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DEPARTMENT OF AGRICULTURE

Food and Consumer Service

7 CFR Parts 210 and 226

Child and Adult Care Food Program:

Improved Targeting of Day Care Home Reimbursements

RIN 0584–AC42

AGENCY: Food and Consumer Service, USDA.

ACTION: Final rule.

SUMMARY: This final rule amends the Child and Adult Care Food Program regulations governing reimbursement for meals served in family day care homes by incorporating changes resulting from the Department's review of comments received on a January 7, 1997, interim rule. These changes and clarifications involve: The appropriate use of school and census data for making tier I day care home determinations; documentation requirements for tier I classifications; tier II day care home options for reimbursement, including use of child care vouchers; calculating claiming percentages/blended rates using attendance and enrollment lists; and procedures for verifying household applications of children enrolled in day care homes. This final rule also amends the National School Lunch Program regulations to facilitate tier I day care home determinations by requiring school food authorities to provide elementary school attendance area information to sponsoring organizations. These revisions implement in final form the provisions of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 to target higher CACFP reimbursements to low-income children and providers.

EFFECTIVE DATE: April 27, 1998.

FOR FURTHER INFORMATION CONTACT: Mr. Robert M. Eadie, Policy and Program Development Branch, Child Nutrition Division, Food and Consumer Service, Department of Agriculture, 3101 Park Center Drive, Room 1007, Alexandria, Virginia 22302, or telephone (703) 305–2620.

SUPPLEMENTARY INFORMATION:

Executive Order 12866

This final rule has been determined to be economically significant and was reviewed by the Office of Management and Budget under Executive Order 12866.

Regulatory Flexibility Act

This rule has been reviewed with regard to the requirements of the Regulatory Flexibility Act (5 U.S.C. 601–612). This rule is expected to have a significant impact on a substantial number of small entities. Specifically, it will impact day care homes classified as tier II day care homes. Additional discussion of this impact is contained in the Economic Impact Analysis following this rule.

Executive Order 12372

The Child and Adult Care Food Program (CACFP) and the National School Lunch Program (NSLP) are listed in the Catalog of Federal Domestic Assistance Under No. 10.559 and 10.555, respectively, and are subject to the provisions of Executive Order 12372, which requires intergovernmental consultation with State and local officials (7 CFR part 3015, subpart V, and final rule related notice published at 48 FR 29114, June 24, 1983).

Unfunded Mandate Reform Act

Title II of the Unfunded Mandate Reform Act of 1995 (UMRA), Pub. L. 104–4, establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and the private sector. Under section 202 of UMRA, the Food and Consumer Service generally must prepare a written statement, including a cost-benefit analysis, for proposed and final rules with ''Federal mandates'' that may result in expenditures to State, local, or tribal governments, in the aggregate, or to the private sector, of $100 million or more in any one year. When such a statement is needed for a rule, section 205 of UMRA generally requires the Food and Consumer Service to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, more cost-effective or least burdensome alternative that achieves the objectives of the rule.

This rule contains no Federal mandates (under the regulatory provisions of Title II of UMRA) for State, local, and tribal governments or the private sector of $100 million or more in any one year. Thus, this rule is not subject to the requirements of sections 202 and 205 of UMRA.

Paperwork Reduction Act

This final rule contains information collection requirements which are subject to review by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35). The final rule contains changes to the information collection requirements that were not included in the interim rule. Specifically, the final rule contains changes based on recent day care home participation data and on information contained in a recent study, and a requirement that school food authorities provide, upon request, elementary school attendance area information for schools in which 50 percent or more of enrolled children have been certified eligible for free or reduced price meals. In accordance with section 3507(d) of the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 et seq.) the information collection or recordkeeping requirements included in this final rule have been submitted for approval to OMB. When OMB notifies us of its decision, we will publish a document in the **Federal Register** providing notice of the assigned OMB control number or, if approval is denied, providing notice of what action we plan to take.

Title: Child and Adult Care Food Program: Improved Targeting of Day Care Home Reimbursements.

Description: Under this final rule, some existing recordkeeping activities contained in 7 CFR parts 210 and 226 would be affected. The OMB control numbers are 0584–0006 and 0584–0055, respectively.

Description of Respondents: State agencies, school food authorities and sponsoring organization of family day care homes.

Estimated Annual Recordkeeping Burden: Changes in the annual burden

hours and participation figures from the interim rule are based on recent participation data and information contained in a recent study, Early Childhood and Child Care Study, Profile of Participants in the CACFP: Final Report, Volume 1, prepared in May of 1997. Specifically, adjustments were made in the number of National School Lunch Program State Agencies (SA), the number of sponsoring organizations of family day care homes, and the annual frequency of sponsoring organization's recordkeeping requirements. In addition, an adjustment was made to the projected number of households of tier II children who complete and submit an application. The use of this data results in the deletion of 23,813 reporting hours and the addition of 12,208 recordkeeping burden hours from the burden hours used in the interim rule estimate of burden hours to the Child and Adult Care Food Program.

The final rule also requires that school food authorities provide, when available and upon request by Child and Adult Care Food Program sponsoring organizations, elementary school attendance area information for schools in which 50 percent or more of enrolled children have been certified eligible for free or reduced price meals. This provision was not specifically addressed in the interim rule because the Department assumed that attendance area information would be publicly available to sponsoring organizations. However, given the importance of attendance area information in making tier 1 day care home determinations using school data, and commenter concern regarding the availability of attendance area information, the final rule requires school food authorities to provide this information. The final rule does not require the creation or collection of new data, but rather the provision, upon request, of attendance area information that already exists, thereby imposing a minimal burden. The inclusion of this provision results in the addition of 39,752 reporting burden hours to the burdens for the National School Lunch Program.

Executive Order 12988

This final rule has been reviewed under Executive Order 12988, Civil Justice Reform. This rule is intended to have preemptive effect with respect to any State or local laws, regulations or policies which conflict with its provisions or which would otherwise impede its full implementation. This rule is not intended to have retroactive effect unless so specified in the **EFFECTIVE DATE** section of this preamble. Prior to any judicial challenge to the provisions of this rule or the application of its provisions, all applicable administrative procedures must be exhausted. In the CACFP: (1) Institution appeal procedures are set forth in 7 CFR 226.6(k); and (2) disputes involving procurement by State agencies and institutions must follow administrative appeal procedures to the extent required by 7 CFR 226.22 and 7 CFR part 3015.

This rule implements in final form the amendments set forth under sections 708(e) (1) and (3) of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), Pub. L. 104–193, which was enacted on August 22, 1996. In accordance with section 708(k)(3)(A) of PRWORA, the Department published an interim rule, instead of a proposed rule, on January 7, 1997 (62 FR 889). Due to errors contained in the preamble and regulatory text of the rule published on January 7, 1997, the Department published a correction document on February 6, 1997 (62 FR 5519), and extended the original 90-day comment period to 120 days, through May 7, 1997.

Among other things, this final rule amends § 210.9(b)(20) of the National School Lunch Program regulations to require that school food authorities provide, when available and upon request by CACFP sponsoring organizations, elementary school attendance area information for schools in which 50 percent or more of enrolled children have been determined eligible for free or reduced price meals. This provision was not specifically addressed in the interim rule published on January 7, 1997 (62 FR 889) because the Department assumed that such information would be publicly available to sponsoring organizations. However, a number of sponsoring organizations have expressed concern about their ability to obtain this information. Attendance area information is essential to making tier I day care home determinations using school data, an option specifically required by the PRWORA amendments. In addition, the requirement to provide attendance area information only pertains to those school food authorities in which such information already exists, thereby imposing a minimal burden. For these reasons, the Administrator of the Food and Consumer Service has determined, in accordance with 5 U.S.C. 553(b)(3)(B), that it is impracticable and contrary to the public interest to take prior public comment and that good cause therefore exists for promulgating this provision in the final rule without prior public notice and comment.

In addition, this final rule amends § 226.15(f) to include criteria on the appropriate use of school and census data for making tier I day care home determinations. These criteria place primary emphasis on the use of elementary school free and reduced price enrollment data. The preamble to the interim rule expressed the Department's strong preference for school data over census data, stated several reasons for this preference, and indicated that the Department would subsequently issue guidance for use by sponsoring organizations in making tier I day care home determinations. The Department issued this guidance on March 10, 1997. Because the criteria were not set forth in the interim rule, there was no opportunity for formal public comment. However, sponsoring organizations have made their initial tier I determinations in accordance with the criteria set forth in the March 10 guidance, and in this final rule. For this reason, the Administrator of the Food and Consumer Service has determined, in accordance with 5 U.S.C. 553(b)(3)(B), that it is impracticable and contrary to the public interest to take prior public comment and that good cause therefore exists for promulgating this provision in the final rule without prior public notice and comment.

The final rule is being published based on comments received on the interim rule, in accordance with the requirement contained in section 708(k)(3)(B) of PRWORA. The Department anticipates that it may later propose additional changes to address issues that arise after implementation of the two-tiered reimbursement structure on July 1, 1997.

Background

This rule implements in final form the amendments set forth under sections 708(e) (1) and (3) of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), Public Law 104–193, which was enacted on August 22, 1996. In accordance with section 708(k)(3)(A) of PRWORA, the Department published an interim rule, instead of a proposed rule, on January 7, 1997 (62 FR 889).

In addition to requiring that an interim rule be published by January 1, 1997, section 708(k)(3)(B) of PRWORA also required the Department to publish a final rule on these provisions by July 1, 1997. These extremely short timeframes limited the Department's ability to benefit from public input in the development of the interim or final rule. Thus, although the Department allowed 120 days for public comment on the interim rule, the requirement to

publish a final rule by the date for implementation of the two-tiered system (July 1, 1997) meant that the final rule could not reflect any knowledge gained by the Department, State agencies, or sponsoring organizations in operating the two-tiered system.

The Department recognizes the importance of State and local-level input in developing effective program regulations that carry out the intent of PRWORA while minimizing administrative burden. Therefore, the Department is interested in receiving comments on implementation and operation during the first year of the two-tiered system. Based on the comments received, the Department may develop, at a later date, a proposed rule to implement any needed changes within the statutory framework.

In an effort to improve the targeting of benefits to low-income children, PRWORA establishes a two-tiered system for reimbursing meals served in family day care homes participating in the Child and Adult Care Food Program (CACFP), effective July 1, 1997. Under this system, tier I day care homes are those that are located in low-income areas or those in which the provider's household income is at or below 185 percent of the Federal income poverty guidelines. All meals served to enrolled children in tier I day care homes are reimbursed at essentially the same rates as prior to the two-tiered system, as adjusted for inflation, regardless of the income levels of enrolled children's households. Tier II day care homes are those which do not meet the location or provider income criteria for a tier I day care home. All meals served in tier II day care homes are reimbursed at lower rates, unless the provider elects to have the sponsoring organization identify children from income-eligible households. In that case, meals served to identified income-eligible children are reimbursed at the tier I rates.

The Department received 713 comments on the interim rule published in the **Federal Register** on January 7, 1997. Of these, 21 were from State agencies administering the CACFP or National School Lunch Program (NSLP); 140 from sponsoring organizations of day care homes; 352 from day care home providers; 5 from advocacy groups; 192 from parents and other members of the general public; and 3 from others, including one from a State Representative, one from a public school system, and one from a school administrator's association.

In general, commenters were opposed to the changes made to the CACFP by Public Law 104–193. Of the commenters, 583 specifically expressed concern about the negative impact they anticipate that these provisions will have on child care and, therefore, on children, including: (1) Potentially significant dropout of providers from the CACFP, which could result in an increase in the number of ''underground,'' unlicensed day care homes; (2) a possible increase in day care rates if tier II providers choose to ''pass along'' the effect of lost meal reimbursement to parents in the form of higher day care rates; (3) a potential decrease in the quality of meals served to children in CACFP day care homes, due to the lower reimbursement rates; and (4) an overall decrease in available quality child care at a time when new work requirements resulting from welfare reform necessitate an increased supply. Instead of the two-tiered reimbursement system set forth in PRWORA, 103 commenters suggested that budgetary savings could be achieved by maintaining one set of rates, but by lowering them. Only three commenters expressed support for the two-tiered reimbursement system.

Several of the concerns expressed by commenters were addressed in the economic impact analysis, which was published as an appendix to the interim rule (62 FR 904). Overall, it is expected that non-low-income providers and parents will bear most of the costs resulting from the two-tiered reimbursement system—as was the intent of PRWORA. First, as a result of the two-tiered reimbursement system, the annual rate of growth of the number of day care home providers participating in the CACFP is expected to decline. This anticipated decline in the annual rate of growth is attributed to a combination of decreased incentive for non-low-income providers to join the program, due to the lower reimbursement rates, and an increase in the number of these providers leaving the program. Similarly, the decreased CACFP reimbursements may cause some currently regulated and sponsored homes not only to drop out of the CACFP, but also to consider moving out of licensed care altogether.

As noted by some of the commenters, providers who remain in the program and operate tier II day care homes will most likely respond to their decrease in revenues from the CACFP through some combination of raising child care fees, absorbing the loss, and reducing their operating costs. Though many factors influence a provider's response, including the competitiveness of the child care market in which the provider operates, affected providers (tier II) will probably choose to pass some of their revenue loss on to their clientele, primarily non-low-income parents, through higher child care fees. To cut operating costs, tier II providers may also change their management practices relating to food service and developmental opportunities and materials. Providers may decide that certain snacks under the old, higher CACFP reimbursements will not be served under the new, lower rates, such as an afternoon snack. Providers might also respond by decreasing meal portions, although by specifying minimum serving sizes, CACFP regulations limit the extent to which this could be done. Among other comparisons, the CACFP study mandated by section 708(l)(1)(E) of PRWORA will compare the nutritional quality of meals served in post-tiering tier II day care homes with the quality of meals served in those day care homes before tiering.

The comments received on the provisions of the interim rule, and the Department's response to them, are discussed in greater detail in the preamble that follows. Although the Department carefully considered all of the comments received, many of the changes recommended by commenters are not feasible under the language of PRWORA. Any provisions that are not discussed in the preamble to this final rule were not addressed by commenters, and are retained as set forth in the interim rule. However, in several cases, the preamble addresses provisions on which the Department received no comments, in order to bring to readers' attention certain significant provisions of PRWORA and the interim rule.

Tier I Day Care Homes

Definition

The interim rule, in § 226.2, defined a ''tier I day care home'' as:

(a) A day care home that is operated by a provider whose household meets the income standards for free or reduced-price meals, as determined by the sponsoring organization based on a completed free and reduced price application, and whose income is verified by the sponsoring organization of the home in accordance with § 226.23(h)(6);

(b) A day care home that is located in an area served by a school enrolling elementary students in which at least 50 percent of the total number of children enrolled are certified eligible to receive free or reduced price meals; or

(c) A day care home that is located in a geographic area, as defined by FCS based on census data, in which at least 50 percent of the children residing in the area are members of households which meet the income standards for free or reduced price meals.

The definition promulgated in the interim rule was based on the definition

of ''tier I family or group day care home'' contained in section 17(f)(3)(A)(ii)(I) of the National School Lunch Act (NSLA), as amended by section 708(e)(1) of Public Law 104–193.

No comments were received on the definition of ''tier I day care home'' as added by § 226.2 of the interim rule. Therefore, this final rule retains the definition of ''tier I day care home'' as set forth in the interim rule.

Provision of Area Data

Unless a provider demonstrates that household income meets the free or reduced price eligibility standards, a sponsoring organization must use elementary school or census data—referred to collectively in this preamble as ''area data''—to qualify the day care home as a tier I day care home. Section 708(e)(3) of PRWORA amended section 17(f)(3) of the NSLA to set forth requirements pertaining to the provision of area data for use in making tier I day care home determinations.

School Data

Based on the provisions of PRWORA, the interim rule added § 210.9(b)(20) to the NSLP regulations to require that school food authorities provide (by March 1, 1997, and by December 31 each year thereafter) the State agency that administers the NSLP with a list of all elementary schools under their jurisdiction in which 50 percent or more of enrolled children have been determined eligible for free or reduced price meals as of the last operating day of October. Similarly, § 210.19(f) as added by the interim rule requires each State agency that administers the NSLP to provide (by March 15, 1997, and by February 1 each year thereafter) the State agency that administers the CACFP with a list of all elementary schools in the State in which 50 percent or more of enrolled children have been determined eligible for free or reduced price meals. Section 210.19(f) also requires the State agency that administers the NSLP to provide the list to any sponsoring organization that requests it. In addition, § 226.6(f) as amended by the interim rule requires the State agency that administers the CACFP to provide its sponsoring organizations with this list of elementary schools by April 1, 1997, and by February 15 each year thereafter.

The Department received 64 comments concerning the provision of elementary school free and reduced price enrollment data for the CACFP. Of these, five commenters objected to the requirements because they believe that they place an unnecessary burden on school food authorities and/or NSLP State agencies. For example, two commenters pointed out that this requirement is unrelated to the administration of the NSLP. The Department agrees that provision of these data is not directly related to administration of the NSLP, and is cognizant of the modest administrative burden it may place on State and local entities. Nevertheless, section 17(f)(3)(E)(ii) of the NSLA, as amended by section 708(e)(3) of PRWORA, explicitly requires that NSLP State agencies annually provide this data in order to facilitate tier I day care home classifications in the CACFP. Despite commenters who indicated that this is a new reporting burden, § 210.8(c) of the NSLP regulations previously required that school food authorities report the total number of enrolled free, reduced price, and paid children to the NSLP State agency on the October claim for reimbursement. In order to submit this data, school food authorities must already consolidate the enrollment data submitted by individual schools. In addition, while there was no prior Federal requirement that school food authorities report the names of participating schools to the State agency, many States already collected this information. Finally, although PRWORA required NSLP State agencies to provide the list directly to sponsoring organizations upon request, the interim rule requires that NSLP State agencies also provide it to CACFP State agencies, which will provide it to all sponsoring organizations. We expect that this requirement will reduce the number of requests received by NSLP State agencies from sponsoring organizations, thereby further minimizing the burden associated with this provision. Finally, the burden is also minimized due to the fact that more than three-fourths of States operate the CACFP out of the same State agency as the NSLP.

In addition, two commenters recommended that the annual February 15 date by which the CACFP State agency must provide the list of schools to sponsoring organizations be changed to April 1 or April 15, in order to provide the CACFP State agency additional time to assemble the data and distribute it to sponsoring organizations. While the interim rule requires that the CACFP State agency provide the school data to sponsoring organizations by February 15, which is only two weeks after its receipt from the NSLP State agency, the form in which the data is received from the NSLP State agency should not require any work by the CACFP State agency beyond duplicating and mailing the data to sponsoring organizations. In the Department's opinion, two weeks is sufficient time to perform this task. Furthermore, it is critical that the data be provided in as timely a manner as possible after receipt by the CACFP State agency, so that sponsoring organizations are able to make their tiering determinations with current information.

Therefore, this final rule makes no change to §§ 210.9(b)(20) and 210.19(f) regarding the requirement that school food authorities and NSLP State agencies, respectively, provide free and reduced price enrollment data for use by CACFP sponsoring organizations. In addition, no change is being made to the February 15 annual date by which the CACFP State agency must provide sponsoring organizations with the school data, contained in § 226.6(f)(9).

Sixteen commenters on the interim rule indicated that the free and reduced price enrollment data used in the CACFP should be based on a month other than October. These commenters expressed concerns that requiring October data will impose a new reporting burden on school food authorities and NSLP State agencies, and that data from another month would be more reflective of schools' free and reduced price enrollment. With regard to whether data from another month would more accurately reflect the free and reduced price enrollment of schools, five commenters recommended specific months that should be used instead of October, including January, March, May and June. Four commenters recommended that each NSLP State agency decide on the appropriate month for provision of data. In addition, 12 commenters questioned whether sponsoring organizations could themselves obtain updates of free and reduced price enrollment data from school food authorities or individual schools more frequently than annually, and one commenter recommended that NSLP State agencies provide updated data to sponsoring organizations on a monthly basis. Finally, 185 commenters expressed concern about the accuracy of the school data provided.

The Department continues to believe that October data accurately reflects the free and reduced price enrollment of schools, and also imposes the least burden on school food authorities. Nevertheless, in response to commenter concerns, this final rule permits NSLP State agencies to establish the list of schools on free and reduced price data on data from a month other than October.

At a minimum, PRWORA and the interim rule require that free and reduced price enrollment data be

provided to sponsoring organizations on an annual basis. In the interests of minimizing any burden associated with provision of this data, and the potential for administrative confusion which could result from monthly fluctuations in the data, this final rule does not require that data be provided more frequently than annually, and permits State agencies to update the list of schools more frequently only under unusual circumstances.

The circumstances under which State agencies may update the list help address commenters' concerns regarding the accuracy of the data provided. If, for example, free and reduced price data for a newly opened school becomes available after the list has already been provided, it would be logical for the NSLP State agency to provide to the CACFP State agency and requesting sponsoring organizations the new data for this particular school, and any other schools affected by its opening. Similarly if, after the list of schools is provided, it is discovered that data provided by a particular school food authority is several years old, the NSLP State agency should provide new data on those schools. However, this means that routine monthly fluctuations in a school's free and reduced price data may not be used to qualify or disqualify a home from tier I status after its initial determination of eligibility has been made. Although PRWORA and the interim rule explicitly allow a State agency to change a tier I determination if information becomes available indicating that a home is no longer in a qualified area, this should be done only when there has been a substantial, sustained shift in an area's socioeconomic makeup, not when there are minor fluctuations in a school's free and reduced price enrollment from one month to the next. In order to ensure that all sponsoring organizations (whose service areas often overlap) have equal access to any updated information, and to help ensure the integrity of the data provided, sponsoring organizations will not be permitted to use free and reduced price information obtained directly from local school food authorities without the express prior consent of the State agency administering the CACFP. Sponsoring organizations that become aware of particular circumstances that they believe would warrant the issuance of new data should notify the CACFP State agency, which can communicate with the NSLP State agency as necessary.

