Connections

Mike Finnegan, Coastal Enterprise Inc.

Tim Fuller, State Fire Marshal

Peter Geiger, Geiger Brothers

Susan Gendron, Commissioner of Education

Bill Glover, Maine State Housing Authority

Ellie Goldberg, Maine Children’s Alliance

Bill Hager, Child Care Services of York County

Chris Hall, Maine Chamber of Commerce

Janet Henry, Maine Philanthropy Center

Alex Hildebrand, Muskie School, USM

Sonya Howard, Maine Roads to Quality

Kathleen Kearney, Coastal Enterprise Inc

Joyce Kyllonen, Catholic Charities

Linda Labas, Center for Community Inclusion and Disability studies

Ronald C. Lambert, Jr., USDA Community Programs Director

Amanda LeClerc, Stepping Stones Day Care

Lorna Leo, Child Care Connections

Peter Lindsay, United Way Success by Six

Eileen MacAvoy, Piscataquis, Penobscot Counties Resource Development Center

John Massaua, Maine Small Business Center

Dewey Meteer, Child Development Services, Department of Education

Nancy Meagher, Bank of America

Laurie Mondville, Family child care provider

Charlene O’Clair, Director, Sandcastle Preschool Program Foundation

Erin Oldham, Glenwood Research

Lee Parker, Family Focus

Sue Reed, Maine Roads to Quality

Steve Rowe, Attorney General, State of Maine

Connie Roy, parent

Aaron Shapiro, Portland’s Division of Housing and Neighborhood Services

Betsy Squibb, University of Maine at Farmington

Bob Steinberg, Child Care Licensing

Lauren Sterling, Children’s Cabinet

Louise Stoney, National Child Care Information Center

Peter Taylor, Maine Community Foundation

Richard Taylor, Fire Marshal

Paula Thomson, Maine Office of State Planning

Alton W. Wedberg, USDA Community Programs Area Specialist

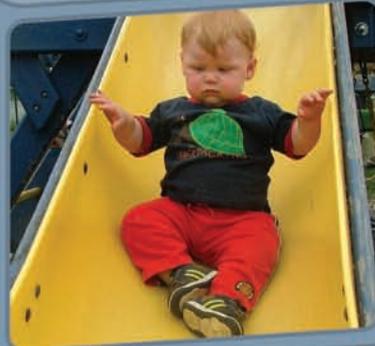
Owen W. Wells, Libra Foundation

Orman Whitcomb, CDBG Program Manager

Karen White, Central Maine Community College

Patti Woolley, Kennebec Valley Community Action Program

Ken Young, Kennebec Council of State Governments



Appendix B:

Financing & Technical Assistance Programs

Some of the financial resources described below, and other forms of subordinated debt financing, can be accessed through intermediaries such as community development corporations and Councils of Governments.

Financing Programs

SBA programs for private, for-profit businesses

- 1. SBA 7A Loan Guarantee Program** provides a 75% (or under certain circumstances 85%) guarantee on bank loans of less than \$2 million. 7A allows lenders to charge the prime rate [currently roughly 6%] plus 2% for loans with a term of 7 years or more. Loans can be used for fixed assets, such as real estate, construction costs and equipment purchases, and also working capital. The term can be from 15-25 years.
- 2. SBA 504 Direct Loan Program** finances real estate, building construction, and equipment. The 504 program involves a fully-secured bank loan for 50% of the borrowing amount and an SBA certified development company taking a second mortgage on 40%. Maine has three certified development companies: CEI, Eastern Maine Development Corporation, and New England Business Finance (also known as Granite State Development Company). SBA loans are fixed rate and generally charge rates lower than commercial rates—slightly below prime plus 2 percent for origination and servicing fees. The term on a 504 loan is either 20 years for real estate or 10 for equipment. The maxi-

mum 504 loan is \$1.5 million with public policy priorities allowing up to \$2 million (this might include child care).

- 3. Micro-Business Loans** are available to family day care businesses through CEI, some of the Councils of Governments, as well as Portland and several other towns.
- 4. Community Development Block Grant Program** – Child care and Head Start programs have chiefly received funding through the CDBG public services program, which subsidizes program operations. The CDBG Planning Grant Program covers up to \$10,000 in professional planning services, such as architectural fees. The Public Facility Program, with grants of up to \$300,000, covers capital costs. However, most funds are awarded to towns to build fire stations and community centers. Under the state plan, child care facilities are technically eligible but are not a priority category. Funding is highly competitive.

US Department of Agriculture, Rural Development, Community Facilities Programs

USDA can make and guarantee loans for community facilities in rural areas and towns of up to 20,000 in population owned by public entities, non-profit corporations and tribal governments.

- 1. Community Facilities Direct Loan** – This program makes long-term, low-interest loans. Rates are currently 4.25% for borrowers in low-income communities although rates fluctuate with the market. Loan terms are up to 40 years. USDA has a great deal of flexibility in how they structure the loan, and they use that flexibility to create terms and loan amounts to maximize a project's chances of successfully servicing the debt. Although the state of

Maine's allocation for this program is \$3-4 million, historically the office has sought and received additional funding. Typical lending in Maine is \$8-10 million. This year Maine's direct loans are close to \$20 million. (The availability of these funds may be affected by the reallocation of USDA appropriations for the program to hurricane relief in the Gulf Coast area).