Accordingly, this final rule amends §§ 210.9(b)(20) and 210.19(f) to permit NSLP State agencies to base the list of free and reduced price schools for the CACFP on data as of the last operating day of the preceding October, or another month specified by the NSLP State agency. In order to accommodate NSLP State agencies which select a month other than October, § 210.9(b)(20) is also amended by adding language to clarify that school food authorities must annually provide the list of schools to the NSLP State agency by December 31, or, if data is based on a month other than October, within 60 calendar days following the end of the selected month. Similarly, § 210.19(f) is amended by adding language that NSLP State agencies must annually provide the list of schools to the CACFP State agency by February 1, or within 90 calendar days following the end of the month designated by the NSLP State agency if data is based on a month other than October. In addition, § 226.6(f)(9) is amended to clarify that the CACFP State agency must annually provide the list of schools to sponsoring organizations by February 15, or within 15 calendar days of receipt of the list from the NSLP State agency if data is based on a month other than October. Section 210.19(f) is further amended in this final rule to permit NSLP State agencies to provide updated free and reduced price enrollment data on individual schools, but only when unusual circumstances render the initial data obsolete.

In addition, the Department received 272 comments which expressed concern about the availability or accessibility of elementary school attendance area information, which is necessary for sponsoring organizations to obtain in order to be able to use the free and reduced price enrollment data.

First, many commenters suggested methods of classifying tier I day care homes which would greatly reduce, or even eliminate the need for attendance area information. For example, 38 commenters suggested that State agencies be given the authority to qualify larger geographic areas, such as cities or school districts, as tier I areas, thus eliminating the need for individual elementary school attendance area information for those areas. Similarly, six commenters suggested using data from the elementary school geographically closest to the provider, instead of data from the school serving the provider. Finally, 15 commenters recommended that sponsoring organizations be permitted to accept a provider's self-declaration of the elementary school serving the day care home as sufficient proof of the home's location in the school attendance area. Several of these commenters also recommended that sponsors be required to verify provider self-declarations through obtaining elementary school attendance information for a sample of their providers.

Although the Department appreciates commenters' suggestions and recognizes that they potentially would reduce the burden of obtaining attendance area information, none of the suggested alternatives is permissible under the provisions of PRWORA. Due to the definition contained in section 17(f)(3)(A)(ii)(I) of the NSLA, as added by section 708(e)(1) of PRWORA, which describes a ''tier I day care home'' in part as a day care home ''served by a school enrolling elementary students,'' it would be contrary to the law to permit larger geographic areas to qualify as tier I areas, or to use data from the elementary school geographically closest to a provider's home. In addition, as discussed in a memorandum issued on April 25, 1997, a sponsor may not rely on a provider's self-declaration of elementary school attendance area for making a tier I determination. To comply with the law and the interim rule, a sponsor must independently substantiate and document any attendance area information obtained from its providers. (Additional discussion of provider self-declaration of elementary school attendance areas may be found later in this preamble under ''Documentation Requirements.'')

In addition, 62 of the commenters indicated that obtaining elementary school attendance area information for schools with a free and reduced price enrollment of 50 percent or more is burdensome and difficult for sponsoring organizations. Another of the concerns, expressed by nine commenters, was that school districts will not release attendance area information to sponsoring organizations due to concerns about liability for erroneous tier I classifications made using school data. In addition, 11 commenters indicated that there is no attendance area information available for some school districts, and 50 commenters indicated a concern that sponsoring organizations will have difficulty keeping up with school boundaries because they change frequently. Finally, 42 commenters suggested that NSLP State agencies be required to provide attendance area information, either directly to sponsoring organizations or through the CACFP State agency, along with the list of elementary schools in which 50 percent or more of enrolled children are determined eligible for free or reduced price meals. Many of these commenters indicated that NSLP State agency provision of attendance area information would eliminate

duplication of effort by sponsoring organizations, and ensure that the information obtained and used by sponsors is consistent.

When the interim rule was drafted, it was assumed that attendance area information would be publicly available to sponsoring organizations. In response to concerns expressed on this issue after publication of the interim rule, the Department issued a memorandum on February 10, 1997, in which NSLP State agencies were asked to urge their local school food authorities to make attendance area information available to sponsoring organizations upon their request.

Requiring NSLP State agencies to collect attendance area information from all elementary schools in the State with 50 percent or more of enrolled children identified as eligible for free or reduced price meals would, in most cases, place a substantial burden on NSLP State agencies. In addition, the Department believes it is unnecessary to impose an additional information collection requirement on NSLP State agencies when the information that sponsoring organizations need to make tier I day care home determinations is usually maintained by the local school district, and not by the NSLP State agency. Although NSLP State agencies are required by PRWORA and the interim rule to collect data from school food authorities regarding schools with 50 percent or more free and reduced price enrollees, attendance area information for individual schools is significantly more complex and varied.

However, given the significant commenter concern regarding the availability of attendance area information, this final rule requires school food authorities to provide elementary school attendance area information, when it is available for the schools under their jurisdiction, upon request by sponsoring organizations. We are requiring that the information be provided ''when it is available'' in recognition of the fact that not all school districts have distinct attendance areas attached to each of their elementary schools. The Department wishes to emphasize that it does not intend for school food authorities to create new information, but rather to provide sponsoring organizations only with attendance area information that already exists.

With regard to commenter concerns about a school district's liability if erroneous tier I day care home classifications are made based on school data, school districts should be assured, as previously indicated in our February 10, 1997, memorandum, that they will not be held financially or otherwise liable by FCS for erroneous tier I classifications, whether due to a sponsoring organization's misuse of attendance area information, or due to an inadvertent error by the school district when providing the information. Conversely, sponsoring organizations will not be liable for erroneous information obtained from school food authorities as long as the sponsoring organization takes action to correct misclassifications made with erroneous school data as soon as it learns of the errors.

As indicated above, many commenters expressed concern that sponsoring organizations will have difficulty maintaining up-to-date boundary information because boundaries for some schools change frequently. The Department recognizes that changes to a school's boundaries made during a school year may not be immediately known by the sponsor. However, the Department expects sponsoring organizations to make reasonable efforts to use current boundary information when making tier I determinations with school data. Therefore, this final rule requires that sponsoring organizations obtain current attendance area information at a minimum on an annual basis, for use in classifying new day care homes that enter the program. However, as discussed above with regard to changes in a school's percentage of free and reduced price enrollment from year to year, the Department does not expect sponsoring organizations to routinely reclassify tier I day care homes before the three-year period has expired based on shifts in an elementary school's boundaries.

Accordingly, this final rule amends § 210.9(b)(20) by adding the requirement that school food authorities provide elementary school attendance area information, upon request by sponsoring organizations, when it is available for the schools under their jurisdiction. In addition, § 226.15(f) is amended by adding the requirement that when making tier I day care home determinations based on school data, sponsoring organizations shall use attendance area information that has been obtained, or verified with appropriate school officials to be current, within the last school year.

Census Data

Section 708(e)(3) of PRWORA amended section 17(f)(3)(E)(i) of the NSLA to require that the Secretary provide each CACFP State agency with appropriate census data showing the areas of the State in which at least 50 percent of children are from households meeting the income standards for free or reduced price meals. In addition, § 226.6(f)(9) as amended by the interim rule requires CACFP State agencies to make the census data available to sponsoring organizations.

A special tabulation of data showing, for each census block group in the country, the percentage of children age 0–18 who are from households meeting the income standards for free or reduced price meals has been used for determining area eligibility for the Summer Food Service Program (SFSP) since 1994. By January 1997, the Department had provided this special tabulation to all CACFP State agencies that do not also administer the SFSP. In addition, since the CACFP defines a child as age 12 and under, a special tabulation of census data for children ages 0–12 was provided to all CACFP State agencies in March 1997. Because the 0–12 tabulation was not initially made available to State agencies, they were instructed that they could permit sponsoring organizations to use either of the special tabulations for determining tier I day care home eligibility for the purposes of implementation. However, after September 30, 1997, all sponsoring organizations must use the special tabulation of census data for children ages 0–12 since that data corresponds with the definition of ''child'' in the CACFP.

No comments were received concerning the provision of census data. Therefore, this final rule retains the requirement contained in § 226.6(f) as added by the interim rule that State agencies provide sponsoring organizations census data.

Making Tier I Day Care Home Determinations

By requiring that school and census data ultimately be provided to sponsoring organizations, PRWORA places the responsibility for determining which day care homes are eligible as tier I day care homes on sponsoring organizations. This is accomplished by applying the school or census data provided by the CACFP State agency, or by determining and verifying that the households of day care home providers are eligible for free or reduced price meals.

Appropriate Use of Area Data

With regard to using area data for making tier I day care home determinations, the preamble to the interim rule expressed the Department's strong preference that sponsoring organizations use elementary school free and reduced price eligibility data over

census data in making tier I day care home determinations. The preamble also stated several reasons for this preference, and indicated that the Department would issue subsequent guidance for use by sponsoring organizations in making tier I day care home determinations.

The Department issued guidance on the use of elementary school and census data for making tier I day care home determinations in the form of a March 10, 1997, memorandum, well in advance of the April 1, 1997, regulatory deadline at § 226.6(f)(2) for sponsors' submission of management plan amendments which detailed their system for making tier I determinations. That guidance indicated that, because it is typically more recent and more representative of a given area's current socioeconomic status, school data must be consulted first when using area data to try to qualify a day care home as a tier I day care home. The only exceptions to this rule are in cases in which busing, or other ''district-wide'' bases of attendance, such as magnet or charter schools, result in school data not being representative of an attendance area, or when attendance areas are not used by the school district. In these cases, census data should generally be consulted by sponsoring organizations instead of school data.

In addition, the guidance indicated that if, after reasonable efforts are made, a sponsoring organization is unable to obtain local elementary school attendance area information, as discussed above, the sponsor may use census data to determine a day care home's eligibility as a tier I day care home. The Department did not attempt to define ''reasonable efforts,'' but rather provided discretion to State agencies to provide additional guidance in this area to sponsoring organizations.

Finally, the guidance delineated circumstances in which sponsoring organizations may consult census data after having consulted school data which fails to support a tier I determination. These circumstances were: (1) Rural areas with geographically large elementary school attendance areas; or (2) other areas in which an elementary school's free and reduced price enrollment is above 40 percent. This approach enables sponsoring organizations to identify ''pockets of poverty'' with higher concentrations of low-income children which are not evident when only consulting the list of schools with 50 percent or more of enrolled children determined eligible for free or reduced price meals. The March 10 guidance pointed out, however, that NSLP State agencies were only required by § 210.19(f), as amended by the interim rule, to provide a list of elementary schools in the State in which at least 50 percent of enrolled children are determined eligible for free or reduced price meals.

The Department received 166 comments on the appropriate use of school and census data, all of which indicated that there should be no restrictions on the use of school or census data for making tier I day care home determinations. Thirty-one of these commenters indicated their belief that PRWORA does not indicate a preference for one data source over another. Forty commenters indicated that the Department's policy restricting the use of census data to specific circumstances was contrary to what they believed to be PRWORA's intent to serve the maximum number of low-income children. Eleven commenters objected to the Department's position that school data should not generally be used in cases with significant student busing or other district-wide bases of attendance, such as magnet schools. Two commenters indicated that CACFP policy should not be based on comparisons to the SFSP because the programs are very different.

The Department prefers school data over census data because, in most cases, school data is more capable of accurately documenting an area's current socioeconomic status. Thus, placing primary reliance on school data for making tier I day care home determinations on the basis of area data is necessary to achieve the targeting goals of PRWORA. In addition, section 17(f)(3)(E)(ii)(II) of the NSLA, as amended by section 708(e)(3) of PRWORA, requires that in determining ''whether a home qualifies as a tier I family or group day care home under subparagraph (A)(ii)(I),'' State agencies and sponsoring organizations ''shall use the most current available data at the time of the determination.'' Subparagraph (A)(ii)(I) of section 17(f)(3) of the NSLA encompasses all of the methods (i.e., elementary school data, census data, and provider's household income) for making tier I determinations. In most instances, free and reduced price applications are collected annually by elementary schools. Therefore, these data are a far more recent statement of individual and aggregate economic circumstances than census data, which was collected in 1990.

One hundred twenty-two commenters expressed concern that elementary school free and reduced price data does not necessarily accurately reflect an area's economic circumstances. These commenters cited several reasons, including that many low-income families choose not to apply for school meal benefits, and therefore, are not included in the school data. Although it is true that not all eligible households submit free and reduced price school meal applications on behalf of their school-age children, studies such as the National Evaluation of School Nutrition Programs (Abt Associates, 1983) have demonstrated that low-income households are more likely to apply on behalf of their elementary-age children than low-income households with older children. In addition, the special tabulation of census block group data is based on data submitted by a sample drawn from one out of every six American households. As such, it provides an excellent basis for generalizing about poverty at the national, State, and county levels. However, the average census block group includes approximately 400 housing units containing about 900 persons, and the one in six income sample is drawn randomly from all census block groups, not equally from within each block group. As a result, there is no way of predicting how many households within a particular block group completed and returned the household income questionnaire to the Bureau of the Census. The average number of households in a block group with school-age children which returned the questionnaire is unlikely to be greater than the average number of households with children enrolled in the local elementary school. Thus, census data for a particular block group is typically less accurate than school data.

Despite the shortcomings of census data, the Department believes that its inclusion in the law as a potential source for documenting a day care home's eligibility as a tier I day care home was purposeful and logical. There are, as noted above, certain circumstances in which school data does not more accurately portray the surrounding area's socioeconomic status than census data. In addition, if an area's socioeconomic makeup has not changed substantially since the census data were collected in 1990, there may also be other circumstances, such as rural and urban ''pockets of poverty,'' in which census block group data can appropriately identify an eligible portion of an otherwise ineligible elementary school attendance area.

With regard to commenter objections to the Department's position that school data should not generally be used in cases with significant student busing or

other district-wide bases of attendance, the Department would like to reiterate that it promulgated this policy because in cases with district-wide bases of attendance, the school data does not necessarily reflect the household income levels of a particular geographic area. However, the March 10 guidance was not intended to require that, whenever busing occurred, census data would have to be used. Pupil busing might be used for a small portion of the student population and might not affect the elementary school data's ability to accurately portray an area's household income levels. Rather, the guidance was intended to underscore the Department's strong belief that Congress intended sponsoring organizations to utilize area data which best portrays the current household income levels of the area in which a particular day care home is located. Each community's situation may be potentially unique, and the State agency is in the best position to determine when busing or other circumstances have diminished the school data's ability to accurately portray an area's current household income levels. In addition, although the two programs are different in many operational respects, the Department believes that basing the CACFP policy on that for the SFSP is warranted in this situation due to the programs' similarities in establishing eligibility based on geographic areas.

Therefore, despite the concerns expressed by commenters, the Department continues to believe that school data is preferable to census data in the majority of cases, and that the policy set forth in the March 10 memorandum is consistent with the intent of Pub. L. 104–193 to utilize the best available data on aggregate socioeconomic conditions in order to better target CACFP benefits to low-income areas. Therefore, this final rule incorporates the criteria on the appropriate use of school and census data for making tier I day care home determinations set forth in the March 10, 1997, memorandum.

When making tiering determinations based on area data, sponsoring organizations are expected to make reasonable efforts to ensure that day care homes located within the geographic limits of an eligible school attendance area or census block group are classified as tier I homes only when appropriate. That is, if a sponsoring organization believes that a segment of an otherwise eligible elementary school attendance area is non-needy, the sponsoring organization must take additional steps to ensure that homes within the attendance area have been appropriately classified. For example, although sponsors should consult school data first in most circumstances, it is possible that some socioeconomically diverse school attendance areas which meet the 50 percent threshold might include substantial segments which are well above the criteria for free or reduced price meals. In such cases, in accordance with the law's intent to target higher meal reimbursements to low-income children and providers, it would be necessary for the sponsor to consult census data as well as to determine which part of the elementary school attendance area should be classified as tier I. If a review of the census block group data confirms the sponsoring organization's belief that a segment of an otherwise eligible school attendance area is, in fact, above the criteria for free or reduced price meals, the sponsoring organization must reclassify the homes in that area as tier II day care homes, unless the individual providers can document tier I eligibility on the basis of their household income.

Finally, in order to comply with the March 10 memorandum, 12 commenters requested that NSLP State agencies be required to provide free and reduced price enrollment data on all elementary schools in the State, or at least for all schools with 40 percent or more free or reduced price enrollment, instead of the currently required 50 percent. The Department will not impose a requirement on NSLP State agencies beyond the explicit requirement in section 708(e)(3) of PRWORA that they annually provide a list of elementary schools with 50 percent or more free or reduced price enrollment. However, as indicated in guidance issued by the Department on May 16, 1997, the CACFP State agency can request that the NSLP State agency provide data for schools with between 40 and 49 percent free and reduced price enrollment, or even data for all elementary schools in the State. In fact, we are aware that several NSLP State agencies have already provided the additional data. However, sponsoring organizations which do not have access to data for schools below 50 percent may consult census data to attempt to qualify day care homes located in identifiable ''pockets of poverty'' as tier I day care homes. There may also be some limited circumstances in which using census data is appropriate to identify ''pockets of poverty'' even when elementary school free and reduced price enrollment is below 40 percent. In both of these circumstances, however, sponsors must first receive State agency approval to ensure that determinations are made using the data, whether school or census, that is most reflective of an area's current household income levels.

Accordingly, this final rule amends § 226.15(f) to include the above-described criteria on the appropriate use of school and census data for making tier I day care home determinations.

Verification of Providers' Household Income

The definition of ''tier I day care home'' contained in section 17(f)(3)(A)(ii)(I) of the NSLA, as amended by section 708(e)(1) of Public Law 104–193, and as added to § 226.2 by the interim rule, requires that a day care home that qualifies as a tier I day care home on the basis of the provider's household income must have this income verified by the sponsoring organization. Therefore, the interim rule added to § 226.23(h)(6) the requirement that sponsoring organizations conduct verification of the provider's household income, for all day care homes that qualify as tier I day care homes on this basis, prior to approving the home as a tier I day care home. This verification must be performed in accordance with the verification performed for ''pricing programs'' in § 226.23(h)(2)(i), and consists of verifying the income information provided on the application by collecting documentation from the household, such as pay stubs or income tax statements.

The Department received 115 comments on the verification requirements for tier I day care homes. Of these, 71 commenters specifically objected to the verification requirements for tier I day care homes because they believe that the requirements are too burdensome. The Department received 44 comments which suggested that verification be conducted on a sample of applications, as currently required in the NSLP, instead of on all applications. Several of these commenters recommended that the sample consist of 3 percent of all applications; one commenter suggested a 50 percent sample. Three commenters supported more stringent verification than that required in the interim rule; for example, one commenter wanted pricing verification conducted on the applications of households of children enrolled in tier II day care homes. Finally, 17 commenters questioned how to perform the verification, or requested additional guidance, because sponsoring organizations of day care homes are unfamiliar with this type of verification. Seven commenters made recommendations concerning verification procedures.

The Department recognizes that verification of all applications for providers whose homes qualify as tier I homes on the basis of their household income places an additional administrative burden on sponsoring organizations. However, given the significant financial benefit associated with classification of a day care home as a tier I day care home, in the form of tier I reimbursements for meals served to all children enrolled in the home, Congress determined that it was necessary to impose these requirements to ensure that day care homes that are classified as tier I homes on the basis of household income are truly low-income, despite their location in an area which would not qualify them for tier I status. Thus, the explicit language of section 17(f)(3)(A)(ii)(I), as added by section 708(e)(1) of PRWORA, which defines a ''tier I day care home'' as one which is operated by a ''provider whose household meets the income eligibility guidelines . . . and whose income is verified by the sponsoring organization of the home,'' requires that *all* day care homes qualifying as tier I day care homes on the basis of the provider's household income have income verified prior to participation as a tier I home. Conducting verification on only a sample of the applications, as recommended by commenters, would not meet the requirements of PRWORA. In addition, income verification is an important control for ensuring accurate tiering determinations.

In response to concerns expressed by sponsoring organizations and State agencies about how to perform the required verification for providers whose day care homes qualify as tier I homes on the basis of household income, the Department issued verification guidance for day care homes on May 14, 1997. This guidance was based on the verification guidance issued for the School Nutrition Programs, which is also used by CACFP day care centers.

Therefore, this final rule makes no changes to the requirements for verification of the income information for providers qualifying as tier I day care homes on the basis of their household income contained in the definition of ''tier I day care home,'' and in § 226.23(h)(6) as added by the interim rule.

Misclassification of Tier I Day Care Homes

Based on the fact that there is a significant financial benefit associated with the classification of a day care home as a tier I day care home, § 226.14(a) as amended by the interim rule requires State agencies to assess overclaims against sponsoring organizations which misclassify day care homes as tier I day care homes, unless the misclassification is determined to be inadvertent under guidance issued by FCS.

The Department received 66 comments on assessing overclaims for misclassification of day care homes. Of these, 16 commenters requested that the first six months or one year of implementation be considered a ''grace period'' during which overclaims for misclassification are not assessed against sponsoring organizations except in cases of fraud. Twenty-four commenters suggested that the amount under which an overclaim can be ''disregarded'' in the CACFP, which is currently $100, be increased. Several of these commenters recommended that the disregard amount be based on a percentage of the sponsor's administrative budget. In addition, 12 commenters requested clarification or expressed concern that sponsoring organizations should not be assessed overclaims for reclassifications made by the State agency, in accordance with § 226.6(f)(9) as amended by the interim rule, based on information to which the sponsor could not reasonably have had access prior to the reclassification by the State agency. Finally, nine commenters requested guidance on how the Department will define ''inadvertent'' errors.

In accordance with the preamble to the interim rule, the Department issued guidance on assessing overclaims for improper tier I day care home classifications on August 6, 1997.

With regard to commenters' concerns that overclaims not be assessed for reclassifications made by the State agency based on information to which the sponsor could not reasonably have had access prior to the reclassification by the State agency, the Department wishes to stress that assessing an overclaim in such a situation would not be in accordance with the regulation or the August 6, 1997, guidance. In these situations, the sponsoring organization would be directed by the State agency to correct a home's determination, but an overclaim for the previous classification would likely not be appropriate.

In addition, this rule does not authorize a ''grace period'' during which State agencies would not have to assess overclaims against sponsors except in cases of fraud. This regulation and the guidance provided in support of this regulation do not require the establishment of a claim when the misclassification is inadvertent. The Department does not intend for State agencies to assess overclaims for every tiering misclassification made by sponsors. As the guidance emphasizes, State agencies need not assess overclaims for occasional or inadvertent errors, but rather for widespread or recurring misclassifications, or a systemic problem that may indicate improper management by the sponsor. Finally, any change to the disregard amount must first be considered in a proposed rule. Thus, the Department cannot implement commenters' recommendations that the current disregard amount in the regulations at § 226.8(e) be changed in this final rule, but will monitor the impact of the two-tiered reimbursement structure on administrative payments and, if warranted, may include a change in a future proposed rulemaking.

Therefore, this final rule makes no changes to the language in § 226.14(a) as amended by the interim rule.

Length of Determinations

Based on section 17(f)(3)(E)(iii) of the NSLA, as amended by section 708(e)(3) of PRWORA, § 226.6(f)(9) as amended by the interim rule requires that determinations of a day care home's eligibility as a tier I day care home be valid for three years if based on school data, or until more recent data are available if based on census data. In addition, § 226.6(f)(9) indicates that a sponsoring organization, the State agency, or FCS may change the determination if information becomes available indicating that a home is no longer in a qualified area.

The Department received 17 comments on the length of tier I determinations. Of these, 12 commenters requested that the Department clarify that State agencies should not routinely require annual redeterminations of tiering status. In contrast, three commenters supported annual redeterminations. Finally, several commenters indicated that sponsors must have access to any information used by State agencies to reclassify a home's status.

The Department agrees with commenters who indicated that redeterminations of a day care home's eligibility as a tier I day care home based on school area data should not routinely occur on an annual basis. Guidance issued by the Department on March 12, 1997, clarified that the State agency should not require that redeterminations be made more frequently than the standards set forth in the law (i.e., three years if based on school data, and until more recent data are available if based on census data)

except in situations in which there is substantial, sustained socioeconomic change, not minor fluctuations in school data.

Accordingly, in response to commenter concern, this final rule amends § 226.6(f)(9) and 226.15(f) to clarify that State agencies should not routinely require annual redeterminations of the tiering status of day care homes based on updated elementary school data.

Documentation Requirements

As discussed above, PRWORA and the interim rule clearly place the responsibility for making tiering determinations on the sponsoring organization. The interim rule amended § 226.15(e)(3) to require sponsoring organizations to collect and maintain documentation sufficient to support their tier I determinations.

The Department received 15 comments on the documentation requirements contained in the interim rule. Specifically, these commenters supported permitting State agencies and/or sponsoring organizations to accept a provider's self-declaration of the elementary school serving the day care home as sufficient documentation of the provider's residence in a particular elementary school attendance area.

In addition to the requirements discussed above, the interim rule amended § 226.6(f)(2) to require each sponsoring organization to submit an amendment to its management plan by April 1, 1997, describing its system for making tier I day care home classifications, subject to review and approval by the State agency. Further, sponsoring organizations are ultimately liable for classifications which are not supported with proper documentation. State agencies must evaluate the documentation used by sponsoring organizations to classify day care homes as tier I homes as part of the review required by § 226.6(l). Finally, § 226.14(a) requires State agencies to assess overclaims against sponsoring organizations for improper classifications, unless the misclassification is determined to be inadvertent under guidance issued by the Department.

As stated in guidance issued by the Department on April 25, 1997, a sponsoring organization's system of classifying a day care home as a tier I home on the basis of elementary school data may involve a sponsoring organization requesting that each provider identify the elementary school serving the home. However, for the purpose of making a tier I determination, a sponsoring organization may not rely on a provider's self-declaration that it is located within a particular elementary school's attendance area. To comply with PRWORA and the regulations, a sponsor must independently substantiate and document attendance area information obtained from its providers with official source documentation. Most commonly, sponsors would obtain an official school-boundary identifying map, match provider addresses to the map's boundaries, and retain the map as documentation. If such maps were unavailable, the sponsor might instead contact school officials to verify the attendance area of the schools serving its providers and document the results of this contact, either with a letter from school officials to the sponsor, or with a memorandum to the files detailing the information provided by school officials and the name of the official(s) consulted.

These documentation requirements are necessary in order to ensure that tier I classifications are being made in accordance with PRWORA, and to ensure that sponsoring organizations, and not the individual providers, are making tiering determinations, as required by PRWORA. This is especially important given the significant financial benefit to a provider associated with classifying a day care home as a tier I home.

Accordingly, in order to further clarify the documentation requirements for tier I day care home determinations, this final rule amends § 226.15(e)(3) to indicate that sponsoring organizations must document tier I determinations based on school data with official source documentation obtained from the school, as discussed above.

Tier II Day Care Homes

Definition

Section 226.2 as amended by the interim rule defines a ''tier II day care home'' as a day care home that does not meet the criteria for a tier I day care home. This definition is based on language contained in section 17(f)(3)(A)(iii) of the NSLA, as amended by § 708(e)(1) of PRWORA.

No comments were received on the definition of ''tier II day care home'' as added by § 226.2 of the interim rule. Therefore, this final rule retains the definition of ''tier II day care home'' as added by the interim rule.

Election by Providers

In contrast to tier I day care homes, in which all meals served are reimbursed at the same rates (tier I), meals served in tier II day care homes may be eligible for two levels of reimbursement—the tier I rates for meals served to identified income-eligible children, and tier II rates, which are lower, for meals served to all other children.

Sections 17(f)(3)(A)(iii) (II) and (III) of the NSLA, as amended by PRWORA, clearly give day care home providers, and not their sponsoring organizations, the authority to elect whether income-eligible children are identified by the sponsoring organization. The interim rule amended sections 226.6(f)(2) and 226.18(b)(11) to require that sponsoring organizations inform providers of day care homes classified as tier II day care homes of the options available to them under PRWORA with regard to whether income-eligible children are identified or not. The approach that providers select determines if, and how, sponsors are to establish the eligibility of children enrolled in tier II day care homes.

After publication of the interim rule, the Department received several questions concerning the reimbursement approaches available to tier II day care homes. In response to these questions, the Department issued a memorandum on June 2, 1997, to clarify these provisions and to resolve any confusion on this issue created by the interim rule. The following explanation restates the information contained in the June 2, 1997, memorandum.

Under the first approach set forth in PRWORA and discussed in the interim rule, a day care home provider may elect to have its sponsoring organization attempt to identify all income-eligible children enrolled in the day care home. In that case, for all meals served to enrolled children who are determined by the sponsoring organization to meet the criteria for free or reduced price meals (i.e., they are from households with incomes at or below 185 percent of the Federal income poverty guidelines), the home receives the tier I rates of reimbursement. Meals served to all other enrolled children are reimbursed at the tier II rates of reimbursement, which are lower.

If a provider selects this first approach, the sponsoring organization may establish the eligibility of enrolled children in several ways. First, a child may be identified as income-eligible based on the sponsoring organization's receipt of a completed free and reduced price application which demonstrates that the household's income is at or below 185 percent of the Federal income poverty guidelines. (The Department acknowledges that the term

''income eligibility statement'' more accurately describes the purpose of such a form in day care homes. However, this rule refers to ''free and reduced price applications,'' instead of ''income eligibility statements,'' in order to maintain consistency with the terminology contained in § 226.23.) In addition, PRWORA also expanded, for tier II day care homes only, the categorical eligibility options found in section 9(d)(2) of the NSLA to include other Federal or State supported child care or other benefit programs with income eligibility limits at or below 185 percent of poverty. Meals served to a child who is a member of a household which participates in, or is subsidized under, such a program would also be eligible for tier I rates of reimbursement. The categorically eligible programs used to demonstrate the eligibility of children enrolled in tier II homes include those programs identified in section 9(d)(2) of the NSLA (i.e., food stamps, certain state programs for Temporary Assistance for Needy Families, and the Food Distribution Program on Indian Reservations), as well as any qualifying Federal programs identified by the Department, or State programs identified by the State agency. (Section 226.23(e) of the regulations, which contains the categorically eligible programs identified in section 9(d)(2) of the NSLA, still contains references to Aid to Families with Dependent Children (AFDC), which was eliminated pursuant to PRWORA and replaced by the program for Temporary Assistance for Needy Families (TANF). The Department will issue a future rulemaking to incorporate the provisions of PRWORA concerning TANF into the CACFP regulations.)

To facilitate the use of expanded categorical eligibility in tier II day care homes, § 226.6(f)(10) as amended by the interim rule requires that State agencies provide all sponsoring organizations, on an annual basis, a list of State-funded programs which meet the criteria for expanded categorical eligibility. In addition, on March 18, 1997, the Department provided to State agencies a list of Federal programs that meet the criteria. As indicated in the preamble to the interim rule, we expect that the process of identifying eligible programs will be ongoing at both the Federal and State levels, especially at first. This may necessitate that the list of eligible programs be updated more frequently than annually, as qualifying programs are identified.

Children from households participating in, or subsidized under, one of these programs could be identified by the sponsor in two ways. First, instead of providing income information on the free and reduced price application furnished by the sponsoring organization, the household could identify itself as participating in, or subsidized under, one of the categorically eligible programs listed on the application. Alternatively, a free and reduced price application would not be necessary for those children for whom the sponsoring organization or provider knows, on the basis of documented proof, to be categorically eligible for tier I reimbursement. This could occur when a provider receives payment for a child's care in the form of a subsidized voucher (and the voucher program has been identified by the Department or State agency as meeting the income criteria for categorically eligible programs); when the household provides the sponsor or provider with an official letter issued by the welfare or other office documenting the household's participation in a qualifying program, such as the National School Lunch Program; or when the sponsoring organization has legitimate access, for reasons unrelated to the CACFP, to eligibility information for another qualifying program. In these cases, a copy of the child's voucher, or other documentation by the sponsor of the child's participation in the other qualifying program, would be an acceptable alternative to completion of the free and reduced price application. Thus, when a provider elects the first option, the eligibility of each enrolled child may be established by submission of income information on a free and reduced price application, categorical eligibility information on a free and reduced price application, or with a copy of a voucher or other documentation available to the provider or sponsor.

When a household completes a free and reduced price application identifying itself as participating in, or subsidized under, one of the categorically eligible programs, § 226.23(e)(1)(iv) and the definition of ''Documentation'' in § 226.2 as amended by the interim rule require that such households provide the name of the enrolled child, the name of the qualifying program, and the household's case number for the program, along with the signature of an adult member of the household. Several commenters asked for clarification of the documentation requirements when the categorically eligible program in which the household participates does not issue case numbers to participants. Since not all programs issue case numbers, sponsors may accept a household's identification on the free and reduced price application of its participation in an approved Federal or State identified categorically eligible program as sufficient documentation for categorically eligible programs that do not utilize case numbers. Though they are not required to do so for free and reduced price applications collected in tier II day care homes, sponsors may verify households' participation in these programs through contact with officials of the categorically eligible program.

The only partial exception to this rule involves the Head Start Program. Because of the restrictions on Head Start categorical eligibility contained in § 9(b)(6)(A)(iii) of the NSLA, the sponsoring organization may not simply accept the household's self-identification of a child as a Head Start participant. Specifically, the NSLA limits Head Start categorical eligibility to Federally funded, income-eligible participants. Because parents of Head Start participants likely will not know whether their children are in Federally funded slots, the sponsoring organization must obtain documentation from the Head Start grantee which certifies that the child is: (1) Enrolled in a Federally funded Head Start slot; and (2) is from a household which meets Head Start's low-income criteria. The Department will issue a rulemaking in the near future to codify this provision of the law. However, sponsoring organizations and State agencies must comply with this provision in the meantime because it is explicitly contained in the law.

The second approach set forth in PRWORA recognizes that some day care providers may not want any of the households of the children in their care to receive free and reduced price applications, a fact pointed out by many commenters on the interim rule. Under this approach, the provider may elect to have the sponsor identify only categorically eligible children, under the expanded categorical eligibility provision, and receive tier I rates of reimbursement for the meals served to these children. In this case, as described above, the sponsor would identify only those children whom the sponsoring organization or provider knows, on the basis of documented proof, to be categorically eligible for tier I benefits, and would have on file only copies of vouchers or other proof of participation in an eligible program rather than free and reduced price applications.

The Department would like to emphasize that the above two approaches to identifying income-eligible children would not permit a provider to selectively identify for its

sponsoring organization those children whom the provider suspects or believes may be income-eligible, based on the provider's personal estimate of a household's socioeconomic status, and have its sponsoring organization send applications only to those households. The only time that a ''selective identification'' approach may be used is when either the sponsor or provider already possesses documented evidence of the child's or household's participation in, or subsidy under, a categorically eligible program. In these cases, the documentary evidence may be used to establish eligibility in lieu of an application. If a provider selects the first approach discussed above, then all enrolled children for whom the sponsor or provider does not already possess documentation of categorical eligibility would receive applications. Under the second approach above, no applications would be distributed.

In addition, the Department would like to point out that the interim rule required free and reduced price applications to be distributed even when a voucher, or other documented evidence was being used to establish a child's categorical eligibility. Subsequent to the publication of the interim rule, the Department reconsidered its position and concluded that the clear intent of PRWORA is to facilitate identification of income-eligible children in tier II homes by providing an approach under which a tier II day care home may receive tier I rates of reimbursement for eligible children without the distribution of applications to households. The Department's June 2, 1997, memorandum clarified this method, and this final rule removes references in § 226.23(e)(1)(i) to this requirement.

The preamble to the interim rule specifically requested comments on the appropriateness of the use of direct certification to establish an enrolled child's eligibility for tier I rates of reimbursement in a tier II day care home, and indicated that the use of direct certification in day care homes may be addressed in a future proposed rulemaking based on the nature of these comments. Direct certification, which is not permitted under the interim rule, is another method of establishing eligibility without the use of free and reduced price applications. The Department received 15 comments on the use of direct certification in tier II day care homes. Of these, 14 commenters supported direct certification, and one opposed it. Many of these commenters noted that direct certification reduces the paperwork associated with eligibility determinations, and several commenters also recommended that direct certification be included in this final rule, instead of in a future proposed rulemaking.

Under a system of direct certification, sponsoring organizations would contact the welfare (or other qualifying program) office directly and submit a list of children enrolled in their day care homes. From that list, the welfare office would identify children whose households are participating in the welfare program. It has been the Department's experience in the School Nutrition Programs, because of time and staffing constraints, that social service agencies may be reluctant to respond to these types of requests even from public entities such as school food authorities. Given that many areas are served by several sponsoring organizations that would want eligibility information for direct certification from the same local social service agency, it is possible that social service agencies would not be willing, or able, to handle all of these requests.

The key issue surrounding direct certification, however, involves access to information and household confidentiality. Eligibility information could only be released for programs which permit sharing of confidential information for purposes of determining eligibility in CACFP. A social service agency (or other government entity) may have significant concerns about sharing confidential information on households' eligibility. Therefore, the Department remains convinced that, if necessary, the appropriate place to address direct certification is in a proposed rulemaking, and not in this final rule.

Finally, under the third approach for tier II day care homes set forth in PRWORA, providers may choose to receive tier II reimbursements for all meals served to enrolled children. This approach recognizes those situations in which the provider believes it to be unlikely that any households of children in care will be income eligible for tier I reimbursements. In this case, the sponsoring organization will not collect any free and reduced price applications from the households of enrolled children, nor will it identify categorically eligible children based on provider or sponsor knowledge. Essentially, tier II homes whose providers elect this approach will operate exactly as they did before implementation of the two-tiered reimbursement structure, except that they will receive lower rates of reimbursement.

Accordingly, this final rule amends § 226.23(e)(1) to clarify the procedures for determining the income eligibility of children enrolled in tier II day care homes, particularly with respect to the use of vouchers or other documents in lieu of free and reduced price applications, as discussed above. In addition, § 226.18(b)(11) is amended to specify the three options for reimbursement available to providers of tier II day care homes. Finally, § 226.23(e)(1)(iv) and the definition of ''Documentation'' contained in § 226.2 are amended to indicate that households identifying themselves as participating in, or subsidized under, a categorically eligible program need only provide the program's case number if applicable.

Confidentiality of Household Income Information

The interim rule amended § 226.23(e)(1)(i) to require that sponsoring organizations keep eligibility information concerning individual households confidential. Specifically, sponsoring organizations are prohibited from making this information available to day care home providers. The interim rule does, however, permit sponsoring organizations to inform tier II day care homes of the number of identified income-eligible children, but not the names of these children. As discussed in the preamble to the interim rule, these requirements were promulgated to carry out the clear intent of PRWORA to protect the confidentiality of the households of children enrolled in day care homes.

The preamble to the interim rule specifically requested comments on how best to balance the confidentiality of the households of enrolled children with the needs of tier II day care home providers. The Department received 230 comments on this provision. Of these, 175 commenters expressed their belief that day care providers need to know the eligibility status of each child in their care, so that they can know the exact amount that should be in their reimbursement check each month. Many of these commenters also indicated their belief that the confidentiality of households can be protected as long as the sponsoring organization does not release specific income information from individual households, but only whether or not children in those households have been determined eligible. Others expressed concern that a check on fiscal accountability will be lost if providers do not know how much their sponsors should pay them. Three commenters indicated that providers will leave the program if they cannot know the exact amount to expect in their reimbursement payment. In addition,

seven commenters recommended that sponsors be permitted to include a parent waiver of confidentiality on the free and reduced price application distributed to households. Finally, 31 commenters expressed their support for the interim rule, under which providers are not permitted to know the eligibility status of enrolled children.

Unlike the households of children participating in other Child Nutrition Programs, households whose children are in care in CACFP day care homes do not apply to the home in order to obtain food benefits. Rather, the primary purpose of applying to the day care home is to secure care for their children. Although the children receive the nutritional benefits of the meals provided through the CACFP, the direct financial benefits associated with applying for meals go to participating providers and sponsoring organizations. The household receives only an indirect financial benefit in that the provider's receipt of higher meal reimbursements helps to keep overall day care fees lower. Thus, the Department strongly believes that it would be irresponsible to compromise the confidentiality of these households solely for the administrative convenience of providers or sponsoring organizations.

Further, while it might be convenient for providers to have information on the income status of the households of children in care, it is not necessary for the purposes of administering the Program. In accordance with PRWORA, the sponsoring organization has the responsibility for using the eligibility information to file reimbursement claims with the State agency, and for subsequently paying each provider based on the number of meals served in the home.

Many commenters expressed concern that under the interim rule providers will have no way of ensuring that their reimbursement payments are correct, as mentioned above. The Department recognizes that provider payments must be reliable and accurate. The Department fully expects that State agencies are already examining sponsor payment procedures during administrative reviews to ensure proper payments. In addition, providers who believe that their payments are incorrect may also bring the matter to the attention of the State agency. If a State agency receives repeated complaints from a particular sponsor's providers, it would be appropriate to conduct a special review of that sponsor.

With regard to whether free and reduced price applications may contain a household waiver of confidentiality which would permit sponsoring organizations to divulge the eligibility status of enrolled children, the Department strongly discourages such a practice due to PRWORA's emphasis on household confidentiality. However, if a State agency chooses to distribute an application which includes a household confidentiality waiver statement, or allows its sponsoring organizations to do so, this final rule requires that the form also include a statement informing the household that its participation in the program is not in any way dependent upon signing the waiver. Thus, a household may complete the application and choose not to have the information released to the day care home provider.

Accordingly, this final rule amends § 226.23(e)(1)(i) to require that applications that include a household confidentiality waiver statement must also include a statement informing the household that its participation in the program is not dependent upon signing such a waiver.

Finally, the Department would like to point out, as several commenters did, that this provision will not affect the ability of all tier II day care homes with identified income-eligible children to calculate their reimbursement payments, but rather only those tier II day care homes with identified income-eligible children whose sponsoring organizations select the actual count method for reimbursing their homes. For those tier II day care homes whose sponsors select either claiming percentages or blended rates, knowing the claiming percentage or blended rate will enable providers to calculate the precise amount of the reimbursement they will receive each month. (Additional discussion of the reimbursement methods available to sponsoring organizations is contained in the ''Meal Counting and Claiming Procedures'' section of the preamble below.)

At this time, the Department is not aware of any alternative to the system set forth in the interim rule that would protect the confidentiality of households. Therefore, this final rule retains the provision in the interim rule that prohibits sponsoring organizations from making free and reduced price eligibility information concerning individual households available to day care home providers.

With regard to the process of distributing and collecting free and reduced price applications from the households of children enrolled in tier II day care homes, the Department received 90 comments. Of these, 25 commenters indicated that this activity was burdensome for sponsoring organizations. Nineteen commenters expressed their concern that the households will not return completed applications because they have no financial incentive to do so. In addition, 35 commenters wanted providers to be involved in the process of distributing and/or collecting free and reduced price applications from the households of enrolled children, indicating their belief that provider involvement will facilitate return of the statements. Four commenters requested that the applications collected for the first year be valid through September 30, 1998, in order to coincide with the fiscal year.

The Department would like to point out that PRWORA's inclusion of ''expanded categorical eligibility'' for use in tier II day care homes, as previously discussed in this preamble, is one method which is intended to simplify the income eligibility determination process, and thus, encourage the return of completed applications by households. In addition, under the interim rule, as well as guidance issued by the Department on January 24, 1997, it is permissible for sponsors to have their day care home providers distribute free and reduced price applications to individual households of enrolled children, as long as the completed forms are returned by the households directly to the sponsor. If sponsoring organizations choose to have their providers distribute applications to the households of enrolled children, the Department recommends and would anticipate that providers will take the opportunity to explain the purpose of the form and to stress the importance of the household completing the form and returning it to the sponsor. This type of procedure could facilitate the household's return of eligibility information to the sponsoring organization, while at the same time maintaining the confidentiality of the income information provided by the households. However, the Department would also like to point out that either State agencies or sponsors which believe that providers should not have any role in the process of distributing applications to households may prohibit such activity.