2. **Small Grant Child Care Set-aside** – USDA can make a grant of up to 75% of the cost of a project, up to \$50,000. The grant amount depends on the community's median income level, starting at \$15,000 for a project located in a town whose median income is less than 90% of the state's median. The grant rises to \$50,000 for projects in communities where the median income is less than 60% of the statewide median.
3. **Planning Grants** – Planning grants are only available in areas with extremely low workforce participation rates. The only areas qualifying in Maine are the two Passamaquoddy reservations.
4. **Community Facilities Guaranteed Loan Program** – USDA will also provide 90% guarantees on loans made to eligible borrowers who can qualify for conventional loans with this credit enhancement.

USDA, Rural Development Business Programs

Business and Industry Guaranteed Program

– Commercial businesses located in communities with fewer than 50,000 people are eligible for guarantees up to 80 percent of a loan made by a commercial lender. Whereas SBA's equivalent guarantee covers a maximum of \$500,000 of debt, USDA's guarantee can be up to \$10 million.

Finance Authority of Maine (FAME) Child Care Revolving Loan – A state bond issue four years ago created a \$300,000 revolving loan for child care. The borrower needs to provide collateral and the maximum loan size is \$100,000. Because of the rates, amount of money available, terms and collateral requirements, the program has made only three loans, all to family child care providers. Although the program is open to family child care businesses located in leased premises, unless the provider has considerable personal assets, it is unlikely she would qualify for a loan. Two of the three loans were to add dedicated space for the child care program. Six loan applications have been denied. All non-profit applicants have been unable to satisfy the underwriting requirements.

Head Start Grants

Head Start grantees are eligible for one-time capital grants from the federal Head Start program that can be as high as several hundred thousand dollars (generally up to 25% of the total project cost), although these grants are getting smaller and harder to get. Among other things, these grants have been used to retrofit several elementary school classrooms to accommodate preschool-aged children.

Maine Child Care Investment Tax Credit

As an incentive for providers to make financial investments that enhance the quality of child care programs, the Office of Child Care and Head Start certifies whether a specific investment contributes significantly toward the goal of providing quality child care services. Individual taxpayers can receive a tax credit equal to 10% of their investment for ten years. Corporations and partnerships are eligible for a credit equal to 30% of investments up to \$30,000. The tax credit is only calculated on that portion of the investment that is certified as contributing to improved quality.

Maine State Housing Authority

The first two of the MSHA programs listed below involve the state's community action agencies as partners, many of whom operate Head Start and/or child care programs. These programs may be especially useful to low-income family child care providers.

- 1. Lead Control Program** – Lead paint was repeatedly cited as a problem for home-based caregivers because of the state's old housing stock. MSHA provides grants to low-income homeowners and renters for lead paint hazard control.
- 2. Home Rehabilitation Program** – Low income homeowners are eligible for very low interest loans – 1 % for 20 years – to finance the replacement of failing home components.
- 3. Low Income Housing Tax Credits** is a federal subsidy for the development of rental housing. MSHA administers that program in Maine. A portion of the equity raised through the sale of these tax credits can be used to cover a portion of the cost of community facilities that are part of the housing development, including child care centers. However, the use of housing tax credits for child care is more feasible in conjunction with large developments. As a matter of policy in Maine most tax credit projects are relatively small; in the 24-30 unit range. Affordable housing developers and child care providers should be regularly reminded of this financing source to increase the chances that opportunities to use tax credits for child care facilities are identified and used.

Coastal Enterprises, Inc. (CEI)

CEI finances all types of child care – home- and center-based, and profit and nonprofit. Since 1985 CEI has provided 157 loans totaling \$7.7 million to create or sustain 4,458 cen-

ter-based and home-based child care slots. Individual loans have ranged from \$1,500 to \$406,000 although its largest borrower received six loans totaling almost \$1.4 million. CEI's average loan is approximately \$50,000. Its longest term is 20 years but is shorter term, approximately 3 to 5 years, for family child care or working capital. CEI is more willing than conventional lenders to structure loans flexibly to meet a borrower's unique needs. For example, it might charge interest only for a brief period before the principal portion begins to amortize. This can be helpful with a new child care center where it takes some months to build enrollment and therefore the center's revenues might be insufficient to service the principal portion of the loan for a number of months. Family child care providers typically borrow for working capital, equipment, or to construct an addition. Most of these loans are in the \$2,500 – \$10,000 range. CEI is one of three SBA certified development companies in Maine. This allows CEI to offer second mortgages of up to \$1.5 million or 40 % of a project's cost.