Several of the commenters who indicated that providers should be involved in the process of distributing and/or collecting free and reduced price applications recommended that sponsors be allowed to inform providers which of the households of enrolled children have returned applications. Providers, in turn, could periodically urge those households that had not returned the forms to do so. Although

actual income information on individual households would not be released under such a scenario, the Department has serious concerns about this procedure and believes that simply knowing a household has returned a free and reduced price application may lead to assumptions about a family's income status. Therefore, the Department issued guidance on March 12, 1997, informing State agencies and sponsors that sponsors may not be permitted to inform their providers about which of the households of enrolled children have returned applications, as it would be inconsistent with the confidentiality provision of § 226.23(e)(1)(i).

Finally, as indicated above, four commenters recommended that free and reduced price applications collected during implementation be valid through September 30, 1998, to coincide with the fiscal year. In order to facilitate sponsors' implementation of the two-tiered reimbursement system, the Department already has permitted free and reduced price applications which were collected from households between March 1, 1997, and June 30, 1997, to be effective for a one-year period beginning July 1, 1997. Depending on when the applications were actually collected by sponsoring organizations, the information on the applications could be as much as 16 months old when they expire on July 1, 1998. Therefore, although sponsors may collect applications before the end of the one-year period that begins July 1, 1997, in order to have redeterminations coincide with the fiscal year cycle, free and reduced price applications which become effective upon implementation of the two-tiered system on July 1, 1997, may not be valid for more than a one-year period. This requirement helps ensure that individual eligibility determinations are based on up-to-date information, and is also consistent with policy in the other Child Nutrition Programs.

Meal Counting and Claiming Procedures

The two-tiered structure of reimbursement set forth under PRWORA necessitates new meal counting and claiming procedures for use by sponsoring organizations and those tier II day care homes in which there are a mix of income-eligible and non-income-eligible children.

The interim rule amended § 226.13(d) to set forth three methods by which sponsoring organizations may reimburse their tier II day care homes with a mix of income-eligible and non-income-eligible children—actual meal counts, claiming percentages, and blended rates. The interim rule permits sponsoring organizations to select which of the three methods they will use, though each sponsor must use only one method for all of its homes, and may change this method no more frequently than annually. In addition, if a sponsoring organization selects claiming percentages or blended rates, the interim rule requires that they be recalculated for each home at least every six months, unless the State agency requires the sponsor to recalculate a home's claiming percentage or blended rate before the required semiannual recalculation because it has reason to believe that a home's percentage of income-eligible children has changed significantly or was incorrectly established in the previous calculation.

The preamble to the interim rule requested comments on the ''reimbursement categories'' method set forth in the law and discussed in the preamble, but not included as an option in the interim rule due to the Department's opinion that it does not offer any distinct advantages over claiming percentages and blended rates. Under the ''reimbursement categories'' method, sponsoring organizations would either: (1) Establish multiple reimbursement rates within the range defined by the tier I and tier II rates, and then assign a home one of these rates based on the percentage of income-eligible children in the home; or (2) using only the tier I and tier II rates, reimburse all meals served in homes with 50 percent or more income-eligible children at the tier I rates, and all homes with less than 50 percent income-eligible children at the tier II rates. (The preamble to the interim rule describes the ''reimbursement categories'' method in more detail.) In addition, the interim rule also requested suggestions on other systems of meal counting and claiming that would not place an undue burden on day care home providers or sponsors, but would provide for reimbursement payments that accurately reflect the income level of the households of enrolled children.

The interim rule also amended § 226.13(d) to set forth the meal counting requirements for day care homes. Under these regulations, providers of tier II day care homes whose sponsoring organization uses the actual count method of reimbursement are required to record and submit to the sponsoring organization the number and types of meals served each day to each enrolled child by name. Providers whose sponsoring organization uses either claiming percentages or blended rates must submit the total number of meals served, by type, to enrolled children.

The Department received 62 comments on the meal counting and claiming provisions. Of these, 25 commenters commented on whether a State agency could require all sponsoring organizations in the State to use the same method for reimbursing tier II day care homes with a mix of income-eligible and non-income-eligible children: 19 commenters opposed the State selecting one method for all sponsors; six commenters supported it. Several commenters who supported State agency selection of the reimbursement method indicated that allowing sponsoring organizations to select the method would promote unhealthy competition among sponsoring organizations. Many commenters also indicated that State agencies already require providers to keep actual daily meal counts. These commenters believed that such requirements would necessarily force sponsoring organizations to utilize actual counts, thus depriving them of a meaningful choice of reimbursement method.

In response to commenter concern on this issue, the Department would like to reiterate that the choice of reimbursement method is the sponsoring organization's, and not the State agency's. In accordance with § 226.13(d)(3) as added by the interim rule, each sponsoring organization selects the method—either actual counts, claiming percentages, or blended rates—for reimbursing its tier II day care homes with a mix of income-eligible and non-income-eligible children. As discussed in the preamble to the interim rule, the Department decided to allow sponsoring organizations maximum flexibility by permitting them to select the reimbursement method in order to accommodate the varying levels of management sophistication among sponsors. State agencies may not require all sponsors in the State to use the same method.

With regard to commenters' concern that permitting sponsoring organizations to select the method of reimbursement would promote unhealthy competition among sponsoring organizations, none of the methods offers a financial advantage over the other to providers. Providers will choose, as they do now, the sponsoring organization whose services best meet their needs. The Department expects that this decision will be based on a variety of factors, and not exclusively the reimbursement method used by the sponsor.

However, State agencies may require—and many already do, for the purpose of monitoring compliance with licensing requirements concerning the number and ages of children in care, or for integrity or other purposes—that day care home providers maintain actual daily meal counts by child. When a State agency institutes such a requirement, sponsoring organizations still may select either actual counts, claiming percentages, or blended rates as the method they use to reimburse their tier II day care homes with a mix of income-eligible and non-income-eligible children. Sponsors selecting claiming percentages or blended rates will only use total meal counts by type of meal (i.e., breakfast, lunch/supper, supplement), rather than the daily meal counts by child, to calculate a home's reimbursement. Perhaps most significantly, use of claiming percentages or blended rates offers the additional advantage that sponsoring organizations do not have to immediately assess the eligibility status of each newly enrolled child in a day care home. Eligibility determinations for children new to a home need only be done by the time the recalculation of the claiming percentage or blended rate is necessary, which is at least every six months.

In addition, 14 commenters on the meal counting and claiming provisions indicated their belief that sponsoring organizations should only be required to recalculate each home's claiming percentage or blended rate on an annual basis, rather than semiannually as required in the interim rule. Most of these commenters pointed out that PRWORA required only annual recalculation. Four commenters indicated that requiring recalculation on a semiannual basis would add unnecessary paperwork for sponsoring organizations. Finally, two commenters indicated that any integrity concerns surrounding annual redeterminations of claiming percentages or blended rates were already adequately addressed in § 226.13(d)(3) as added by the interim rule, which permits State agencies to require sponsoring organizations to recalculate the claiming percentage or blended rate at any time, as discussed above.

Several commenters were concerned, as mentioned above, that PRWORA and the interim rule were in conflict because PRWORA requires annual redeterminations of claiming percentages or blended rates, while the interim rule requires semiannual redeterminations. The Department would like to point out that section 17(f)(3)(A)(iii)(IV) of the NSLA, as amended by section 708(e)(1) of PRWORA, sets forth two possible alternatives that may be used by the Secretary for simplified meal counting and claiming, and also gives the Secretary the authority to develop his own simplified procedures. While the alternative of claiming percentages/blended rates as set forth in PRWORA does indicate that the claiming percentage or blended rate be set on an annual basis, PRWORA does not require the Secretary to use either of these specific alternatives. In selecting claiming percentages and blended rates, and by requiring that recalculations be made on a semiannual basis, the discretion provided to the Secretary in PRWORA was being exercised.

Among the reasons for requiring semiannual recalculations was the Department's concern, as discussed in the preamble to the interim rule, that the simplified methods set forth in PRWORA, including claiming percentages and blended rates, do not adequately capture the frequent enrollment changes that are common in many day care homes. Despite one commenter's belief that the policy for recalculations in day care homes should be consistent with that for CACFP centers, the enrollment changes in day care homes affect the claiming percentage or blended rate much more dramatically than enrollment changes in centers do, simply because of the smaller number of children enrolled in a family day care home. Requiring that the claiming percentages and blended rates be recalculated on a semiannual, rather than annual, basis helps balance the need to account for the effects of these enrollment changes by ensuring more current numbers with the Department's desire to minimize administrative burden on sponsors. In addition, the Department is also concerned about the potential for abuse with claiming percentages and blended rates. Again, requiring semiannual instead of annual recalculations, as well as providing the State agency the authority to require a sponsoring organization to perform recalculations any time it has reason to believe that a home's percentage of income-eligible children has changed significantly or was incorrectly established in the previous calculation, will help minimize the potential for abuse associated with this method. Finally, despite commenters who indicated their belief that providing State agencies the authority to require recalculations would adequately address integrity concerns, the Department believes that requiring semiannual recalculations, in conjunction with providing State agencies this authority, is much more effective in promoting program integrity and maximizing the accuracy of the claiming process.

In response to the request in the interim rule for comments on the ''reimbursement categories'' method, as well as any alternative methods of reimbursement, the Department received five comments. Two commenters supported the reimbursement categories method. In addition, two commenters recommended the reimbursement categories method discussed in the preamble to the interim rule under which a tier II day care home would receive tier I rates of reimbursement for all meals served as long as at least 50 percent of enrolled children were determined eligible for free or reduced price meals. Finally, one commenter recommended that three tiers of reimbursement be instituted, with the middle tier applicable for all tier II homes with a mix of income-eligible and non-income-eligible children.

These comments did not persuade the Department to relinquish its concerns about the accuracy, complexity, and integrity of the alternative methods of reimbursement. The Department continues to hold the position that neither of the reimbursement categories methods described in PRWORA is acceptable as a means of reimbursing tier II day care homes with a mix of income-eligible and non-income-eligible children, since they are much less accurate in accomplishing the law's goal of targeting reimbursements to low-income children than either claiming percentages or blended rates.

Accordingly, this final rule makes no change in the requirement set forth in the interim rule that sponsoring organizations that select claiming percentages or blended rates as the method for reimbursing their tier II day care homes perform recalculations of the percentages or rates on at least a semiannual basis.

When a sponsoring organization chooses claiming percentages or blended rates for reimbursing its tier II day care homes with a mix of income-eligible and non-income-eligible children, § 226.13(d)(3)(ii) as added by the interim rule requires that the claiming percentage or blended rate be based on ''one month's data concerning the number of enrolled children determined eligible for free or reduced price meals.'' (This provision of the regulations was corrected in a docket published in the **Federal Register** on February 6, 1997 (62 FR 5519)). The preamble to the corrected interim rule

discussed two methods available to sponsoring organizations for making these calculations—attendance lists and enrollment lists—and requested comments on whether both of these alternative methods should continue to be permitted in the final rule.

The sponsoring organization, after having determined the income eligibility of enrolled children, uses the information on the attendance or enrollment list to calculate the home's claiming percentage or blended rate. As discussed in the preamble to the interim rule, the primary difference between attendance and enrollment lists is that attendance lists produce weighted results of participation. That is, an attendance list shows, whether based on days or meals, the *rate* of participation of each child, by name, in the home in the month. In contrast, an enrollment list provides no measure of the rate of participation: a child who participates only one day during the month is counted the same for purposes of the calculation as a child who participates every day during the month. As indicated in the preamble to the interim rule, though the attendance list may impose an additional burden on the sponsor and its day care homes, it provides a higher level of accuracy than an enrollment list. Furthermore, an attendance list based on meals, rather than days, is an actual count of meals provided, by child, for one month, therefore providing the most accurate results on which to base the home's claiming percentage or blended rate.

The Department received three comments on the use of attendance and enrollment lists. Two commenters indicated a preference for attendance lists over enrollment lists. One commenter suggested that each State agency be permitted to decide which method all sponsors in the State will use, instead of sponsors. Since sponsoring organizations have the choice of which method to use for reimbursing their tier II day care homes with a mix of income-eligible and non-income-eligible children, sponsors choosing claiming percentages or blended rates also may select which method—either attendance list or enrollment list—to use in calculating claiming percentages or blended rates for their homes. The Department believes that permitting sponsoring organizations to select the method, instead of the State agency, will provide flexibility to sponsoring organizations, in recognition of their varying sizes and levels of management sophistication. Therefore, this final rule retains both attendance lists and enrollments lists as the methods for sponsoring organizations to use in calculating claiming percentages or blended rates for their homes. In light of the limited commenter input, the Department will attempt to gather information based on operating experience from State and local program administrators concerning the ramifications of allowing sponsors to choose either method, and may consider proposing changes in this area in a future rulemaking.

In addition, questions were raised subsequent to the publication of the interim rule regarding how to define ''attendance'' and ''enrollment'' for the purposes of making these calculations. The Department would like to clarify that, for the purposes of calculations made using either an attendance list or an enrollment list, sponsoring organizations and providers may consider a child ''in attendance'' or ''enrolled'' only when the child: (1) Is officially enrolled for care (i.e., the provider has the requisite enrollment paperwork for the child); (2) is present in the home for the purpose of child care; and (3) has eaten at least one meal with the other children in care during the claiming period. Thus, the difference between the two methods is not a function of a difference in definitions; rather, it is that an attendance list reflects *weighted* participation (i.e., the frequency of either the child's attendance or the number of meals eaten by the child) and is, therefore, a more mathematically accurate portrayal of the home's meal service during the month.

Accordingly, §§ 226.13(d)(3)(ii) and (iii) are amended by adding specific reference to attendance lists and enrollment lists as the methods available to sponsoring organizations for calculating each home's claiming percentage or blended rate. In addition, in order to ensure consistency of application among all sponsoring organizations, this final rule amends § 226.2 to include the above-discussed definition of enrollment/attendance under the current definition of ''enrolled child.''

Administrative Funds for Sponsoring Organizations

In accordance with § 226.12(a), during any fiscal year, administrative payments for sponsoring organizations may not exceed the lesser of: (1) Actual expenditures for the costs of administering the Program less income to the Program; or (2) the amount of administrative costs approved by the State agency in the sponsoring organization's budget; or (3) the sum of the products obtained by multiplying each month the number of homes administered by the sponsoring organization by a set of fixed reimbursement rates. In addition, § 226.12(a) of the regulations indicates that ''during any fiscal year, administrative payments to a sponsoring organization may not exceed 30 percent of the total amount of administrative payments and food service payments for day care home operations.'' The interim rule did not make any changes to the regulations concerning administrative payments, including the requirement limiting a sponsor's administrative funds.

Nevertheless, the Department received 14 comments on this provision of the regulations, all of which expressed concern that lower food service payments resulting from the two-tiered reimbursement system will result in some sponsoring organizations being reimbursed for less than their full cost of administering the Program because of the 30 percent cap. Most commenters suggested changing the maximum limit on administrative payments to a figure higher than 30 percent. Some recommended that this regulatory provision be ''suspended'' until such time as its impact on sponsoring organization operations can be determined. In addition, 28 commenters indicated that sponsoring organizations need additional administrative funds to effectively administer the two-tiered reimbursement system. Finally, six commenters requested that State agencies continue to be required to make administrative fund advances available to sponsoring organizations, a former requirement of State agencies which was made optional under section 708(f) of Pub. L. 104–193.

No changes were made by the interim rule to the provision limiting administrative payments to 30 percent of administrative and food service payments because it is the Department's position that the current limitation on administrative payments is reasonable. Further, the current limitation on administrative payments, by maintaining an appropriate balance between the amount spent by sponsoring organizations on administrative and program meal expenses, helps achieve the Program goal of serving meals to enrolled children within reasonable fiscal limits. The Department recognizes that a limited number of sponsoring organizations, such as those with few homes, a high percentage of tier II day care homes, and a high percentage of non-income-eligible children in these homes, may be affected by this limitation under the two-tiered

reimbursement system. However, at this time the Department does not foresee that this possible consequence of the law will be widespread enough to warrant changing or suspending the current limitation. The study mandated by section 708(l) of PRWORA requires the Department to monitor the number of sponsoring organizations in the CACFP and consider whether changes need to be proposed in a future rulemaking. Absent such evidence, the Department is unwilling to make a change to the administrative reimbursement limit. For similar reasons, it is premature for the Department to propose any change to the current administrative rates paid to sponsors.

As indicated above, section 708(f) of Pub. L. 104–193 amended section 17(f) of the NSLA to make payment of advances to CACFP institutions, including administrative advances to sponsoring organizations of day care homes, optional. Although this provision of PRWORA is already in effect due to its nondiscretionary nature, the Department will make a conforming change to include this provision in the regulations in a future rulemaking. Due to this legislative provision, it is beyond the authority of the Department to *require* that State agencies continue to make advances available to sponsors. Therefore, sponsoring organizations should address concerns regarding advances to their State agencies.

Accordingly, this final rule makes no changes to the regulations governing administrative payments, including the requirement in § 226.12(a) regarding the limitation on administrative payments to sponsoring organizations.

Verification Requirements for Tier II Homes

As discussed in the preamble to the interim rule, no changes were made to the verification requirements for State agencies. Because day care homes are considered ''nonpricing programs'' (i.e., there is no separate identifiable charge made for meals served to participants), State agencies must follow the provisions of § 226.23(h)(1), for ''nonpricing programs,'' to verify the applications of day care home providers'' own children, as well as the applications of households of children enrolled in tier II day care homes. This section requires that State agencies review all free and reduced price applications on file to ensure that: (1) The application has been correctly and completely executed by the household; (2) the sponsoring organization has correctly determined and classified the eligibility of enrolled children; and (3) the sponsoring organization has accurately reported to the State agency the number of enrolled children who meet the criteria for free or reduced price eligibility and the number who do not. This section also permits State agencies to conduct additional verification to determine the validity of information supplied by households on the application, in accordance with § 226.23(h)(2), the verification procedures for ''pricing programs.'' In addition, State agencies may conduct the required verification in conjunction with the reviews required by § 226.6(l).

The Department received two comments on the verification requirements for applications collected from the households of children enrolled in tier II day care homes. Commenters expressed concern regarding the burden associated with a State agency review of all applications on file, and suggested that State agencies instead be required to review a sample of the applications.

The Department recognizes that the requirement at § 226.23(h)(1) that a State agency review all of the applications maintained by a sponsoring organization could place a significant burden on a State agency, especially when the State agency is conducting a review of a large sponsoring organization with a large number of tier II day care homes for which applications have been collected. Since the verification required for applications collected from the households of children enrolled in tier II day care homes does not include verification of the income information provided by the households (or, for categorically eligible children, confirmation of participation in the categorically eligible programs) as discussed above, it is the Department's position that conducting the required verification on less than 100 percent of the applications strikes a balance between the need for detecting widespread or significant problems and the burden of reviewing all applications on file. Unlike most child care centers or sponsoring organizations of centers, the total number of applications for a sponsoring organization of day care homes may be quite large. Therefore, this final rule requires State agencies to conduct verification, in accordance with § 226.23(h)(1), only of the applications for enrolled children in those tier II day care homes that are selected for inclusion in the required review of the sponsoring organization, in accordance with §§ 226.6(l) (1) and (2), instead of for all of the sponsor's tier II day care homes. However, to help ensure that widespread or significant problems are identified, this final rule requires State agencies to ensure that the homes selected for review are representative of the sponsor's proportion of tier I, tier II, and tier II day care homes with a mix of income-eligible and non-income-eligible children, and that at least 10 percent of all applications on file in the sponsorship are reviewed as part of the State agency's review. The review requirements for sponsoring organizations and their day care homes are set forth in § 226.6(l). This rule also adds language to clarify that these verification requirements also apply to situations in which vouchers or other documentation are used in lieu of applications, in which case the State agency would review the voucher or other documentation on file.

Finally, the interim rule does not require sponsoring organizations to perform pricing program verification of income eligibility information for children enrolled in day care homes. However, the Department has been asked whether sponsoring organizations have the authority to verify the income information provided by the households of children enrolled in day care homes if they have reason to question the validity of the information. In order to help ensure Program integrity and appropriately targeted reimbursement rates, it is the Department's opinion that sponsoring organizations should have this authority.

Accordingly, this final rule amends § 226.23(h)(6) to explicitly provide sponsoring organizations the authority to conduct pricing verification of the income information provided by the households of children enrolled in day care homes. In addition, this final rule amends § 226.23(h)(1) to require State agencies to conduct nonpricing verification only for the applications of enrolled children in day care homes that are included in the required review of the sponsoring organization.

Other Amendments

This rule also makes technical changes to the definition of ''Documentation'' in § 226.2, and to §§ 226.23(e)(1) (i) and (iv), to include amendments which were made to these sections in an interim rule published on May 1, 1997 (62 FR 23613), but inadvertently eliminated from the Code of Federal Regulations when the January 7, 1997, interim rule (62 FR 889) on the two-tiered reimbursement system went into effect on July 1, 1997.

List of Subjects

7 CFR Part 210

Breakfast, Children, Food assistance programs, Grant program—Social

programs, Lunch, Meal Supplements, Nutrition, Reporting and recordkeeping requirements, School Nutrition Program, Surplus agricultural commodities.

7 CFR Part 226

Day care, Food assistance programs, Grant programs—health, infants, and children, Records, Reporting and recordkeeping requirements, Surplus agricultural commodities.

Accordingly, the interim rule amending 7 CFR parts 210 and 226 which was published at 62 FR 889 on January 7, 1997, is adopted as a final rule with the following changes:

PART 210—NATIONAL SCHOOL LUNCH PROGRAM

1. The authority citation for part 210 continues to read as follows:

Authority: 42 U.S.C. 1751–1760, 1779.

2. In Section 210.9, paragraph (b)(20) is revised to read as follows:

§ 210.9 Agreement with State agency.

* * * * *

(b) *Annual agreement.* * * *

(20) No later than March 1, 1997, and no later than December 31 of each year thereafter, provide the State agency with a list of all elementary schools under its jurisdiction in which 50 percent or more of enrolled children have been determined eligible for free or reduced price meals as of the last operating day the preceding October. The State agency may designate a month other than October for the collection of this information, in which case the list must be provided to the State agency within 60 calendar days following the end of the month designated by the State agency. In addition, each school food authority shall provide, when available for the schools under its jurisdiction, and upon the request of a sponsoring organization of day care homes of the Child and Adult Care Food Program, information on the boundaries of the attendance areas for the elementary schools identified as having 50 percent or more of enrolled children certified eligible for free or reduced price meals.

* * * * *

3. In § 210.19, paragraph (f) is revised to read as follows:

§ 210.19 Additional responsibilities.

* * * * *

(f) *Cooperation with the Child and Adult Care Food Program.* On an annual basis, the State agency shall provide the State agency which administers the Child and Adult Care Food Program with a list of all elementary schools in the State participating in the National School Lunch Program in which 50 percent or more of enrolled children have been determined eligible for free or reduced price meals as of the last operating day of the previous October, or other month specified by the State agency. The first list shall be provided by March 15, 1997; subsequent lists shall be provided by February 1 of each year or, if data is based on a month other than October, within 90 calendar days following the end of the month designated by the State agency. The State agency may provide updated free and reduced price enrollment data on individual schools to the State agency which administers the Child and Adult Care Food Program only when unusual circumstances render the initial data obsolete. In addition, the State agency shall provide the current list, upon request, to sponsoring organizations of day care homes participating in the Child and Adult Care Food Program.

PART 226—CHILD AND ADULT CARE FOOD PROGRAM

1. The authority citation for part 226 continues to read as follows:

Authority: Secs. 9, 11, 14, 16, and 17, National School Lunch Act, as amended (42 U.S.C. 1758, 1759a, 1762a, 1765, and 1766).

2. In § 226.2:

a. Paragraphs (b), (c), and (d) of the definition of ''Documentation'' are revised; and

b. The definition of ''Enrolled child'' is amended by adding a sentence at the end.

The revisions and addition read as follows:

§ 226.2 Definitions

* * * * *

Documentation means: * * *

(b) For a child who is a member of a food stamp or FDPIR household or an AFDC assistance unit, ''documentation'' means the completion of only the following information on a free and reduced price application:

(1) The name(s) and appropriate food stamp, FDPIR or AFDC case number(s) for the child(ren); and

(2) The signature of an adult member of the household; or

(c) For a child in a tier II day care home who is a member of a household participating in a Federally or State supported child care or other benefit program with an income eligibility limit that does not exceed the eligibility standard for free or reduced price meals:

(1) The name(s), appropriate case number(s) (if the program utilizes case numbers), and name(s) of the qualifying program(s) for the child(ren), and the signature of an adult member of the household; or

(2) If the sponsoring organization or day care home possesses it, official evidence of the household's participation in a qualifying program (submission of a free and reduced price application by the household is not required in this case); or

(d) For an adult participant who is a member of a food stamp or FDPIR household or is an SSI or Medicaid participant, as defined in this section, ''documentation'' means the completion of only the following information on a free and reduced price application:

(1) The name(s) and appropriate food stamp or FDPIR case number(s) for the participant(s) or the adult participant's SSI or Medicaid identification number, as defined in this section; and

(2) The signature of an adult member of the household.

Enrolled child means * * * In addition, for the purposes of calculations made by sponsoring organizations of family day care homes in accordance with §§ 226.13(d)(3)(ii) and 226.13(d)(3)(iii), ''enrolled child'' (or ''child in attendance'') means a child whose parent or guardian has submitted a signed document which indicates that the child is enrolled for child care; who is present in the day care home for the purpose of child care; and who has eaten at least one meal during the claiming period.

* * * * *

3. In § 226.6, paragraph (f)(9) is amended by removing the second sentence of the paragraph and by adding a new sentence in its place, and by adding a new sentence at the end to read as follows:

§ 226.6 State agency administrative responsibilities.

* * * * *

(f) * * *

(9) * * * The State agency shall provide the list to sponsoring organizations by April 1, 1997, and by February 15 of each year thereafter, unless the State agency that administers the National School Lunch Program has elected to base data for the list on a month other than October, in which case the State agency shall provide the list to sponsoring organizations within 15 calendar days of its receipt from the State agency that administers the National School Lunch Program. * * * The State agency shall not routinely require annual redeterminations of the tiering status of tier I day care homes based on updated elementary school data.

* * * * *

4. In § 226.13:

a. Paragraph (d)(3)(ii) is amended by adding a new sentence after the first sentence; and

b. The first sentence of paragraph (d)(3)(iii) is revised.

The addition and revision read as follows:

§ 226.13 Food service payments to sponsoring organizations for day care homes.

* * * * *

(d) * * *

(3) * * *

(ii) * * * Sponsoring organizations shall obtain one month's data by collecting either enrollment lists (which show the name of each enrolled child in the day care home), or attendance lists (which show, by days or meals, the rate of participation of each enrolled child in the day care home).* * *

(iii) Determine a blended per-meal rate of reimbursement, not less frequently than semiannually, for each such day care home by adding the products obtained by multiplying the applicable rates of reimbursement for each category (tier I and tier II) by the claiming percentage for that category, as established in accordance with paragraph (d)(3)(ii) of this section.* * *

* * * * *

5. In § 226.15:

a. Paragraph (e)(3) is revised; and

b. Paragraph (f) is amended by adding seven new sentences after the second sentence, and by adding a new sentence at the end.

The additions and revision read as follows:

§ 226.15 Institution provisions.

* * * * *

(e) * * *

(3) Documentation of: The enrollment of each child at day care homes; information used to determine the eligibility of enrolled providers' children for free or reduced price meals; information used to classify day care homes as tier I day care homes, including official source documentation obtained from school officials when the classification is based on elementary school data; and information used to determine the eligibility of enrolled children in tier II day care homes that have been identified as eligible for free or reduced price meals in accordance with § 226.23(e)(1).

* * * * *

(f) * * * When using elementary school or census data for making tier I day care home determinations, a sponsoring organization shall first consult school data, except in cases in which busing or other bases of attendance, such as magnet or charter schools, result in school data not being representative of an attendance area's household income levels. In these cases, census data should generally be consulted instead of school data. A sponsoring organization may also use census data if, after reasonable efforts are made, as defined by the State agency, the sponsoring organization is unable to obtain local elementary school attendance area information. A sponsoring organization may also consult census data after having consulted school data which fails to support a tier I day care home determination for rural areas with geographically large elementary school attendance areas, for other areas in which an elementary school's free and reduced price enrollment is above 40 percent, or in other cases with State agency approval. However, if a sponsoring organization believes that a segment of an otherwise eligible elementary school attendance area is above the criteria for free or reduced price meals, then the sponsoring organization shall consult census data to determine whether the homes in that area qualify as tier I day care homes based on census data. If census data does not support a tier I classification, then the sponsoring organization shall reclassify homes in segments of such areas as tier II day care homes unless the individual providers can document tier I eligibility on the basis of their household income. When making tier I day care home determinations based on school data, a sponsoring organization shall use attendance area information that it has obtained, or verified with appropriate school officials to be current, within the last school year. * * * The State agency shall not routinely require annual redeterminations of the tiering status of tier I day care homes based on updated elementary school data.

* * * * *

6. In § 226.18, paragraph (b)(11) is amended by adding a new sentence at the end of the paragraph to read as follows:

§ 226.18 Day care home provisions.

* * * * *

(b) * * *

(11) * * * These options include: electing to have the sponsoring organization attempt to identify all income-eligible children enrolled in the day care home, through collection of free and reduced price applications and/or possession by the sponsoring organization or day care home of other proof of a child or household's participation in a categorically eligible program, and receiving tier I rates of reimbursement for the meals served to identified income-eligible children; electing to have the sponsoring organization identify only those children for whom the sponsoring organization or day care home possess documentation of the child or household's participation in a categorically eligible program, under the expanded categorical eligibility provision contained in § 226.23(e)(1), and receiving tier I rates of reimbursement for the meals served to these children; or receiving tier II rates of reimbursement for all meals served to enrolled children.

* * * * *

7. In § 226.23:

a. Paragraph (e)(1)(i) is amended by removing the third sentence and adding a new sentence in its place, by adding the words ''or FDPIR'' after the words ''food stamp'' each time they appear in the sixth sentence, and by adding a new sentence to the end;

b. Paragraph (e)(1)(iv) is revised;

c. A new paragraph (e)(1)(vi) is added;

d. Paragraph (h)(1) is revised; and

e. Paragraph (h)(6) is amended by adding a new sentence to the end.

The additions and revision read as follows:

§ 226.23 Free and reduced price meals.

* * * * *

(e)(1) * * *

(i) * * * At the request of a provider in a tier II day care home, sponsoring organizations of day care homes shall distribute applications for free and reduced price meals to the households of all children enrolled in the home, except that applications need not be distributed to the households of enrolled children that the sponsoring organization determines eligible for free and reduced price meals under the circumstances described in paragraph (e)(1)(vi) of this section. * * * If a State agency distributes, or chooses to permit its sponsoring organizations to distribute, applications to the households of children enrolled in tier II day care homes which include household confidentiality waiver statements, such applications shall include a statement informing households that their participation in the program is not dependent upon signing the waivers.

* * * * *

(iv) If they so desire, households applying on behalf of children who are members of food stamp or FDPIR households or AFDC assistance units may apply under this paragraph rather than under the procedures described in paragraph (e)(1)(ii) of this section. In

addition, households of children enrolled in tier II day care homes who are participating in a Federally or State supported child care or other benefit program with an income eligibility limit that does not exceed the eligibility standard for free and reduced price meals may apply under this paragraph rather than under the procedures described in paragraph (e)(1)(ii) of this section. Households applying on behalf of children who are members of food stamp or FDPIR households; AFDC assistance units; or for children enrolled in tier II day care homes, other qualifying Federal or State program, shall be required to provide:

(A) For the child(ren) for whom automatic free meal eligibility is claimed, their names and food stamp, FDPIR, or AFDC case number; or for the households of children enrolled in tier II day care homes, their names and other program case numbers (if the program utilizes case numbers); and

(B) The signature of an adult member of the household as provided for in paragraph (e)(1)(ii)(G) of this section. In accordance with paragraph (e)(1)(ii)(F) of this section, if a case number is provided, it may be used to verify the current certification for the child(ren) for whom free meal benefits are claimed. Whenever households apply for children not receiving food stamp, FDPIR, or AFDC benefits; or for tier II homes, other qualifying Federal or State program benefits, they must apply in accordance with the requirements set forth in paragraph (e)(1)(ii) of this section.

* * * * *

(vi) A sponsoring organization of day care homes may identify enrolled children eligible for free and reduced price meals (i.e., tier I rates), without distributing free and reduced price applications, by documenting the child's or household's participation in or receipt of benefits under a Federally or State supported child care or other benefit program with an income eligibility limit that does not exceed the eligibility standard for free and reduced price meals. Documentation shall consist of official evidence, available to the tier II day care home or sponsoring organization, and in the possession of the sponsoring organization, of the household's participation in the qualifying program.

* * * * *

(h) * * *

(1) *Verification procedures for nonpricing programs.* Except for sponsoring organizations of family day care homes, State agency verification procedures for nonpricing programs shall consist of a review of all approved free and reduced price applications on file. For sponsoring organizations of family day care homes, State agency verification procedures shall consist of a review only of the approved free and reduced price applications (or other documentation, if vouchers or other documentation are used in lieu of free and reduced price applications) on file for those day care homes that are required to be reviewed when the sponsoring organization is reviewed, in accordance with the review requirements set forth in section 226.6(l) of this Part. However, the State agency shall ensure that the day care homes selected for review are representative of the proportion of tier I, tier II, and tier II day care homes with a mix of income-eligible and non-income-eligible children in the sponsorship, and shall ensure that at least 10 percent of all free and reduced price applications (or other documentation, if applicable) on file for the sponsorship are verified. The review of applications shall ensure that:

(i) The application has been correctly and completely executed by the household;

(ii) The institution has correctly determined and classified the eligibility of enrolled participants for free or reduced price meals or, for family day care homes, for tier I or tier II reimbursement, based on the information included on the application submitted by the household;

(iii) The institution has accurately reported to the State agency the number of enrolled participants meeting the criteria for free or reduced price meal eligibility or, for day care homes, the number of participants meeting the criteria for tier I reimbursement, and the number of enrolled participants that do not meet the eligibility criteria for those meals; and

(iv) In addition, the State agency may conduct further verification of the information provided by the household on the approved application for program meal eligibility. If this effort is undertaken, the State agency shall conduct this further verification for nonpricing programs in accordance with the procedures described in paragraph (h)(2) of this section.

* * * * *

(6) * * * Sponsoring organizations of day care homes may verify the information on applications submitted by households of children enrolled in day care homes in accordance with the procedures contained in paragraph (h)(2)(i) of this section.

Dated: February 13, 1998.

Shirley R. Watkins,

Under Secretary, Food, Nutrition and Consumer Services.

Economic Impact Analysis

1. Title

Child and Adult Care Food Program: Improved Targeting of Day Care Home Reimbursements.

2. Statutory Authority

Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Pub. L. 104–193)

3. Rulemaking Background

The interim and final rules amend the Child and Adult Care Food Program (CACFP) regulations governing reimbursement for meals served in family or group day care homes by incorporating provisions of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Pub. L. 104–193). These provisions better target assistance to low income children by reducing the reimbursement for meals served to children who do not qualify for low-income subsidies. Specifically, this rule develops a two tier reimbursement structure for meals served to children enrolled in family or group day care homes. Under this structure, the level of reimbursement for meals served to enrolled children will be determined by: (1) The location of the day care home; (2) the income of the day care provider; or (3) the income of each enrolled child's household. The rules target CACFP meal reimbursement payments to low-income children and the day care home providers who serve them, where low-income is defined as not exceeding 185 percent of the Federal income poverty guidelines. The rules retain essentially near-current reimbursement rates for meals served to children by providers residing in low-income areas or served by providers who are low-income. Near-current reimbursements will also be retained for meals served to children who are identified as low-income even if the provider neither resides in a low-income area nor is low-income. Meals served to all other children will be reimbursed at the lower rates, although the lower rates are still high enough that participation in CACFP is expected to remain strong and new day care homes will continue to join CACFP. The interim rule became effective July 1, 1997; the final rule becomes effective 60 days after publication in the **Federal Register**.

4. Motivation for Statutory Changes and Summary of Findings

Until 1978, eligibility for free and reduced price meals in the Child and Adult Care Food Program (CACFP) was based on essentially the same income thresholds and procedures as those used in the National School Lunch Program: children in households at or below 130 percent of the Federal income poverty guidelines were eligible to have meals served to them reimbursed at the ''free'' (highest) rate while children in households with incomes above 130 but not exceeding 185 percent of the guidelines were eligible to have their meals reimbursed at the ''reduced price'' (middle) rate. In 1978, about 70 percent of CACFP enrolled children were from households at or below 185 percent of the Federal income poverty guidelines. The Child Nutrition Amendments of 1978 (Pub. L. 95–627) eliminated individual free and reduced price eligibility determinations (means tests) in CACFP day care homes, which substantially reduced program burden, and established a single reimbursement rate for each type of meal served in day care homes. Public Law 95–627 made no comparable changes to CACFP day care centers. The day care home meal reimbursement rates were set (by rulemaking) slightly below the rates used for meals served to children in CACFP centers with documented incomes below 130 percent of the Federal income poverty guidelines (''free'' rates). The burden reduction and single rates in day care homes had the effect of promoting program growth. However, that growth turned out to be primarily among non-needy children (above 185 percent of Federal income poverty guidelines). By the late 1980's, just 30 percent of children in CACFP day care homes were from households with incomes at or below 185 percent of the Federal income poverty guidelines, and by 1995, the proportion had fallen to 22 percent. Public Law 95–627's elimination of individual means testing in CACFP day care homes thus produced a program at odds with the Child Nutrition Program's historical focus of targeting higher benefits to low-income children.

The President and Congress proposed to re-target benefits in CACFP day care homes by retaining the current day care home rates for meals served to low-income children and establishing new, lower rates for meals served to the non-needy. The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Pub. L. 104–193) sought to re-target benefits but, to keep program administration burdens down, did not call for a reinstatement of individual means testing of all day care home participants. Public Law 104–193 effectively retained the current meal reimbursements for meals served in tier I CACFP day care homes, i.e., day care homes operated by low income providers or located in low income areas. In all other CACFP day care homes, tier II homes, a lower rate was established, as these children are less likely to be low income. Public Law 104–193 provides for low income children in tier II day care homes by allowing the higher meal reimbursements to be claimed for all meals served to the children in tier II homes who are individually means tested and found to be needy. These changes, along with others called for by Public Law 104–193, are being implemented by this rule and the interim rule. Public Law 104–193's two tier rate structure is estimated to produce a six year savings of $1.7 billion (fiscal years 1997–2002).

Despite the reduction in reimbursement rates, the numbers of tier I and tier II day care homes participating in the CACFP are both expected to grow, although at slower rates than projected before Public Law 104–193. That CACFP day care home participation is expected to remain strong is important since welfare reform will lead more low-income parents to enter the workforce, which will increase the demand for day care. Tier I homes will continue to effectively receive the pre-Public Law 104–193 reimbursement rates. While the reimbursements available to tier II homes have been reduced—CACFP weekly revenue for an average tier II home with no documented low income children will drop from $82 to $41—CACFP meal reimbursements still represent another source of income for day care homes and in many cases will provide ample incentive to participate in the CACFP. Some would-be tier II providers will find that the lower rates offer insufficient incentive to remain in the CACFP and will leave the program; however, FCS expects that most tier II providers will remain in the CACFP and accommodate the reduced rates through some combination of absorbing the loss, raising child care fees, and making cost-saving operational changes. In addition, there is about a 20 percent annual turnover of homes offering day care services, and these homes regularly offer a fresh group of homes that will probably choose to participate in the CACFP.

Other CACFP organizations are also affected by Public Law 104–193 and this rulemaking. Organizations that sponsor day care homes (sponsors), which have agreements with State CACFP agencies to operate the CACFP in day care homes have new burdens due to the two tier system. The new sponsor burdens are associated with classifying day care homes as tier I or tier II, determining whether children in tier II homes have incomes below 185 percent of the Federal income poverty guidelines, informing homes of their new rights and responsibilities under this rule, and performing the other administrative duties imposed by this rule. The Department estimates that for sponsors considered as a group, the new, recurring burdens (one-time implementation burdens were not estimated) will represent an average increase of about 2 percent over current burden levels. However, as with any average, some sponsors will realize more than a 2 percent increase in recurring burden (while others will realize less than a 2 percent increase). In addition, implementation burdens during the first year or two of tiering may be significant. State CACFP agencies will see a noticeable increase in recurring burden associated with complying with new tiering related sponsor review requirements, providing sponsors with school and census area-eligibility information, and providing sponsors tiering related technical assistance. State agencies administering the NSLP and school districts also have new responsibilities under this rulemaking, although these responsibilities do not entail substantial new burdens.

5. Comparison of Final Analysis With Interim Analysis

The final analysis makes few technical changes to the interim analysis (in terms of numbers used and assumptions made). All technical changes are based on new CACFP program data, a recently completed study of the CACFP, or comments received on the interim analysis. Updating the analysis with the new program and study data produces improved cost and burden estimates. The changes significantly decrease the total Federal savings expected from the two tier system, with projected six year savings, fiscal years 1997–2002, declining from $2.2 to $1.7 billion. Essentially no changes have been made to the analysis' assessment of the effects that the two tier system will have on particular providers, parents, and children.

New CACFP program data was used to update several numbers in the analysis, including the number of CACFP participating day care homes (DCHs), the number of DCH sponsors,

and the average number of DCHs served by sponsors. These updates have a negligible effect on the findings of the analysis.

Since the publication of the interim analysis on January 1, 1997, the Food and Consumer Service has completed the Early Childhood and Child Care Study [1] (ECCCS). The ECCCS is a nationally representative evaluation of the CACFP and includes household income data for DCH providers and children enrolled in DCHs. The data on provider's and enrolled children's household incomes are appreciably different from the figures used in the interim analysis. ECCCS found that 38 percent of DCH providers are low-income while only 22 percent of children enrolled in DCHs are low-income. The interim analysis, based on the best data available at that time, indicated that 22 percent of DCH providers and 30 percent of DCH enrolled children were low-income, which understated the number of low-income providers and overstated the number of low-income DCH children. Together with the provider income data, the income data for DCH enrolled children indicate that low-income providers will probably serve a substantial number of non-low-income children, since 38 percent of providers are low-income while only 22 percent of DCH enrolled children are.

The ECCCS income data have several implications for the analysis. The provider data imply there are more low-income providers than estimated in the interim analysis. This change increases the percentage of DCH meals that will be reimbursed at the higher meal reimbursement rates and is the piece of data responsible for improving the accuracy of the estimate of Federal savings from tiering. The increased percentage of low-income providers also has implications for sponsor burdens. Since sponsors are responsible for identifying which DCHs are eligible for the higher reimbursement rates (tier I) and for verifying the DCHs' tier I eligibility, the increased proportion of DCHs eligible for the higher rates will increase the burden on sponsors for making DCH tier I eligibility determination burdens.

The final analysis is organized nearly the same as the interim, and the analytic section appearing in the interim analysis (numbered 6 in the final analysis and 4 in the interim) has effectively been left unchanged. Section 3, Rulemaking Background, in the final analysis is the same as Section 3, Background, in the interim analysis. Sections 4 and 5, Motivation for Statutory Changes and Summary of Findings and Comparison of Final Analysis with Interim Analysis, respectively, are new to the final analysis. Section 7, Requirements for Regulatory Analyses, as Established by Regulatory Flexibility Act, is an expanded version of the corresponding section in the interim analysis (numbered 5 there) and now includes a discussion of comments received on the interim analysis. Portions of the analytic section were altered to ensure that the analysis accurately describes the two tier system established by the interim and final rules. Since most changes made by the final rule are minor, these changes did not effect significant changes to the analysis. However, three changes made by the final rule are worth noting because they change burden estimates. These changes concern sponsors' income documentation requirements for low-income children in tier II DCHs, requirements for State agency reviews of low-income documentation during States' reviews of sponsors, and the requirement that school food authorities (SFAs) provide sponsors with school attendance area boundary information.