Technical Assistance Programs

- 1. SBA Women's Business Center** - CEI operates the center out of its Augusta office. SBA uses the Kaufman Foundation curriculum to assist family child care start-up businesses.
- 2. The Maine Small Business Center** provides business planning assistance to for-profit center- and home-based child care business start-ups and expansion.
- 3. USDA Specialists** – The USDA community facility staff at its four regional offices in Presque Isle, Bangor, Lewiston, and Scarborough, are very helpful in arranging USDA loans.



***Magic Years – Southern Kennebec
Child Development Corporation***

Appendix C:

Inventory of Facility Quality Issues

Interviews and observations produced the following list of factors that commonly impact the quality of early care and education facilities in Maine:

Adequate Classroom Square Footage: Because of the high cost of capital for facilities, minimum state licensing regulations become the standard to which providers often design facilities.

- State licensing requires 35 square feet of useable classroom space per child. Those who have studied early childhood space recommend classrooms containing 45 to 50 square feet of useable classroom activity space, and even more for programs serving infants and toddlers or children with special needs.¹⁴
- While the trend to improve program quality is evident in recently revised state regulations reducing group size, licensing regulations for centers allow larger rooms to be subdivided by barriers higher than the eye-level of the children using the space. This lack of acoustical separation between groups often contributes to excessive noise levels.

Appropriate Non-Classroom Spaces: In an effort to keep occupancy costs low, many centers don't include the type of ancillary spaces needed to support a good program, such as a teacher break room; teacher work space to prepare lesson plans and activities; private space (rather than a "staircase landing") for parent-teacher conferences, indoor gross-motor or multi-purpose space; and sufficient administrative offices.

Scarcity of Appropriate Buildings: The high cost of real estate combined with the child care industry's limited capacity to compete for more desirable properties means that appropriate child care space is unavailable in some communities. Programs most often decide where to locate based on the cost, leading centers to be inappropriately housed in inconvenient locations or buildings that were designed for other purposes.

Buildings that Cannot Easily Be Adapted for Child Care: Many centers are located in buildings with difficult-to-change structural attributes:

- Having to walk through one classroom to reach another, which is disruptive and prevents optimal use of the space.
- Old and inefficient mechanical systems such as heating, electrical and plumbing.
- A lack of sinks and bathrooms either in or directly adjacent to and accessible from classrooms.¹⁵
- Insufficient natural light and lack of windows at heights that permit children to directly observe the environment outside their classrooms.
- Poor artificial light, and, in particular, an over-reliance on fluorescents. One director referred to her center as "fluorescent heaven."
- Acoustical problems. Low-cost solutions, such as hanging fabrics and other materials, to provide some short-term relief, are often required to be removed because they create a fire hazard.

- Inadequate storage space resulting in cluttered corridors that create evacuation hazards and over-stimulating classrooms.
- Often the shape, size and proportions of classrooms cannot accommodate enough equipment, increasing the classroom management burden on teachers, and impeding circulation within the room.
- It is difficult and expensive to adapt public school classrooms for preschool programs. One interview said, “People don’t understand the impact of space on four-year-olds; schools don’t have enough space to set up appropriate environments.”
- Because of limited classroom space, cubbies are sometimes located in corridors where they pose a potential fire safety and evacuation risk.

Inadequate and Deferred Maintenance:

Insufficient operating revenue to lease newer and better-managed properties means centers often locate in buildings where maintenance is inadequate or needed repairs have been deferred.

- A number of interviewees reported mold and rodent problems, conditions that can pose a health risk.
- Uneven heating caused by inefficient older heating systems. The resulting conditions create an uncomfortable work environment for staff. An equally chronic problem, especially in drafty rooms, is the existence of horizontal temperature zones that leave either children or caregivers uncomfortable. As one interviewee noted, “Heat above 48 inches does not get down to where the children are.”

Outdoor Playspace: Accreditation has made more providers aware of the importance of outdoor play space. As a result, a number of interviewees identified outdoor playgrounds

and equipment as being inadequate to meet expectations for programmatic quality. Playgrounds accessible to handicapped children are extremely rare.

Cost of Regulatory Compliance:

Fire safety issues are among the most common licensing problems.

- Lead paint removal is a common problem encountered in older buildings.
- Also deterring renovations is the added cost of complying with current building codes and the Americans with Disabilities Act (ADA). Handicapped access required by the ADA is an issue, especially for classrooms located on the basement level.

Home-Based Child Care: Home-based child care programs face their own, albeit less dramatic challenges in creating appropriate physical settings for young children:

- Maine’s housing stock is aging. Older homes are more likely to have conditions that present health and safety risks.
- Supervision may be an issue in family child care homes that use multiple rooms. However, the alternative of using only one room can lead to overcrowding.
- Previously available quality improvement mini-grants of \$500-2,000 enabled providers to buy indoor and outdoor equipment and to fence yards. Indications are that many providers are reluctant to or cannot afford to fence yards and purchase outdoor play equipment without the incentive of grant funding.
- Some family child care providers report that insurance companies have discontinued homeowner policies because the home is used as a business. Presumably a child care business increases the risk to insurers. The extent of this problem is unknown.

- One key informant reported that some fire inspectors require family child care providers to install exit signage and emergency lighting like that found in commercial facilities. It was also reported that some home-based child care businesses have fire safety issues, including some caused by “housekeeping issues,” excessive basement storage, no second means of egress, use of extension cords and other hazards. One health and safety official observed the tension created when in the caregiver’s mind, their home is their castle, but from the perspective of those carrying out state mandated inspections, once a provider cares for someone else’s children, a house “is no longer just their home.”
 - Most family child care is located in owner-occupied dwellings. Tenants sometimes encounter landlord resistance to a child care business operating in a rental property because of concerns about liability and wear and tear on the property.
 - Environmental restrictions may prevent caregivers living in homes with septic systems from operating a child care business because the added use may exceed the system’s capacity.
- Other Issues:** Interviewees reported isolated circumstances where local land use policies were allegedly used to discourage or prevent child care homes or centers from opening. Some suspect that these issues reflect neighborhood concerns about noise or traffic a child care business might cause.

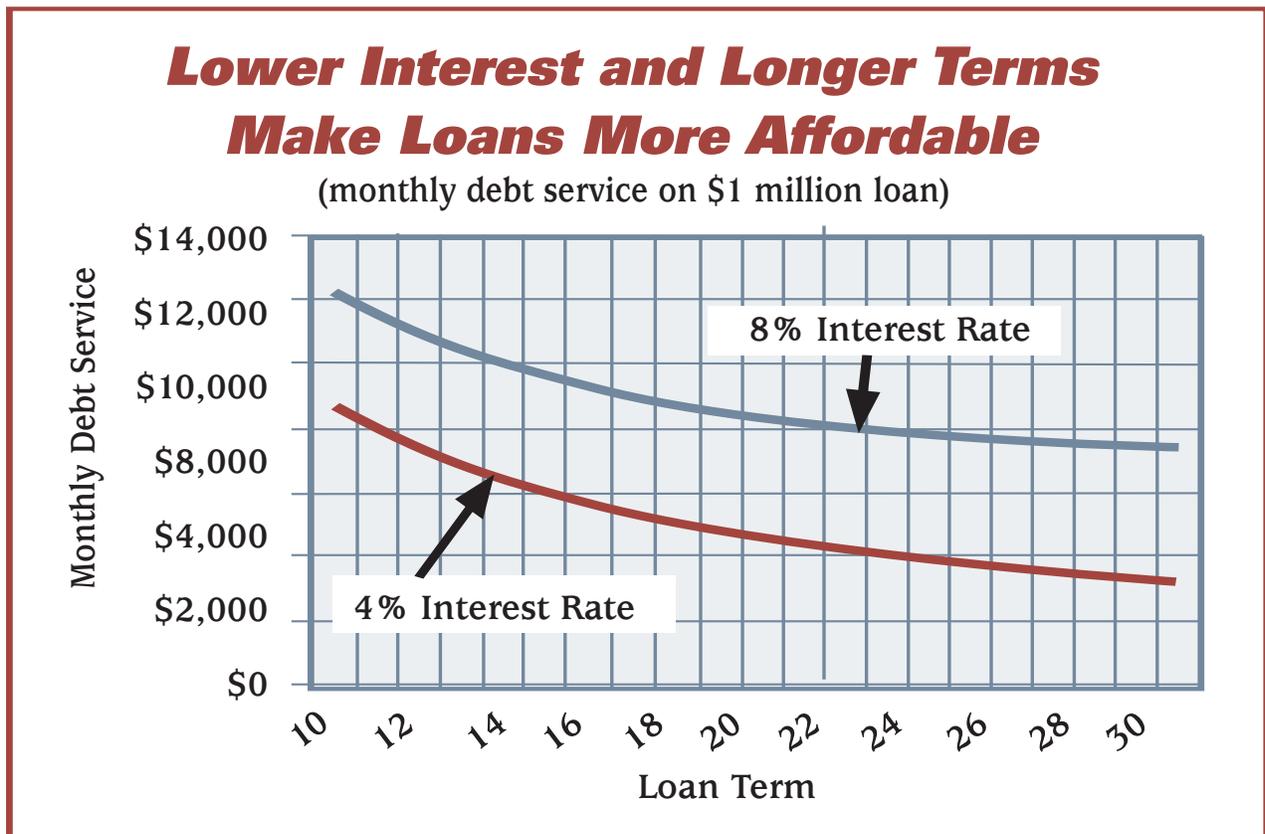
Appendix D: Design of a Deep Capital Subsidy Program

Since the combined child care program income derived from parent fees and state operating subsidies is not sufficient to cover all the costs of operating quality child care programs, including the cost of quality facilities, the construction of facilities will require a deep capital subsidy equal to roughly two-thirds of the cost.¹ The subsidy and the project's costs should be amortized over a long period to minimize the fiscal impact on the state budget; to increase the proportion of the cost the provider could be expected to carry, and, because facilities are long-term capital assets, to spread the cost over its useful life. Also, for reasons of affordability, the interest

rate should be as low as possible. The combined effect of extending the term of the loan and reducing the interest rate is illustrated in the accompanying graph.²

A number of vehicles are available to secure very long-term loans at low interest rates:

- The USDA Rural Development program's Community Facilities loans that are available to nonprofit child care centers in communities with fewer than 20,000 people can be secured with a term of 40 years and an interest rate as low as 4.25% (although the actual rate depends on a combination of median family income in the community and the cost of money). The USDA office in Maine has shown considerable interest in making Community Facilities loans for child care.