The final rule attempts to mitigate sponsor burdens on income determination by allowing sponsors to establish the low-income status of a DCH enrolled child through official evidence, in the sponsor's or provider's possession, that the child's household participates in a Federal or State benefits program with an income eligibility limit not exceeding 185 percent of the Federal income poverty guidelines. This change reduces burden for sponsors by allowing them to establish eligibility for children for whom they have such information without having to contact the children's households to ask for evidence of low-income status.

The final rule also lessens review requirements for State reviews of sponsors' documentation for low-income children. The interim rule required States, as part of sponsor reviews, to verify that the income application (or other acceptable documentation) for every child classified by the sponsor as low-income is complete and supports the eligibility determination made by the sponsor. The final rule lessens the documentation review burden for States by requiring that States review at least 10 percent of all applications on file with a sponsor, where application refers to whatever documentation establishes the income-eligibility of a child. The final rule stipulates that States draw the 10 percent of applications from those DCHs the State must review as part of its sponsor review, but if those DCHs provide less than 10 percent of all applications, then States must draw additional applications until the 10 percent requirement is met.

The third change made by the final rule concerns provision of school attendance area boundary information. The interim rule assumed this information would be readily available, since it is public information and public schools are public institutions. A number of commenters told FCS that the information is not readily available. Boundary information is essential for sponsors to accurately determine whether a DCH should be approved for the higher meal reimbursement rates based on whether the DCH is circumscribed by the attendance area of a school with at least 50 percent of its enrollment approved for free or reduced price meals. The final rule, recognizing sponsors' critical need for this information, requires SFAs to provide boundary information on school attendance areas when sponsors request it. This represents a new burden for SFAs.

Responses to comments received on the interim analysis are located in Section 7, Requirements for Regulatory Analyses, as Established by Regulatory Flexibility Act. There was one quantitative change that resulted from the comments. The average wage rate assumed for sponsors, which was used to estimate the financial burden of tiering on sponsors, was increased. The interim analysis had assumed that a staff level employee would be responsible for performing the new burdens, but commenters caused FCS to reconsider that assumption. The final analysis assumes an average sponsor wage rate that is twice the figure used in the interim analysis, which reflects the new assumption that the tiering burdens will require involvement at the sponsor staff level up through sponsor management.

6. Cost/Benefit Assessment of Economic and Other Effects Benefits

The need to reduce overall Federal expenditures has prompted a review of many programs and led to the legislative decision to improve the targeting of CACFP benefits to low-income children. To accomplish targeting of benefits, the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 establishes two tiers of day care homes and reimbursement rates. Under tiering, any DCH located in a low-income area or operated by a low-income provider is eligible for tier I status, where low-income areas are determined by local school or census data, subject to

restrictions on how the data may be used. All meals served in tier I DCHs are reimbursed at the higher set of reimbursement rates. All DCHs not qualifying for tier I are tier II DCHs. Meals served in tier II DCHs are reimbursed at the lower set of rates, with the exception that meals are reimbursed at the higher set of rates when served to children whom the DCH sponsor documents as being low-income.

The initial establishment of the Child Care Food Program (CCFP) in November 1975 required both types of CCFP providers, day care centers and DCHs, to make individual eligibility determinations based on each participating child's household size and income. Meal reimbursement rates paid to sponsors for meals served in DCHs were based on each enrolled child's documented eligibility for free, reduced price or paid meals. In order to be a DCH, which denotes a CCFP participating home in this analysis, a home has always had to (1) meet State licensing requirements, or be approved by a State or local agency and (2) be sponsored by an organization that assumes responsibility for ensuring the DCH's compliance with Federal and State regulations (these licensing and sponsorship requirements are still in effect).

In the years following establishment of the program, concerns were raised that the paperwork and recordkeeping requirements were creating barriers to DCH participation in the CCFP. In 1978, Pub. L. 95–627 eliminated free and reduced price eligibility determinations for individual children in DCHs (but left unchanged day care centers' individual eligibility determination requirements), and established a single reimbursement rate for each type of meal served in DCHs (lunches/suppers, breakfasts, and supplements). These changes encouraged day care providers' participation in the CCFP by reducing their administrative paperwork burden. The Omnibus Budget Reconciliation Act of 1981 added the requirement of a means test for providers to claim reimbursements for meals served to their own children in care. With this sole exception, all DCHs continued to receive the same reimbursements for all meals served to children in care, regardless of each child's income.

The day care portion of the CCFP (The CCFP was renamed the Child and Adult Care Food Program (CACFP) in 1989 when an adult day care component was added.) has experienced dramatic growth in both DCH participation and Federal government costs. From fiscal year 1986 to fiscal year 1996, the number of participating DCHs increased from 82,000 to 194,000, an increase of 134 percent. During the same period, meal reimbursements in nominal dollars increased from around $190 million to about $750 million, a 280 percent increase.[2,3] Program growth has occurred primarily among non-low-income children: table 1 shows the proportion of low-income DCH participants decreased rapidly after individual eligibility determinations were eliminated in 1978. The table shows that the proportion of DCH children with household incomes below 130 percent of the Federal income poverty guidelines decreased by 33 percentage points between 1977 and 1982, by an additional 9 between 1982 and 1986, and by 5 more between 1986 and 1995. During the same periods the percentage of non-low-income children (above 185 percent of poverty) increased 46, 7, and 7 percentage points, respectively. Although the 1995 data was not available until after the interim rule was published, the marked growth in the proportion of non-low-income enrollment in DCHs between 1977 and 1986 was sufficient to serve as the impetus for Pub. L. 104–193's better targeting of DCH benefits to low-income children.

Table 1

Income Eligibility Status of Children in DCHs over Time

	Percent of DCH Children in Poverty Strata by Year(s)						
Percent of Poverty	1977[a]	1982[b]	Change Between 1977-1982	1986[c]	Change Between 1982-1986	1995[d]	Change Between 1986-1995
≤ 130 %	58 %	25 %	- 33 %	16 %	- 9 %	11 %	- 5 %
131-185 %	24 %	11 %	- 13 %	13 %	+ 2 %	10 %	- 3 %
≥ 185 %	18 %	64 %	+ 46 %	71 %	+ 7 %	78 %	+ 7 %
Total	100 %	100 %	N/A	100 %	N/A	100 %	N/A

[a] Percentages represent the proportion of meals served by category: free (to children from households with income ≤ 130 % of Federal income poverty guidelines), reduced price (131-185 % of poverty), and paid (≥ 185 % of poverty). Since most DCHs operating in 1977 were non-pricing, that is did not charge separately for each meal served, it is assumed children in care of different income strata have equal propensities to consume meals, which implies the proportion of meals served by category in 1977 is a reasonable proxy for children's income eligibility percentages (result assumes children eligible for free or reduced-price benefits generally became approved to receive them).

[b] *Study of the Child Care Food Program*[2] *cited data as being available from Evaluation of Child Care Food Program: Results of the Child Care Food Program: Results of the Child Impact Study Telephone Survey and Pilot Study.*

[c] *Study of the Child Care Food Program.*[2]

[d] *Early Childhood and Child Care Study (total does not sum to 100% due to rounding).* [1]

The 1986 *Study of the Child Care Food Program* (CCFP Study)[2] found that approximately 70 percent of the children enrolled in DCHs in 1986 were non-needy (i.e., they lived in households with incomes about 185 percent of Federal income poverty guidelines). The 1995 Early Childhood and Child Care Study (ECCCS), completed after the passage of Pub. L. 104–193 and publication of the interim rule, validated the potential for re-targeting; it found that in 1995, 78 percent of children enrolled in DCHs were non-needy. The establishment of a two tier reimbursement system offers the potential for re-focusing Federal child care benefits on children who are needy.

The two tier reimbursement rate structure is expected to effect significant Federal budgetary savings. The six year projected savings (fiscal years 1997–2002) are approximately $1.7 billion (see table 4). The savings would result from (1) a reduction in the reimbursement rates for meals served in tier II (non-low-income) DCHs and (2) a projected decrease in the rate of growth in the number of day care homes participating in the CACFP. The projected decrease in the rate of growth in the number of DCHs means the number of DCHs projected to exist in the future (under post-Pub. L. 104–193 CACFP conditions) is smaller than the number that were projected under pre-Pub. L. 104–193 CACFP conditions. Fewer DCHs produce savings by eliminating the meal reimbursements that would have been paid for meals served in the day care homes and by eliminating the administrative payments that sponsors would have received for sponsoring these day care homes (the tiering system leaves unchanged sponsors' per-home administrative reimbursement rates). The estimated savings assume that in fiscal years 1997–2002 approximately 45 percent of DCH meals will be reimbursed at the higher rates. The 45 percent assumption follows from the ECCCS finding that 38 percent of providers qualify for tier I based on income, as well as from assumptions concerning the number of providers eligible for tier I solely on the basis of their residing in low-income areas and assumptions about the number of documented low-income children enrolled in tier II DCHs (the 45 percent derivation is explained in detail near the end of Section 6, Area III, Part a, Tiering Determination Burden)

The reduction in reimbursement rates for meals served to children in tier II DCHs who are not documented income-eligible would result in savings of approximately $1.4 billion over the next six years (fiscal years 1997–2002). Rates for all meals served to these children—lunches/suppers, breakfasts, and supplements—would decrease as shown in table 2. The rate change would result in a savings of about $0.64 for every lunch or supper served during fiscal year 1998, the first full fiscal year in which the new two tier system will be in effect. The lunch/supper savings would increase to about $0.70 per meal by fiscal year 2002. Breakfast savings would range from almost $0.56 per meal served in fiscal year 1998 to $0.60 in fiscal year 2002, and supplement savings would range from about $0.35 cents in fiscal year 1998 to about $0.38 cents in fiscal year 2002.

Table 2

Changes in Tier II DCH Meal Reimbursement Rates Due to Tiering

		Projected Meal Reimbursement Rates[a,b]		
Fiscal Year	Meal Type	DCH Rates Before P.L. 104-193	Tier II DCH Rates After P.L. 104-193	Difference
1998	Lunch/Supper	$ 1.6175	$ 0.9800	-$ 0.6375
	Breakfast	$ 0.8850	$ 0.3300	-$ 0.5550
	Supplement	$ 0.4825	$ 0.1300	-$ 0.3525
1999	Lunch/Supper	$ 1.6600	$ 1.0100	-$ 0.6500
	Breakfast	$ 0.9050	$ 0.3400	-$ 0.5650
	Supplement	$ 0.4950	$ 0.1300	-$ 0.3650
2000	Lunch/Supper	$ 1.7000	$ 1.0300	-$ 0.6700
	Breakfast	$ 0.9275	$ 0.3500	-$ 0.5775
	Supplement	$ 0.5075	$ 0.1400	-$ 0.3675
2001	Lunch/Supper	$ 1.7425	$ 1.0600	-$ 0.6825
	Breakfast	$ 0.9475	$ 0.3600	-$ 0.5875
	Supplement	$ 0.5200	$ 0.1400	-$ 0.3800
2002	Lunch/Supper	$ 1.7875	$ 1.0900	-$ 0.6975
	Breakfast	$ 0.9700	$ 0.3700	-$ 0.6000
	Supplement	$ 0.5325	$ 0.1500	-$ 0.3825

[a] Reimbursement rates are established, in accordance with the National School Lunch Act, as amended, on a school year basis, July 1 through the following June 30. The rates shown are in effect three quarters of the stated fiscal year, October 1 through September 30 of the following year.

[b] Before P.L. 104-193 meal reimbursement rates were rounded to the nearest one-fourth cent. P.L. 104-193 changed the rounding rules to require that meal rates be rounded down to the nearest lower cent.

The growth of day care home participation in the CACFP is projected to slow as a result of the two tier rate structure, as some would-be providers are expected to perceive the program as offering insufficient financial incentive and/or being too administratively burdensome, relative to the financial benefits. A decline in homes' participation would cause a decline in the rate of growth of sponsor administrative payments and meals served (growth would persist, albeit at a slower rate). As shown in table 3, it is estimated that in fiscal year 1998, the first full year of tiering, 18 million fewer meals will be served than would have been served under the current reimbursement rate structure (due to a slower growth rate in day care home participation). The six year effect (fiscal years 1997–2002) of this projected decline in growth is a decrease in the number of meals served by 314 million, which is measured relative to the number projected under pre-July 1, 1997 reimbursement rates. The six year (fiscal years 1997–2002) projected savings from this slowing of program growth is approximately $300 million, measured in nominal dollars.

Table 3

Changes in DCH Meal Growth Rate Due to Tiering

	Projected Meals (In Thousands)[b]					
		After P.L. 104-193				
Fiscal Year	Before P.L. 104-193	Tier I	Tier II	Total	Difference (Total)	Percent Change
1997[a]	792,503	355,577	434,594	790,170	-2,333	- 0.3 %
1998	824,203	362,688	443,285	805,973	-18,229	- 2.2 %
1999	865,413	371,755	454,368	826,123	-39,290	- 4.5 %
2000	907,818	380,863	465,500	846,363	-61,455	- 6.8 %
2001	950,486	389,814	476,439	866,252	-84,233	- 8.9 %
2002	995,158	398,974	487,635	886,609	-108,549	- 10.9 %
1997-2002	5,335,581	2,259,671	2,761,821	5,021,490	-314,089	- 5.9 %

[a] Tiering did not become effective until the beginning of the fourth quarter (July 1, 1997) of fiscal year 1997.
[b] Fiscal year 1996, DCH data implies the average DCH served 20 breakfasts, 31 lunches/suppers, and 31 supplements during an average week.

Costs

The interim and final rules promulgate the two tier CACFP meal reimbursement system specified in Pub. L. 104–193. This system was designed to reduce Federal child care subsidies to providers and parents who are not low-income. Tiering will result in a projected $1.7 billion in Federal savings over the next six fiscal years through (1) lower meal reimbursement payment rates for non-low-income DCH providers and non-low-income children and (2) secondary savings stemming from the lower rates, including the decrease in the growth rate of the number of day care homes participating in the CACFP. The non-low-income providers will likely pass some of their revenue loss on to their clientele (primarily non-low-income parents) through higher child care fees. Non-low-income providers and parents will thus bear most of the costs resulting from the projected $1.7 billion reduction in Federal expenditures—as was the intent of Pub. L. 104–193. In addition to these fiscal costs, operating the two tier system will place new administrative burdens (costs) on DCH sponsors, State CACFP and State National School Lunch Program (NSLP) agencies, and NSLP school food authorities. The following analysis will show these administrative costs are minor in comparison with the costs to non-low-income providers and parents.

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Table 4

Federal CACFP DCH Costs Before and After P.L. 104-193

Projected Costs and Savings (In Thousands of Dollars)

Fiscal Year	Before P.L. 104-193			After P.L. 104-193					Change			
					Meal $				Total DCH $			
	Total DCH $	Total Meal $	Admin. & Audit $	Total DCH $	Tier I Meal $	Tier II Meal $	Total Meal $	Admin. & Audit $	$	%	Meal $ (%)	Admin. & Audit $ (%)
1997[a]	$ 916,721	$ 778,041	$ 138,679	$ 857,194	$ 348,985	$ 369,887	$ 718,872	$ 138,322	-$ 59,527	- 6.5 %	- 7.6 %	- 0.3 %
1998	$ 975,855	$ 830,493	$ 145,362	$ 728,653	$ 365,764	$ 220,352	$ 586,116	$ 142,537	-$ 247,203	- 25.3 %	- 29.4 %	- 1.9 %
1999	$ 1,047,984	$ 893,989	$ 153,995	$ 765,092	$ 386,428	$ 232,018	$ 618,446	$ 146,646	-$ 282,892	- 27.0 %	- 30.8 %	- 4.8 %
2000	$ 1,124,112	$ 960,650	$ 163,462	$ 798,085	$ 405,231	$ 244,080	$ 649,312	$ 148,774	-$ 326,026	- 29.0 %	- 32.4 %	- 9.0 %
2001	$ 1,203,792	$ 1,030,389	$ 173,404	$ 836,217	$ 425,250	$ 256,731	$ 681,981	$ 154,236	-$ 367,575	- 30.5 %	- 33.8 %	-11.1 %
2002	$ 1,289,588	$ 1,105,662	$ 183,926	$ 875,940	$ 446,130	$ 270,014	$ 716,144	$ 159,796	-$ 413,648	- 32.1 %	- 35.2 %	- 13.1 %
1997-2002	$6,558,052	$ 5,599,224	$ 958,828	$ 4,861,181	$ 2,377,788	$ 1,593,082	$ 3,970,871	$ 890,311	-$ 1,696,871	-25.9 %	- 29.1 %	-7.2 %

[a] Tiering did not become effective until the beginning of the fourth quarter (July 1, 1997) of fiscal year 1997.

The costs of tiering to DCH providers will be addressed first and followed by a discussion of costs to families whose children are in tier II DCHs. The new administrative burdens that tiering imposes on DCH sponsors will then be discussed and followed by an examination of the administrative costs for CACFP State agencies, NSLP State agencies, and NSLP school food authorities.

Implementation and use of the tiering system will have both one-time implementation costs and periodically recurring costs for the entities discussed above. The implementation costs will depend highly on the specifics of the State and local CACFP procedures currently in place and on which of the reimbursement options DCH providers choose and which of the claiming options DCH sponsors choose. For these reasons, implementation costs will vary greatly across States and localities. Because of the lack of information on these current practices, quantification of the implementation costs, within a reasonable degree of accuracy, is precluded. It is recognized that these costs may be significant, especially for State CACFP agencies (sponsors will need more technical assistance). The recurring costs are more evident and quantifiable, and what follows is a discussion of the recurring costs the affected entities will incur.

I. Costs to Providers

For CACFP providers the costs of tiering will have an administrative burden component, but will be primarily financial, due to the lower meal reimbursement rates, and will fall on providers operating tier II DCHs. Virtually all tier II DCHs will experience a decrease in CACFP reimbursements; the majority of the $1.7 billion in projected savings is due to lower reimbursements to non-mixed tier II DCHs (a mixed tier II DCH is a tier II DCH where at least one child in care is documented income-eligible; meals served to such children are reimbursed at the higher rates). Non-mixed tier II DCHs comprise an estimated 48 percent of all DCHs (see Costs to Sponsors for explanation). For the average non-mixed tier II DCH, the July 1, 1997 tier II rate decrease will cause weekly CACFP revenues to decline 50 percent, from $82 to $41,[3] which follows directly from the average DCH's weekly meal mix footnoted in table 3 and the meal reimbursements shown in table 2. Since the average DCH has an attendance of about 7 children [1] this $41 decrease ($82–$41) represents about $5.80 per child. Although this is a significant decrease, the $41 a week represents income that would have to be completely or nearly completely replaced by increases in child care fees if the day care home dropped out of the CACFP; therefore, the $41 is sufficiently attractive for most tier II providers to stay in the program and for new providers to continue joining.

a. Potential Tier II Provider Responses to Lower CACFP Reimbursements. Providers of tier II DCHs will most likely respond to decreased CACFP revenues through some combination of raising fees, absorbing the loss, recruiting low-income children, providing care for more children, and reducing operating costs. Studies of the day care market corroborate this. They find that in general providers will not try to pass all of the CACFP loss on to the families they serve,[4 5] but rather employ some of these other options as well.

The amount which existing non-low-income providers can pass on through higher fees will depend on the character of their local day care market. Tier II providers in markets that are competitive on the basis of fee will be discouraged from passing all of the loss on to parents, as they need to keep fees approximately in line with the local going rate to retain their customers.[5] Providers in less competitive markets, such as those where there is a child care shortage, will be able to raise fees and pass most of their loss along to parents. An example of a fee competitive market is one where there are several day care homes operating in a moderate income neighborhood, all having nearly equal appeal to parents and nearly equal fees, but with only a few of the homes being tier II DCHs (the rest being non-CACFP homes or tier I DCHs). Although the tier II DCH providers would be tempted to raise fees in response to the CACFP reimbursement rate decrease, the non-CACFP and tier I DCHs would probably leave their fees unchanged; their doing so may cause the tier II DCHs to leave their fees unchanged as well. Empirical data on the relative extent of these two market scenarios is unavailable. However, because the markets affected by tiering serve mostly non-low-income families who, if fees are raised, would probably choose to pay higher fees to stay with their current provider (i.e., they will pay what is necessary to secure high quality care), fee competitive markets may be the less common variety.

Data from the 1990 Profile of Child Care Settings Study [4] (PCCS) and the 1976 National Day Care Home Study [6] (NDCH) provide information on the likelihood that providers will respond to decreased CACFP reimbursements by absorbing the loss or providing care for more children. The PCCS and NDCH studies indicate that most tier II CACFP providers are not in a position to completely absorb a significant portion of the reduction in meal reimbursements and still make a profit. The 1976–80 NDCH study found that homes like DCHs (sponsored and licensed) do not make even moderate operating surpluses (profits)—the mean net hourly wage for providers in licensed, sponsored homes was $1.92 (in 1976 dollars), 83 percent of the 1976 minimum wage rate of $2.30 per hour (all DCHs are sponsored and licensed, but not all sponsored, licensed homes are DCHs, i.e., participate in the CACFP). The PCCS study suggests that providers' economic situation may have even worsened since the NDCH study: PCCS found that in real dollars, fees for licensed, sponsored homes decreased between the period 1976–80 and 1990. Thus, the PCCS data suggests that providers in sponsored homes, such as DCHs, do not have much of an operating surplus to buffer a cut in subsidies. Other PCCS findings indicate that most providers will not consider taking more children into care as a means of increasing revenues to offset the decrease in CACFP reimbursements. PCCS found that most providers of sponsored, licensed homes are operating near their legal capacity and that over half of all such providers surveyed indicated they are unwilling to take more children into care.

b. Most Probable Provider Responses to Lower CACFP Reimbursements. The PCCS and NDCH data, and the data suggesting that some day care markets may discourage the raising of fees [5] imply that in general tier II providers will respond to decreased meal reimbursements by reducing operating costs; absorbing a small portion of the decrease; and raising fees a modest amount, but will not respond by providing care for more children.

c. Effects on Non-Mixed Tier II Providers. Tier II providers who respond to decreased CACFP revenues by noticeably reducing operating costs or sharply raising fees may, however, only exacerbate their income shortage, as parents may be unwilling to accept the providers' decreased child care expenditures (reduced operating costs) or higher fees and could respond by moving their children to other providers, which would decrease the original provider's income until replacement children could be found. However, given that fees for DCHs (i.e., licensed and sponsored providers) tend to be higher than those found in unlicensed day care homes,[6 7] parents

who patronize DCHs have demonstrated a willingness to pay a premium for licensed care and are therefore less likely to be sensitive to an increase in provider fees.