- A second source of long-term loans is non-profit tax-exempt revenue bonds. Interest earned by the bondholders is exempt from federal income taxes, making the rates lower than what is commercially available. Terms can be as long as 30 years. To secure the lowest interest rates the underwriter would need to determine that the risk of default is low.

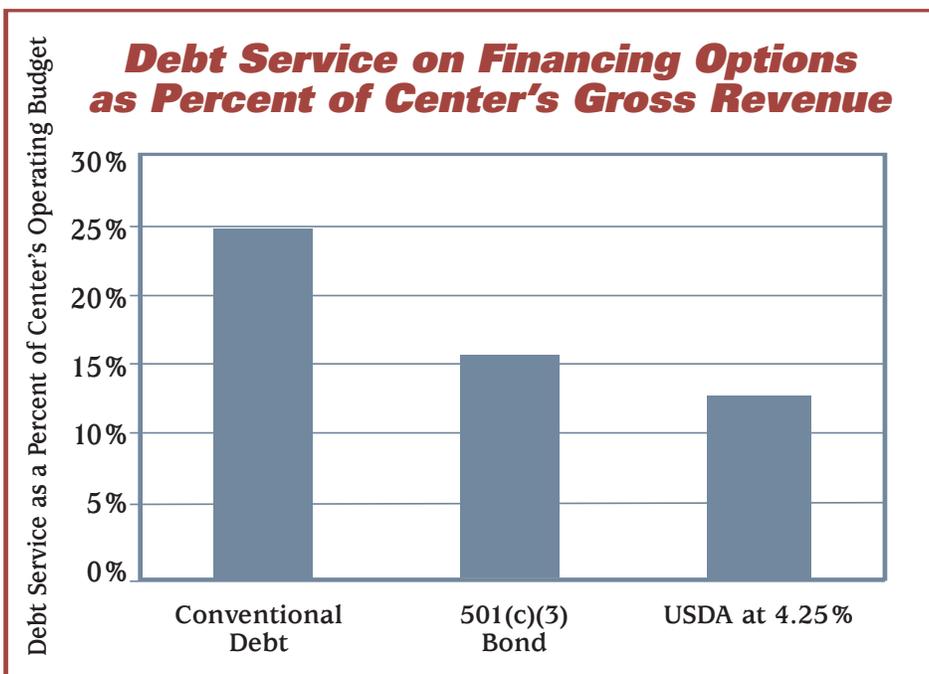
The following table and graph illustrate the impact that rate and term have on affordability with three different financing scenarios: 1) conventional debt from a private lender; 2) non-profit tax-exempt revenue bond debt, and 3) USDA Rural Development Community Facilities Loans. In each case, a \$1.1 million loan finances the construction of a four-classroom child care center serving 50 children, from birth to five years of age. The “affordability” of the debt service is expressed as a percentage of the

center’s operating revenue. The lower the debt service is as a percentage of the center’s overall revenue, the more affordable the loan is.

- Compared to the other examples, the conventional loan has the shortest term and highest interest rate. It would take about 25% of the center’s income to repay the loan.³

Financing Options	Terms in Years	Interest Rate	Loan Principal Amount	Debt Service as % of Revenue
Conventional Debt	20	8.00%	\$1,100,000	25%
501(c)(3) Bond	30	5.00%	\$1,100,000	16%
USDA at 4.25%	40	4.25%	\$1,100,000	13%

- The second example assumes the sale of 501(c)(3) tax-exempt revenue bonds. With a 5% interest rate and a 30-year term, annual debt service is about 16% of a child care program’s gross revenue, which is more affordable than conventional debt.⁴



- The third example uses the USDA Community Facilities program. This vehicle’s favorable interest rate subsidy and 40-year loan repayment term greatly increase affordability compared to conventional loans and provide more favorable financing than the tax-exempt bonds. However, since eligibility for USDA Community Facility Loans is limited to communities with fewer than 20,000 residents and the interest rate subsidy

depends on the town's median income, many child care facilities may be ineligible for these loans or its most affordable options.

For many providers, using 13% of revenues to repay even the most favorable financing source of USDA loans may present a considerable challenge.⁵ Most operators will require a further capital subsidy to finance the major construction or renovation of a facility beyond a favorable loan with a long term and low interest rate.

Debt Service Repayment Model In other states where tax-exempt revenue bonds have been used to finance nonprofit child care facilities (Illinois and Connecticut), the state has layered an additional and substantial capital subsidy on top of the financial benefits that are gained from the longer loan terms and lower interest rates available with tax-exempt bond financing. This additional subsidy takes the form of a contract with the provider for the state to repay a fixed percentage of the debt service each year as loan payments become due. This strategy recognizes that many providers, particularly those serving lower-income children, cannot afford to devote a significant proportion of their revenues to debt service.

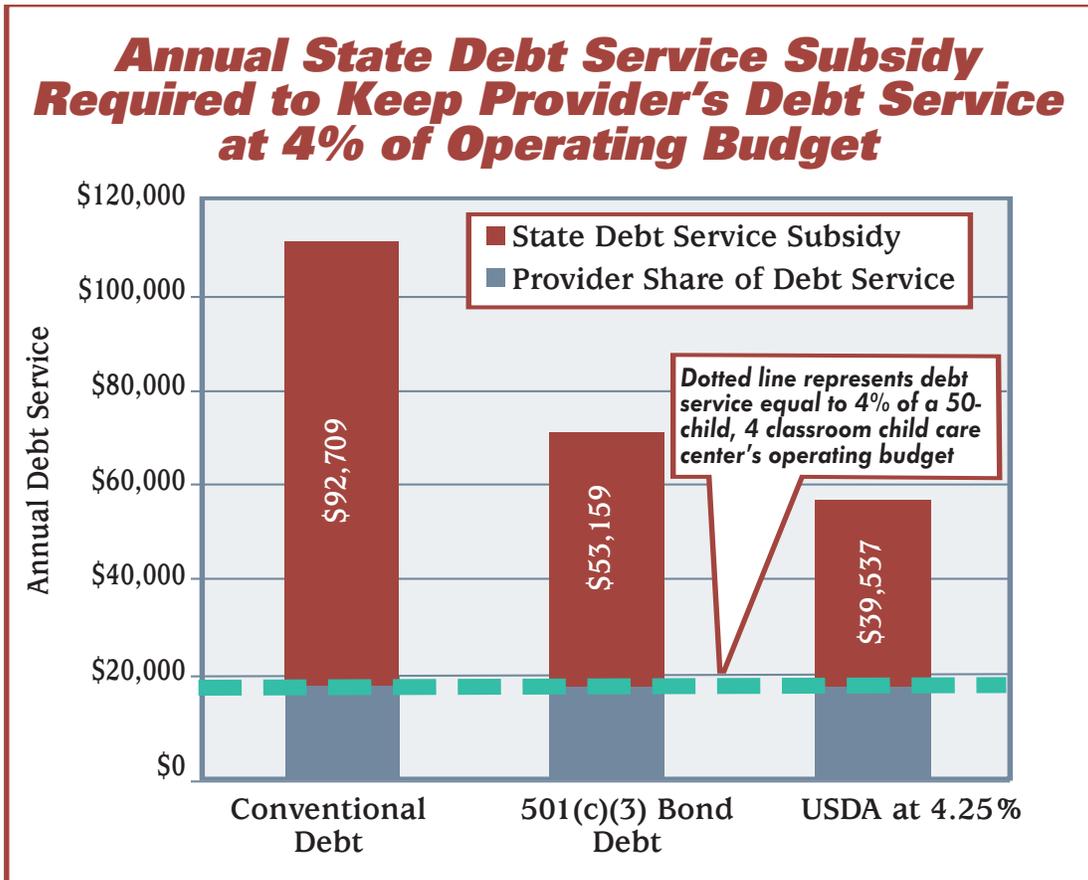
In Connecticut and Illinois this type of innovative state-supported debt repayment program offered in conjunction with tax-exempt bond financing combined three important strategies for making facility development more affordable to a provider:

1. it enabled providers to benefit from longer loan terms than are available on conventional loans;
2. it provided an interest rate subsidy, and
3. the state's repayment of a substantial portion of the debt created an additional level of capital subsidy, further reducing the provider's monthly debt service payments.⁶

As an alternative to annual debt service payments, the state could structure the subsidy as a capital grant to the provider. This would have the effect of reducing the amount the provider would need to borrow. However, each grant would require a large one-time state budgetary outlay. To allow the state to subsidize the construction or renovation of more centers, it makes more sense to spread the cost over a period of years using debt financing, thereby reducing the upfront cost.

Assuming that nonprofit child care centers in Maine serving mostly low-income children can afford to devote roughly 4% of their gross receipts to retire a facility loan, the following graph shows the state's annual debt service associated with the three financing scenarios described above.