The new reimbursement rates will have a significant economic impact on non-mixed tier II DCHs. Based on Food and Consumer Service (FCS) program data [3] and projected increases in the food at home series of the Consumer Price Index, when DCH reimbursement rates are first tiered on July 1, 1997 the weighted average per meal rate for non-mixed tier II DCHs will drop from the tier I level of $1.01 down to $0.50, a 50 percent decrease. The July 1, 1997 rate cut will cause the average non-mixed tier II DCH's weekly CACFP revenues to decline from $82 to $41, a $41 decrease (a 50 percent decline), where the average DCH serves an average weekly meal mix of 20 breakfasts, 31 lunches/suppers, and 31 supplements [3] to seven children.[1] These estimates incorporate the dynamic nature of the licensed day care market, where the annual provider turnover rate is approximately 20 percent: They assume that lowering the meal reimbursement rates will decrease the incentive for day care homes to join the CACFP and also increase the rate of departure for existing DCHs. Numerically, this translates into the expectation that the lower rates will cause the annual rate of growth in DCHs to decrease from just below 5 percent to just below 2.5 percent.

d. Effects on Mixed Tier II Providers. —Although minor in comparison with non-mixed tier II CACFP revenue decreases, tiering's actual meal count system will place a new administrative burden on some portion of the sub-group of mixed tier II providers (an estimated 10 percent of DCHs are mixed tier II) whose sponsors require them to use an actual meal counts system (some providers already keep such counts). There will be no new burden for providers whose sponsors opt for either of the ''simplified'' meal counts systems (as explained in the Costs to Sponsors, Sponsor Meal Claiming Burden section). In an actual counts system, the mixed tier II DCHs would provide the sponsor, for each child in care, the number of reimbursable meals the child was served, by meal type and would also identify each child by name. This reporting requirement represents an increase in burden over the current system where some providers only record and provide sponsors with the total number of reimbursable meals served, by meal type. Few DCHs are expected to incur this burden, however, as this system is burdensome for the sponsors; it is being assumed that only 5 percent of sponsors will choose an actual count system, and that in addition, all such sponsors will be small—serving no more than 50 DCHs, on average only 32 (see the Costs to Sponsors, Sponsor Meal Claiming Burden section). The estimated weekly provider burden associated with an actual count system in an average DCH (serving 7 children [1] and operating 5 days a week [1]) is 35 minutes, which assumes a burden of 1 minute per child per day. The estimated annual burden for such a home is therefore 29 hours. This translates into an annual fiscal impact of $154 per provider. This calculation assumes that providers of licensed, sponsored care are making about $5.30 per hour for their services ($5.30 is an inflation adjusted version of the NDCH study [6] finding that providers of sponsored, licensed homes earned an average of $1.92 per hour in 1976).

e. Effects of Tiering on Potential CACFP Day Care Home Providers. The two tier system may affect whether new day care home providers choose to participate in the CACFP. A provider who attempts to qualify for tier I based on provider's income must supply income data or other evidence showing the provider's household income is at or below 185 percent of the Federal income poverty guidelines before the sponsor can approve the DCH for tier I. While seemingly a simple requirement, anecdotal evidence from sponsors and State agencies suggests that some providers who previously claimed an income below 185 percent of the Federal income poverty guidelines (required to claim reimbursements for meals served to providers' own children in care) are withdrawing from the CACFP altogether over this requirement. This suggests that some providers who begin offering child care after July 1, 1997 (effective date of the two tier system) may also choose not to join the CACFP due to this requirement.

For potential CACFP providers who begin offering child care after July 1, 1997 and who never experienced the pre-Pub. L. 104–193 rates, the $41 per week (about $2,000 per year) available to an average unmixed tier II DCH will be seen as a welcome source of additional income, and many of these would-be tier II providers will join the CACFP. However, $41 is not as attractive as the pre-Pub. L. 104–193 level of $82, and it is therefore expected that new, would-be tier II providers will join the CACFP at a slower rate.

II. Costs to Families

Tiering imposes few costs on low-income families. One cost, limited to low-income families with children in mixed tier II DCHs, is their being asked to provide household income information. Although the families are not obligated to provide this information it is expected that most will. Providing this information consumes time and could lessen a family's privacy. Sponsors have the authority to verify the income information at a later time, in which case the family would be contacted and asked to submit supporting documentation for the income figures provided, representing a second burden and an intrusion on family privacy. Despite being authorized to conduct income verifications, few sponsors are expected to do so in light of the associated burden. As explained below, there may also be a limited number of low-income families with children in non-mixed tier II DCHs; these families will experience costs similar to those described below for non-low-income families.

Tiering is intended to reduce subsidies to non-low-income families, which as previously stated, is the intent of Pub. L. 104–193. The reduction has potential cost implications for these families. The Costs to Providers section explained that providers will likely respond to the decrease in CACFP reimbursements through some combination of reducing operating expenses, raising fees, and absorbing the loss. At one extreme of the day care market, an area not fee-competitive in which DCH providers have the freedom to increase fees to completely offset the reduced reimbursements, raising fees to offset the reimbursement cut would increase fees by about $5.80 a week per child. This would represent a 9 percent increase over the average weekly fees, $70, that parents of non-low-income children currently pay for care ($70 is an inflation-adjusted version of the CCFP Study's figure of $49).[2] At the other extreme of the day care market, a highly fee competitive setting, fees would remain unchanged. Although empirical data on the relative extent of these market types is unavailable, data from the Costs to Providers section suggest that the non-competitive market type may be more common: First, the markets affected by tiering are serving non-low-income families who, if fees are raised, would probably choose to pay the higher fees to stay with their current provider; and second, families patronizing DCHs, which tend to charge higher fees than unlicensed providers, have already demonstrated a willingness to pay more for the higher quality of licensed care.

a. Competitive Markets. In child care markets where providers need to hold

fees down to retain customers, providers are constrained to react to the rate decrease through some mixture of absorbing the cut and cutting operating costs. The providers being considered here are primarily those operating non-mixed tier II DCHs, the group that will experience the greatest tiering related CACFP revenue drop. To cut costs, these tier II providers may change their management practices relating to food service and developmental opportunities and materials, among other potential changes. Although intended as cost cutting measures, some of these changes could have effects on the children in care. In the area of developmental opportunities and materials, lower reimbursements may leave providers somewhat less able to afford the games, books, audio or video tapes, etc. that were attainable when CACFP reimbursements were covering a greater proportion of food expenses. There are also a number of areas in food service where providers could reduce costs, and these would impact children in tier II DCHs. One way to reduce costs would be deciding that certain snacks or meals served under the old, higher CACFP reimbursements will not be served under the new, lower rates, such as an afternoon snack. Providers might also respond by decreasing meal portions, although by specifying minimum serving sizes, CACFP regulations limit the extent to which this could be done. Other means of cutting food service costs could include replacing more expensive ingredients and food items with less expensive ones. While purchasing lower quality items and ingredients may have detrimental nutritional implications, substituting something more affordable could also represent a nutritional improvement if wise choices are made, i.e., purchasing an alternate, more affordable and more healthful combination of foods rather than purchasing a lower-quality version of the same food. The CACFP study mandated by Pub. L. 104–193 will compare the nutritional quality of meals served in post-tiering tier II DCHs with the quality of meals served in those DCHs before tiering, among other pre/post-tiering comparisons.

If a tier II provider decides to cut operating costs, a family may find the resulting conditions unacceptable and seek another provider. The search for a new provider entails costs in the time and potential for lost wages spent finding a new provider. There is also the potential for subsequent transportation and added inconvenience costs if the more suitable providers are not as conveniently located as the original caregiver (although they might also be more convenient). It is also possible that providers constrained to hold fees down will exit the child care market, which would also require a family to find another provider.

Under the fee competitive market scenario just considered, which primarily affects non-low-income families, there is the potential that some of the low-income children in mixed tier II DCHs will experience some of the same costs the children in non-mixed tier II DCHs will experience. Although some of the meals served in a mixed tier II DCH will be eligible for the higher reimbursement rates, others will not. If the provider is constrained to not raise fees to recoup the decreased reimbursements for the non-low-income families, the provider will experience a net decrease in revenue. As discussed above, the provider will likely respond to this net decrease by either reducing operating costs or absorbing the loss. Reducing operating costs would affect the low-income children in care. However, FCS believes only 10 percent of all DCHs will be mixed and that only a portion of these mixed homes are in competitive fee markets (where providers are constrained to keep fees down); under these conditions, few low-income children would be affected.

b. Non-Competitive Markets.—In the other child care market being considered, where providers are not as constrained to hold fees down, providers will likely respond to the rate decrease primarily through increased fees. As suggested earlier in this section, because tiering mainly affects non-low-income families who will likely choose to pay increased provider fees, this type of market may be more common than the competitive fee variety. In non-fee competitive markets, families can respond to increased fees by either paying the higher fees, moving their children to more affordable providers, or dropping out of the labor force (fully or in part) to care for their children. Each choice has different costs for families. In cases where the parents elect not to move the child, the parents will be assuming greater responsibility for food costs than under the previous system where the Federal Government was performing that function (the intent of Pub. L. 104–193). In the case where the provider raises fees enough to completely offset the reduced reimbursements, fees could increase by about $5.80 a week per child, representing a 9 percent increase over pre-tiering average fees.[2] In the second case, where the parents move a child to achieve lower fees, the child may have to break established relationships with the current provider and other children in care. The third alternative, dropping out of the labor force, would presumably occur rarely, as the raising of fees will primarily affect higher income families who will probably choose to absorb the increase.

c. Effects of Tiering on Child Care Choices.—Studies show that child care regulations enforce practices beneficial to childhood development,[6] but the preceding discussion on the relationship between lower meal reimbursements and higher fees implies that under tiering the number of families choosing sponsored, licensed care may decrease. The 1976–80 NDCH Study compared fees among unlicensed providers; licensed but unsponsored providers; and providers who are both licensed and sponsored. The study found that providers who are both licensed and sponsored had the highest fees. In the years since that study, fees charged by licensed and sponsored providers have decreased until equaling the fees charged by licensed but unsponsored providers.[4] This equaling of fees in licensed homes coincided with the post-1978 rapid growth of DCHs. CACFP reimbursements—-available only to sponsored, licensed homes—-may have played a role in bringing down fees charged by licensed, sponsored providers to equal fees of licensed, unsponsored providers, which suggests that tiering's lowering of CACFP rates may cause licensed, sponsored fees to rise. Even if the post-1978 decline in licensed, sponsored provider fees is attributable to other factors, it is likely (as discussed in the Costs to Providers section) that decreased CACFP reimbursements will cause licensed, sponsored providers to raise fees, at least in some markets, which may shift children into more affordable, possibly unlicensed homes. Similarly, the decreased CACFP reimbursements might cause some currently licensed and sponsored providers to consider moving out of licensed care. Therefore, the possibility that CACFP rates will no longer encourage the placement of children in licensed care is another cost that tiering may bring to non-low-income children and even some low-income children.

d. Intended Effect of Tiering.—An important fact is that tiering almost exclusively affects families with incomes above 185 percent of the Federal income poverty guidelines (non-low-income), as intended by Pub. L. 104–193. The only low-income families potentially affected by tiering will be those with children in tier II DCHs. This presumably encompasses few families,

as it is believed, as mentioned earlier, that (1) only 10 percent of all DCHs will be mixed (having both non-low-income and documented low-income children in care) and that only 30 percent of the children in an average mixed DCH will be low-income (see Tier II Household Income-Eligibility Determination Burden under Costs to Sponsors); and (2) that the clear majority of low-income children will be in tier I DCHs. Similarly, the providers affected by tiering will presumably be all non-low-income, since providers with incomes below 185 percent of the Federal income poverty guidelines are eligible for Tier I status. The Federal income poverty guidelines are designed to take into account family size, so that a given household will qualify for low-income status at a lower income level than will a household that has more children.

Although the reimbursement decrease for tier II DCHs is significant, the $41 a week in CACFP reimbursements that the average non-mixed tier II DCH would receive under tiering represents income that would have to be completely or nearly completely replaced by increases in child care fees if the day care home were to drop out of the CACFP altogether; therefore, the reimbursements available to tier II DCHs are sufficient for most tier II providers to stay in the program and for new providers to continue joining. These reimbursements will continue to assist providers with offering healthful, nutritious meals to participating children.

III. Costs to Sponsors

The two tier structure will impose several new administrative burdens on organizations that sponsor DCHs, including determining and documenting which DCHs and children are entitled to receive the higher set of reimbursement rates; verifying the income of all providers who qualify for tier I status based on provider income; determining which providers qualify for tier I based on area-eligibility; and collecting and reporting separate tier I and tier II meal, enrollment, and provider counts and other information on DCHs.

a. Tiering Determination Burden. All sponsors will be responsible for determining whether each of their DCHs is tier I or II. A sponsor can approve a DCH for tier I status if the DCH is located in a low-income area or the provider is low-income. A low-income area is defined as one in which the local elementary school has at least one-half of its enrollment approved for free or reduced price NSLP lunches, or an area in which at least one-half of the resident children are low income, according to the most recent census data.

The interim and final rules establish procedures for acceptable uses of census and school data when approving DCHs for tier I on the basis of geographic eligibility. The rules establish school data as the preferred data source. FCS prefers school data over census data because, in most cases, school data is more capable of accurately documenting current household income levels in an area. Because it is collected on an annual basis, school enrollment data more accurately measures current economic conditions of the current population, whereas significant changes can occur to an area's economic health (e.g., local recession or new employment opportunities) and the income levels of an area's population (through demographic shifts) between the times census data is collected. Since it is more representative of current income levels, establishing it as the preferred data source is necessary for consistency with the targeting goals of Pub. L. 104–193, which states that sponsors ''shall use the most current available data at the time of determination,'' where data refers to elementary school data, census data, and provider household income data.

Sponsors are to use school data to approve a DCH for tier I by area eligibility except when a school's attendance is primarily determined by something other than geographic proximity, which is true of most magnet schools and most schools in districts where substantial amounts of bussing takes place. When attendance is drawn in this manner, it almost always breaks the link between the percentage of enrollment approved for free or reduced price meals and household income levels in the school's attendance area, which makes school data inappropriate, in such instances, for making area-based tier I determinations. The final rule also directs sponsors to use census data for approving as tier I providers who reside in areas not circumscribed by school attendance areas. In all other efforts to classify DCHs for tier I by area-eligibility, sponsors must first use school data. If school data is used, but fails to support an area-based tier I classification, sponsors may then attempt to classify the DCH for tier I using census data if the DCH is either (1) circumscribed by a school attendance area where the school's free and reduced price enrollment is at least 40 percent of total enrollment or (2) circumscribed by a geographically large, rural school attendance area. Except for these two cases and situations where free and reduced price enrollment data does not reflect household income levels in a school's attendance area, sponsors must first receive State agency approval before using census data to classify DCHs as tier I by area eligibility. If a sponsor uses school data and determines that a DCH is located in an eligible enrollment area, but knows that some segments of that enrollment area are clearly non-needy—average income levels are well above the criteria for free and reduced price meals—then the sponsor must consult census data to determine whether the DCH operates in an eligible segment of the enrollment area before approving the DCH for tier I based on school data (eligible segment: census data show that at least 50 percent of the children live in households at or below 185 percent of the Federal income poverty guidelines). DCHs located in clearly non-needy areas within what are otherwise eligible attendance areas are not eligible for tier I via area eligibility.

FCS has attempted to establish procedures for the use of area data that meet the statutory requirements for low-income area data but do not place undue burden on sponsors and other involved organizations. State NSLP agencies will provide sponsors with lists of all State elementary schools in which at least 50 percent of enrollment is approved for free or reduced price meals (documented income below 185 percent of Federal income poverty guidelines). In addition, State CACFP agencies will provide sponsors with tabulations of census block group data showing the proportion of free or reduced price eligible children (income below 185 percent of Federal income poverty guidelines) in each block group. To determine attendance area boundaries for these 50 percent schools, sponsors may request attendance boundary information from the school districts, and school districts are required by the final rule to furnish the boundary information whenever boundaries exist for the schools in question. Sponsors must devise some method to determine which of their DCHs operate in eligible school attendance areas. Sponsors could do this by locating DCHs on a street map that also shows boundaries of eligible attendance areas; by telephoning the school district and being told by a school official whether a particular DCH is located in an eligible attendance area; by using geographic information systems software to create electronic street maps showing eligible attendance areas and DCH locations; or by any other means that allow a sponsor to independently determine whether a

DCH is located in an eligible attendance area. Although school boundaries may change during the 3 years of tier I eligibility following a school-data based tier I determination, and sponsors are to use the most recent boundary information when making determinations for DCHs just entering the CACFP and DCHs whose tier I eligibility status is about to expire, the final rule informs sponsors that in general, area-eligibility re-determinations should not be made when attendance area boundaries change during the 3 year eligibility period following a school-based tier I determination. Discouraging these re-determinations reduces sponsors' determination burdens and provides school-area approved DCHs a greater sense of predictability.

In the case of census data, sponsors can readily obtain block group boundary information from the U.S. census bureau in hard copy or electronic format. The methods that sponsors could use to demonstrate a DCH is located in a census-eligible block group are analogous to the methods described for school data. Census based determinations are valid until more recent census data becomes available.

A sponsor can also approve a DCH for tier I status if the DCH provider can demonstrate low-income status (i.e., income no more than 185 percent of the Federal income poverty guidelines). If a sponsor finds a provider to be low-income, the sponsor must verify the provider's household income before formally approving the DCH for tier I status. Sponsors must annually re-determine every Tier I eligibility determination based on a provider's income. Because verification of this kind is a non-trivial burden to sponsors, it is expected that whenever possible sponsors will approve providers for tier I on the basis of area eligibility. Area eligibility determinations offer sponsors the added benefit of being valid for three years when school data is used and until more recent data is available when census data is used, which would not exceed ten years.

The verification that sponsors will perform on income-approved tier I providers consists of obtaining pay stubs, tax returns, or some other form of independent income documentation to establish that the information provided on providers' tier I income applications is accurate. This type of verification is also known as ''pricing-program'' verification. The interim and final rules mandate this verification to protect the government against providers' financial incentive to qualify for tier I; the average tier I provider would receive 41 more dollars a week in CACFP meal reimbursements in 1998 than would the average non-mixed tier II provider (as was explained in the Costs to Providers section).

Collecting corroborating income documentation from providers for tier I income eligibility verifications represents an increase over pre Pub. L. 104–193 CACFP DCH application review requirements, which were established by the Omnibus Budget Reconciliation Act of 1981, Pub. L. 97–35. Pub. L. 93–35 eliminated CACFP DCH meal reimbursements for providers' own children in care, unless a provider submits an application demonstrating low-income status. Sponsors are not required to obtain supporting income information for these applications and typically make eligibility determinations based on the application information alone. Under the interim and final rules, providers will submit two types of income applications, which have different sponsor verification requirements. The first type will be submitted by providers seeking to qualify for tier I, so that, if approved for tier I, all meals served in the applying provider's home, including those to the provider's own children in care, would be reimbursed at the higher rates. The second type of application would be submitted by providers approved for tier I by area eligibility seeking to claim meals served to their own children in care. Pub. L. 104–193 does not supersede Pub. L. 97–35, so the requirement that a DCH provider demonstrate low-income status in order to claim meals served to the provider's own children remains in effect. For income applications for tier I status, Pub. L. 104–193 requires that pricing program verification (collection of substantiating income documentation) be performed. For applications from area-approved tier I providers seeking to claim meals served to their own children, sponsors will continue to approve these applications based on application content alone, which entails no new burden for sponsors.

Estimating sponsors' tiering determination burden requires first estimating the percentage of DCHs that are eligible for tier I based either on provider's household income or area-eligibility. The analysis does this by first estimating the percentage who are eligible on the basis of provider household income (and possibly also eligible on the basis of area) and then estimating the percentage of DCHs that are eligible on the basis of area exclusively. The ECCCS study, which was completed after the interim rule and analysis were published on January 7, 1997, finds that 38 percent of current DCH providers have household incomes low enough to be income eligible for tier I. Empirical data on the percentage of DCHs eligible for tier I on the basis of area alone is unavailable, as was the case for the interim rule. The figure used in this analysis, 4 percent of all DCHs, is comparable to the 6 percent figure used in the interim analysis.

The final rule's assumption that 4 percent of all DCHs are eligible for tier I by area, but not by income, like the 6 percent assumption in the interim analysis, is a consequence of the constraints imposed by (1) the percentage of meals reimbursed at the higher rates that will be consumed by documented low-income children in mixed tier II DCHs and (2) the percentage of providers eligible for tier I on the basis of income (and possibly area too). Constraint number 1 is considered first. The interim analysis assumed that few DCHs would be mixed tier II and, based on program knowledge, chose 10 percent of all DCHs as being mixed tier II. The interim analysis also assumed that 40 percent of mixed tier II DCHs' enrollments would be low-income. These two assumptions implied that documented low-income children in mixed tier II DCHs would consume nearly 4 percent of all DCH meals, which would all be reimbursed at the higher rates. The final analysis retains the 10 percent assumption, but assumes that 30, not 40, percent of mixed DCHs' enrollments will be documented low-income. The lowering of this percentage reflects the ECCCS finding that only 22 percent of the 1995 DCH enrollment is low-income, down from the CCFP study finding that 30 percent of the 1986 DCH enrollment was low-income. The preceding implies that documented low-income children in mixed tier II DCHs will consume about 3 percent of all DCH meals, which will all be reimbursed at the higher rates.