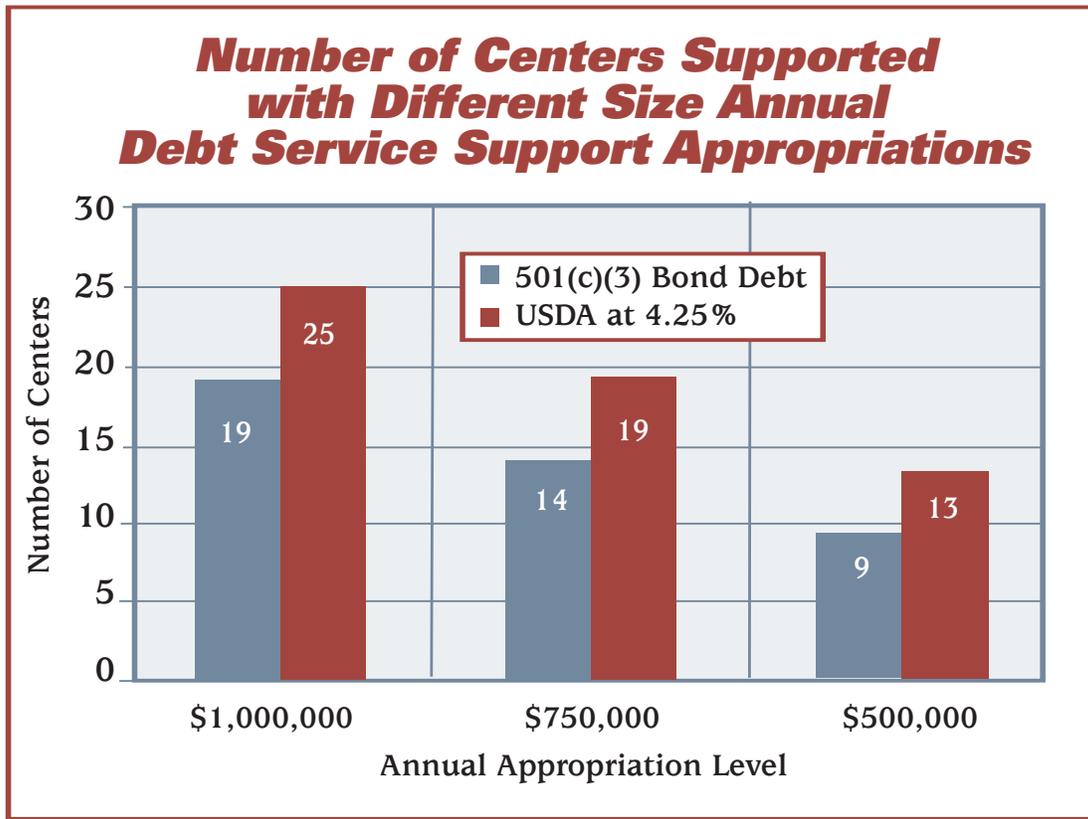
Using the most favorable financing scenario under the USDA Community Facilities Loan program as an example, the state could provide an annual subsidy of \$39,537 to close the gap between the debt service the center can afford to pay (4% of its operating budget or roughly \$17,700), and the full debt service expense. That translates into \$791 per year per child.⁷ Alternatively, the state could make a one-time capital grant of \$760,000. The grant would have the same effect: it would reduce the center's debt service to \$17,700 which is equal to 4% of its gross revenue. By financing the \$760,000 capital cost through the USDA loan instead of making an upfront capital grant, the state can spread the cost through modest annual payments. Equivalent debt service subsidy or capital grant options could be used in conjunction with the conventional bank loan and the tax-exempt revenue bond: Under the tax-exempt revenue bond scenario the state's debt service repayment commitment would need to be \$53,159 per year or \$825,000 as a one-time grant, and subsidizing conventional debt would cost the state \$92,709 per year or \$924,000 as a one-time grant.



Both Illinois and Connecticut have used debt service support payments to subsidize the capital cost of multiple child care facilities in conjunction with tax-exempt revenue bonds to have a greater and more immediate impact on the supply and quality of early childhood facilities across the state. The following graph compares the number of centers that could be financed with state annual debt service appropriations of \$500,000, \$750,000 and \$1 million using the two most affordable financing scenarios described above – the USDA loan and the tax-exempt revenue bond. One million dollars in annual debt service would leverage \$20.7 million for facilities construction using the tax-exempt bond mechanism (assuming a 5% interest rate and a 30-year term) – enough to build 19 centers serving 941 children. One million dollars in annual debt service using the USDA financing mechanism would leverage \$27.8 million – enough

to build 25 centers serving 1,265 children.

Using debt rather than grants enables states to maximize investment in facilities by spending a modest amount each year instead of a substantial upfront budget outlay. Through a modest annual debt service repayment appropriation of \$500,000 to \$1 million to spread the cost of facilities over future years, the State of Maine could strategically finance the development of a number of model facilities that promote the state's early childhood objectives. For example, the recent report for the Task Force on Early Childhood proposed the creation of family service "HUBs" where various child and family services would co-locate. The availability of facilities capital could encourage organizations and public agencies to propose family service models involving innovative service integration collaborations. In addition to child and family service HUBs, responses might include proposals to develop partner-



ships between school systems and child care centers to deliver state-financed preschool services, wrap-around care, and infant and toddler child care in a shared facility, among other ideas. The number of centers a debt service appropriation could support might be increased if it was determined that centers

could afford to pay 5 or 6% of gross revenue for debt service and/or the state required an equity contribution in the form of local fundraising to reduce the amount of debt. These are options that the LISC team could model should this financing concept prove politically and financially plausible.

¹ The proportion of the cost that must be subsidized depends on a number of assumptions that would require further exploration with policymakers.

² The graph compares monthly payments on a \$1 million loan at 4% and 8% interest. As the term increases from 10 to 30 years, the monthly cost declines. The effect of reducing the interest rate from 8% to 4% reduces the cost of a 10 year loan by 17% and a 30 year loan by 35%. The monthly payment on the 30 year loan drops from \$7,300 to \$4,800.

³ In reality, a conventional lender would not finance the entire project cost, whereas the other two approaches can finance 100% of the project cost. To simplify the analysis, this comparison assumes that the entire \$1.1 million cost is financed with debt.

⁴ To illustrate the effect these different loan terms have, several simplifying assumptions have been made. A 501(c)(3) bond involves high transaction costs which make them practical only with large loans or by selling a bond pool that combines financing for multiple projects.

⁵ Occupancy cost includes debt service as well as other costs related to operating and maintaining the facility.

⁶ Moreover, USDA loans and revenue bonds permit 100% of the cost to be financed. Conventional lenders typically lend no more than 70 or 80% of the project's value. The cost might even exceed the market value creating a further gap that must be filled with either grants or donations that function as equity or with difficult to secure subordinated debt.

⁷ Further research would be needed to determine if any regulatory restrictions exist for the use of supplemental state contract revenue as a USDA loan repayment source and, if so, to explore ways to structure the state's payments in a way that would allow the use of the state's capital subsidy with USDA financing.

¹ Evaluation of Maine Roads to Quality conducted by Glenwood Research, January 2005.

² Among the state's nonprofit affordable housing developers are: Coastal Enterprises, Inc. Avesta, local housing authorities and a number of community action programs – Community Concepts, Penquist Community Action and People's Regional Opportunity Program among them.

³ Alex Hildebrand, *The Economic Impact of the Child Care Industry in Maine* (2003), p. 15-16.

⁴ "Maine: Geography and Demography," Maine Center for Disease Control and Prevention, Office of Data Research and Vital Statistics. page III 11, <http://www.maine.gov/dhhs/bohodr/DEMO2000.RTF>

⁵ "Maine: Geography and Demography," Maine Center for Disease Control and Prevention, Office of Data Research and Vital Statistics. Page III 5, <http://www.maine.gov/dhhs/bohodr/DEMO2000.RTF> showing population by county, 1997. December 17 1999.

⁶ See the next section on quality for a fuller discussion of the need for facilities specially designed for child care.

⁷ Alex Hildebrand, *The Economic Impact of the Child Care Industry in Maine* (2003), p. 15-16

⁸ Tools include the National Association for the Education of Young Children (NAEYC) Accreditation Standards and the Early Childhood Environmental Rating Scale (ECERS).

⁹ Sybil Kritchevsky and Elizabeth Prescott with Lee Walling, *Planning Environments for Young Children: Physical Space*, NAEYC, Washington DC, 1977, p. 42.

¹⁰ Access to running water and toilets is extremely important to a well-functioning classroom. Without them, teachers often must leave the classroom to accompany children to the bathroom or to prepare for or clean up after activities. This means that the classroom is left with too few caregivers during these errands. In addition, having accessible bathrooms enables children to use the facilities when they need to, and promotes autonomy.

¹¹ Interview and email exchange with Erin Oldham, Glenwood Research, October 27, 2005.

¹² Because of the high-risk nature of predevelopment lending, loss rates should be expected to be high. For that reason some intermediaries, particularly those assisting child care providers, offer an interest-free "recoverable grant" to cover predevelopment expenses. Since recoverable grants are essentially grants that get repaid when and if other capital is raised, the intermediary would need to secure grant capital instead of loan capital as the funding source. Ideally the intermediary would also have the ability to make small feasibility grants early on in the process to enable providers to put together viable applications for capital resources.

¹³ The proportion of the cost that must be subsidized depends on a number of assumptions that would require further exploration with policymakers.

¹⁴ Children with physical disabilities often require additional equipment. Other special needs children may have personal care attendants or therapists who are present in the classroom. These may indicate the need for more generous space planning.

¹⁵ Access to running water and toilets is extremely important to a well-functioning classroom. Without them, teachers often must leave the classroom to accompany children to the bathroom or to prepare for or clean-up after activities. This means that the classroom is left with too few caregivers during these errands. In addition, having accessible bathrooms enables children to use the facilities when they need to, and promotes autonomy.

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¹⁸ Moreover, USDA and revenue bonds permit 100% of the cost to be financed. Conventional lenders typically lend no more than 70 or 80% of the project's value. The cost might even exceed the market value creating a further gap that must be filled with either grants or donations that function as equity or with difficult to secure subordinated debt.

¹⁹ Further research would be needed to determine if any regulatory restrictions exist in the use of supplemental state contract revenue as a USDA loan repayment source and, if there are, to explore ways to structure the state's payments.

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