Having determined the contribution made by documented low-income children in mixed tier II DCHs to the percentage of total DCH meals reimbursed (and knowing they will be reimbursed at the higher rates), and also knowing the percentage of providers who are income-eligible for tier I (constraint number 2), the percentage of area-eligible, non-income-eligible tier I DCHs can be derived. The ECCCS finding that 38 percent of DCH providers are low income together with the higher reimbursement meals attributable to documented income-eligible children in mixed tier II DCHs imply that 41 percent of all DCH meals will be reimbursed at the higher rates. The only other DCH meals that will be

reimbursed at the higher rates are meals served in area-eligibility approved tier I DCHs with non-income-eligible. As stated above, the interim analysis assumed that 6 percent of all DCHs are area-eligible for tier I, but not income eligible. Given that the final rule assumes a higher proportion of DCHs will be income-eligible, the percentage of DCHs assumed area-eligible, but not income-eligible, has been reduced to 4 percent. Together with the income-eligible tier I DCHs and the documented low-income children in mixed tier II DCHs, the 4 percent implies that sponsors will be approving 42 percent of all DCHs for tier I and also that 45 percent of all DCH meals will be reimbursed at the higher rates.

Thirty-eight percent out of the 42 percent of DCHs that are eligible for tier I are eligible by income, but it is very likely that a substantial proportion of them (income-eligible) reside in low-income areas, which would make them area-eligible also. The burden of conducting pricing program income verifications on providers who apply for tier I on the basis of income and the interim rule's requirement that classifications based on providers' household incomes be re-determined annually will presumably cause sponsors to approve DCHs for tier I on the basis of area eligibility, rather than income, whenever possible. It was therefore assumed that one-half of the income-eligible DCHs will be approved for tier I on the basis of area eligibility rather than income (19 percent of all DCHs), which together with the 4 percent of tier I DCHs that are only area-eligible implies that 23 percent of all DCHs will be approved for tier I by area eligibility. The remaining one-half of tier I income-eligible DCHs, 19 percent of all DCHs, will be approved on the basis of income.

The dynamic nature of the DCH market will increase sponsors' tiering determination burdens. Data from the CCFP Study indicates the DCH market has an annual provider turnover rate of approximately 20 percent.[2] This volatility will lead sponsors to make more tiering determinations than would be necessary for a stable DCH population. See section e: Quantification of New Burdens for Sponsors for the quantification of sponsors' tiering determination burden.

b. Household Income-Eligibility Determination Burden on Sponsors. Meals served in tier II DCHs are reimbursed at the lower set of reimbursement rates. However, meals served to low-income children in tier II DCHs are eligible to be reimbursed at the higher set of rates, but sponsors must first document these children's low-income status before the higher rates can be claimed. The final rule provides tier II DCH providers who wish to secure higher meal reimbursements for low-income enrolled children (making the DCHs ''mixed'' tier II) two options for identifying them and documenting their low-income status. The interim and final rules direct sponsors to conduct all aspect of income-eligibility determinations and prohibits DCH providers from taking part, to protect the confidentiality of the household income information.

One option gives DCHs the opportunity to identify a portion of enrolled income-eligible children without ever asking the children's households to provide income information. Under this option, sponsors use whatever documentation they or their DCHs providers have on file that constitutes official evidence that a child's household participates in or is subsidized by a State or Federal benefits program with an income eligibility limit at or below 185 percent of the Federal income poverty guidelines. The other option supplements the preceding option's income determination activities with income applications sent to households of enrolled children. Under this option sponsors distribute income applications to households of the enrolled children for whom the sponsor lacks official evidence that the household participates in an applicable Federal or State benefits program. Tier II DCH providers receive the higher set of meal reimbursement rates for all meals served to children from households that complete the application, return it to the sponsor, and demonstrate on it that the household's income is at or below 185 percent of the Federal income poverty guidelines, as well as households for which official evidence exists documenting the households' income eligibility.

Sponsors must maintain supporting documentation for all children approved for the higher set of meal reimbursement rates. At least annually, sponsors must re-determine the eligibility of all children previously deemed income-eligible and also give all children previously deemed not income-eligible another opportunity to demonstrate low-income status. For the purposes of this analysis, it is assumed that sponsors will meet the annual re-determination requirement by cycling through each of their mixed DCHs once a year and making income-eligibility determinations on all children currently enrolled at that time. Sponsors must also make income-eligibility determinations for children who enter a mixed tier II DCH after the sponsor has made its annual income-eligibility determinations for that DCH. The schedule that sponsors will use to perform these latter income determinations is determined by the sponsor's choice of meal claiming system. Although it is providers who decide whether the sponsor must make income-eligibility determinations for enrolled children, sponsors decide which meal count system the sponsor and all its DCHs will use. The meal count system chosen determines the schedule on which income-eligibility determinations are made for children who enter mixed DCHs after the annual eligibility re-determination review has occurred. Sponsors can choose between an actual counts system and a ''simplified'' counts version. Each of these systems and its associated income-eligibility determination schedule is described below.

The final rule does not prescribe any additional income eligibility determination requirements, beyond annual re-determinations, for sponsors using an actual counts system. Rather, the provider's incentive structure under this system will determine the income-eligibility determination schedule used. In this system, providers of mixed tier II DCHs must report the number of meals served to each child by type and identify each child by name. Sponsors then use income-eligibility information to determine which set of reimbursements each child's meals are entitled to, with meals served to documented income-eligible children entitled to reimbursement at the higher rates. With reimbursements being determined on a per-child basis in actual meal count systems, providers of mixed tier II DCHs have the incentive to maximize the number of documented income-eligible children in their care. A provider can do this by directing its sponsor to make an eligibility determination on each new child upon the child's entering the provider's DCH. Assuming that most providers in actual count systems will behave in this manner, sponsors in these systems will be making income-eligibility determinations on an irregular, ongoing basis.

The final rule prescribes the income-eligibility determination schedule that sponsors employing simplified counting must use to determine the income-eligibility of children who enter mixed tier II DCHs outside the sponsor's annual income-eligibility determination cycle. The schedule requires that at least semi-annually, sponsors make income-eligibility determinations on all

children who enter a mixed DCH in the prior 6 months. Given that sponsors are already required to annually re-determine eligibility, sponsors using a simplified counting system will likely perform income-eligibility determinations twice a year: annual re-determinations at the beginning of the year and a second determination at mid-year for those children who entered a mixed DCH sometime in the preceding 6 months.

The two meal count systems will require sponsors to make near equal numbers of eligibility determinations; the burdens are expected to be equal. See section e: Quantification of Burdens for the burden estimates.

c. Data Collection and Reporting Burden for Sponsors. Tiering will place several new reporting requirements on sponsors. Sponsors will now have to annually collect and report to their State CACFP agency separate enrollment counts for tier I and tier II DCHs and an enrollment count for documented income-eligible children in mixed tier II DCHs (those DCHs serving at least one documented low-income child). Sponsors must also annually report the number of tier I and tier II DCHs they sponsor, as well as other information about their DCHs. Finally, in the management plan that every sponsor submits to its CACFP State agency, the sponsor will now have to include a description of how it will make DCH tiering determinations.

d. Sponsor Meal Claiming Burden. Under tiering, sponsors will have new burdens related to meal counting and claiming. Before tiering, sponsors were only required to claim meals by meal type (breakfasts, lunches, suppers, and supplements). Under tiering, sponsors will have to claim meals both by reimbursement category (higher/lower set of rates) and, within each category, by meal type. The claiming of meals served in tier I and non-mixed tier II DCHs remains straightforward. It simply entails separating claims submitted by tier I and non-mixed tier II DCHs, which amounts to categorizing the meals, and then, within each category, summing meal counts by type. In contrast, claiming for mixed DCHs requires that for each mixed DCH sponsors split out the meals by reimbursement category, which will typically be a more time consuming process than claiming for non-mixed DCHs. After the meals from mixed DCHs are separated by category, the meals are summed within each category by meal type. The method that sponsors use to split out mixed tier II DCH claims depends on whether the sponsor is using an actual or simplified meal counting system, as described below.

As previously noted, in an actual count system, mixed tier II DCHs record the number of meals served to each attending enrolled child, by meal type, and provide the sponsor with a claim that lists the meals served to each child by type and identifies each child by name. In such a system, the sponsor splits the meals into reimbursement categories by determining the appropriate reimbursement category for each child's meals based on the child's income eligibility status—-the reason each child is identified by name. In contrast, in a simplified count system, the sponsor splits the counts into the two reimbursement categories by applying either blended rates or claiming percentages to the provider's aggregated counts (both blended rates and claiming percentages produce identical fiscal claims). In the case of claiming percentages, a sponsor computes, for each DCH, the number of meals of each type entitled to the higher reimbursements by multiplying the total number of meals claimed of that type by the proportion of children in that DCH who have been determined income-eligible (the remaining meals are reimbursed at the lower set of rates). The procedure for blended rates is essentially the same. In simplified count systems, the semi-annual collection of income information described in section b: Household Income-Eligibility Determination Burden is used to update the claiming percentages/blended rates for each DCH at least every six months. The updated claiming percentages/blended rates reflect the proportion of income eligible children in the DCH.

Simplified counting is less burdensome to sponsors than an actual count system. Actual counts require the sponsor to compare the provider's meal claim against a list of the DCH's income-eligible children to identify which children's meals are entitled to the higher rate. The sponsor then groups meals by reimbursement category and finally, sums by type within each category to produce an aggregated count of meals by category and by type. In contrast, to reach the same result in a simplified system, the sponsor need only multiply the aggregate meal counts by the DCH's claiming percentages/blended rates. Because of the relative ease of meal claiming in a simplified counts system, it is expected that only 5 percent of all sponsors will opt for actual counts and that all will be small sponsors (serving no more than 50 DCHs). In response to the interim rule, several commenters mentioned that some State agencies already require their DCHs to operate actual count systems and suggested that sponsors in these States were constrained to opt for an actual count system. This is not completely accurate. The final rule prohibits States from mandating which meal count systems sponsors use, but at the same time does not infringe on States right to establish additional recordkeeping requirements for their sponsors and DCHs, provided those requirements do not conflict with Federal regulations. Even if a State requires its DCHs to maintain actual counts, a DCH's sponsor is not compelled to opt for an actual counts system; the sponsor could still chose a simplified count system. In this scenario the sponsor would either direct its DCHs to report meals by type and to retain the actual count records at the DCH, or allow the DCHs to submit their actual count records, in which case the sponsor, when preparing its claim, would simply disregard all information except meal totals by type.

e. Quantification of New Burdens for Sponsors. To quantify the effects of this interim rule on sponsors, the 194,000 DCHs [3] were distributed across the 1,200 DCH sponsors [3] according to previous studies of the CACFP, and current DCH program data. Doing this enables the scaling of burden estimates according to sponsor size (the number of DCHs a sponsor serves), which produces more precise burden estimates. The first step in creating this structure, was dividing the approximately 1,200 current sponsors into three groups, as shown in table 5: (1) Small sponsors which serve no more than 50 DCHs, on average about 32 DCHs; (2) medium sponsors which serve between 51 and 300 DCHs, on average about 220; (3) large sponsors which serve more than 300 DCHs, on average about 420.[2 3]

Table 5

Sponsor Characteristics

Sponsor Characteristics	Sponsor Size		
	Small	Medium	Large
% of all Sponsors	50 %	30 %	20 %
% of all DCHs Served	10 %	41 %	49 %
Average Number of DCHs Served per Sponsor	32	220	420
Number of Sponsors (Total = 1,200) in Category	612	360	228

Based on these definitions, 50 percent of all sponsors are small in size and account for 10 percent of all DCHs; 30 percent are of medium size and account for 41 percent of all DCHs; and 20 percent are large and account for 49 percent of all DCHs.[2 3] Next, based on DCH providers' and enrolled children's income data, from ECCCS and other assumptions discussed above under *Tiering Determination Burden*, it was estimated that 42 percent of all DCHs will be approved for tier I; 48 percent will be tier II, and 10 percent will be mixed tier II, as shown in table 6. Finally, it was assumed that 30 percent of sponsors will serve at least one mixed tier II DCH.

Table 6

DCH Characteristics

DCH Type	Percent of All DCHs
Tier I	**42 %**
Area Eligible Only	4 %
Income Eligible, Possibly Area Eligible[a]	38 %
Approved by Area	23 %
Approved by Income	19 %
Tier II	**58 %**
Mixed	10 %
Non-Mixed	48 %

[a] Analysis assumes that more than one-half of all income eligible providers are also area eligible.

The estimates for new sponsor burden are presented in table 7. Shown are estimates for the annual burden hours imposed on each sponsor category, and the percentage of sponsors affected within each sponsor category. Of the listed burdens, only *Meal Claiming* recurs periodically (monthly). The other burdens occur only once or twice a year (with the exception of household income determinations in an actual meal count system, but the number of sponsors involved is minimal, 5 percent of total, i.e., 60). The estimates make the assumption that economies of scale are realized only for *Meal Claiming* burdens, where the recurring nature of the burden would presumably give larger sponsors sufficient incentive to establish efficient meal claiming systems.

Table 7

Estimated Annual Sponsor Burden from Two Tier DCH System

Burden	Estimated Annual Sponsor Burden by Sponsor Size (Hours)			Estimated Percent of Sponsors Affected in Each Size Category		
	Small	Medium	Large	Small	Medium	Large
Tiering Determinations						
1. Low Income Providers (Includes Verification)	16 Hrs.	108 Hrs.	179 Hrs.	100%	100%	100%
2. Area Eligibility	6 Hrs.	43 Hrs.	72 Hrs.	100%	100%	100%
Tier II Household Income-Eligibility Determinations	12 Hrs.	55 Hrs.	110 Hrs.	20%	43%	37%
Data Collection and Reporting[a]	4 Hrs.	15 Hrs.	28 Hrs.	100%	100%	100%
Meal Claiming						
1. Actual Counts System (with mixed tier II DCHs)	23 Hrs.	N/A[b]	N/A[b]	10%	N/A[b]	N/A[b]
2. Simplified Counts System (with mixed tier II DCHs)	11 Hrs.	51 Hrs.	76 Hrs.	10%	43%	37%
3. No Mixed Tier II DCHs	6 Hrs.	25 Hrs.	38 Hrs.	80%	57%	63%

[a] Includes tier I, tier II, and tier II low-income enrollment counts; tier I and tier II DCH counts; and description of tiering determination method in sponsor management plan.

[b] Due to the burden associated with actual meal counts systems, it is expected that only small sponsors will choose actual counts.

The *tiering determinations* burden estimates were calculated using data from ECCCS, which indicate that 38 percent of all DCHs are income-eligible for tier I; the assumption that 4 percent of all DCH providers are non-low-income, but area-eligible for tier I; and the assumption that sponsors will choose to approve tier I income-eligible providers on the basis of area eligibility whenever possible. Thus, it is assumed that 23 percent of all DCH providers (one-half of the 38 percent who are income eligible plus the 4 percent who are only area eligible) will be approved for tier I using area eligibility information, while the remaining tier I eligible DCHs (19 percent) will be approved using provider income information. For the burden estimate, these percentages were assumed to hold for the average sponsor in each sponsor category so that, for example, the average small sponsor (serving 32 DCHs) with its 14.4 tier I homes would approve 7.9 of the 14.4 on the basis of area eligibility (14.4 * 23%/42%) and the remaining 6.5 DCHs on the basis of the provider's income (14.4 * 19%/42%). The estimates incorporate the dynamic nature of the DCH market, which has an annual provider turnover rate of approximately 20 percent.[2] This volatility will require sponsors to make more tiering determinations than would be necessary for a stable DCH population. Finally, the estimates for area eligibility assume that sponsors identify income-eligible DCHs using sponsors' preexisting knowledge of economic conditions in areas where DCHs reside and that sponsors are thereby able to easily identify DCHs lying far outside all income-eligible areas. This approach would allow sponsors to focus their efforts on DCHs with reasonable probabilities of qualifying for tier I by area eligibility. This analysis assumes such an approach will be taken and that the average sponsor will consider 3 homes for low-income area eligibility for every 2 it finds eligible and approves.

The *tier II household income-eligibility determinations* estimates were calculated by estimating the income-eligibility burden associated with the average DCH and then, for sponsors serving mixed tier II DCHs, multiplying that figure by the average number of DCHs administered by sponsors in each of the three size categories.[2 3] The number of children in care in an average DCH was used as the starting point for estimating the per-DCH burden.[1] This figure was then inflated to account for the fact that on average, there is a 30 percent turnover of children every 6 months in the average day care home.[8] This inflated figure represents the number of children whose households could potentially submit an application over a year's time. It is assumed that one-half of households would submit an application, and that of these households, one-third will be documented income eligible through official evidence possessed by the sponsor or provider, without having to submit the application. There is a clear financial incentive for providers to encourage their low-income families to submit income information to sponsors. This incentive and providers' close relationships with parents suggest that providers will attempt to persuade parents to provide the income information and achieve a high response rate.

The *data collection and reporting burden* was calculated assuming that the average sponsor will spend about 12 hours complying with the new

requirements in this area, with 10 of these hours for the new data related requirements and the remaining 2 for the requirement that each sponsor now provide a description of its plan for making DCH tiering determinations in its management plan. The 12 hour burden implies annual burdens of 4, 15, and 28 hours for small, medium, and large sponsors, respectively. These estimates are consistent with this burden being an expansion on the current CACFP requirement that sponsors report quarterly the number of DCHs served and the DCHs' enrollment and submit annually a sponsor management plan.

The *meal claiming* burden was calculated assuming that the *monthly* burden resulting from the new meal claiming requirements will be 2 hours for the average sponsor. This weighted average implies a burden that increases with sponsor size and the number of mixed tier II DCHs being served. The estimates shown in table 7 make the assumption that an actual counts system will impose twice the meal claiming burden of a simplified counts system due to the relative difficulty that sponsors using actual counts are expected to have in producing meal claims broken down by reimbursement category and meal type (relative to the effort required under a simplified counts system). The estimates further assume that among sponsors using a simplified count system, the average meal claiming burden for sponsors without any mixed DCHs will be about one-half the average burden for sponsors serving mixed DCHs. This assumption is consistent with the lower level of effort required to process meal claims from non-mixed DCHs. In addition, as described above, the estimates assume economies of scale so that the burdens are not directly proportional to the number of DCHs a sponsor serves.

Table 8 translates the burdens displayed in table 7 into fiscal costs. The fiscal costs were produced by assuming that the weighted average pay rates for employees responsible for performing the new sponsor burdens is $15.00 per hour.[9] The table implies that the annual increase in administrative costs due to tiering, for the average small, medium, and large sponsor, are about $600, $3,400, and $5,600 (in 1997 dollars), respectively. These costs represent about one percent of the total annual administrative payments the average small, medium, and large sponsor would receive from USDA (in 1997 dollars): $29 thousand, $158 thousand, and $266 thousand, respectively.

Table 8 [c,d]

Estimated Annual Sponsor Fiscal Cost from Two Tier DCH System

Burden	Estimated Annual Sponsor Fiscal Cost by Sponsor Size (In 1997 Dollars)			Estimated Percent of Sponsors Affected in Each Size Category		
	Small	Medium	Large	Small	Medium	Large
Tiering Determinations						
1. Low Income Providers (Includes Verification)	$240	$1,620	$2,685	100%	100%	100%
2. Area Eligibility	$90	$645	$1,080	100%	100%	100%
Tier II Household Income-Eligibility Determinations	$180	$825	$1,650	20%	43%	37%
Data Collection and Reporting [a]	$60	$225	$420	100%	100%	100%
Meal Claiming						
1. Actual Counts System (with mixed tier II DCHs)	$345	N/A [b]	N/A [b]	10%	N/A [b]	N/A [b]
2. Simplified Counts System (with mixed tier II DCHs)	$165	$765	$1,140	10%	43%	37%
3. No Mixed Tier II DCHs	$90	$375	$570	80%	57%	63%
Weighted Average Cost	$549	$3,387	$5,576	—	—	—
Average USDA Administrative Payments, Annual	$28,800	$158,400	$266,400	—	—	—
Wght. Avg. Cost as % of Admin. Payments	2.0%	2.1%	2.1%	—	—	—

[a] Includes tier I, tier II, and tier II low-income enrollment counts; tier I and tier II DCH counts; and description of tiering determination method in sponsor management plan.

[b] Due to the burden associated with actual meal counts systems, it is expected that only small sponsors will choose actual counts.

[c] The sponsor costs shown in table 8 equal the burden hours in table 7 multiplied by a wage rate of $15.00/hour, as described in th text.

[d] The wage rate of $15.00/hour responds to comments on interim rule and is about twice the rate used in the interim analysis. See section 6 for complete explanation. This change approximately doubles the figures relative to the interim analysis.

IV. Costs to CACFP State Agencies

The costs to CACFP State agencies consist of their being required to provide sponsors with low-income area eligibility data; increased requirements for sponsor reviews, particularly auditing sponsors' documentation for approved income-eligible children; and State agencies' obligation to provide sponsors with technical assistance. In terms of area eligibility data, State agencies will be responsible for providing (1) census data identifying all State census blocks where at least 50 percent of the children are from low-income households and (2) an annually updated list of all State elementary schools that have more than 50 percent of their enrollment certified to receive free or reduced-price lunches under the NSLP. The agencies' other responsibility relating to area eligibility data is deciding when to authorize sponsors to use census data to make area eligibility based tier I classifications. The final rule states that when sponsors make area-based tier I classifications, they must first attempt to make the classification using school data, except when school enrollment patterns are not based on geographical proximity, in which case sponsors must make area-eligibility determinations using census data. If a home does not qualify for tier I based on school data and a sponsor wishes to use census data, the sponsor must first receive approval from the State agency, unless the attendance area-bounding the DCH belongs to a school with at least 40 percent of its enrollment approved for free or reduced price meals or a school with a geographically large rural attendance area. In these two special cases, sponsors may approve DCHs for tier I through census data if the school data does not support such a classification, otherwise sponsors must first receive approval from their State

agency before using census data to approve a DCH for tier I.

For the average State CACFP agency, it is estimated that the obligation to provide sponsors with elementary school data annually and census data as it becomes available represents an average annual burden of 25 hours, which assumes each instance of data transmittal and subsequent follow-up takes 1 hour. This estimated burden is equivalent to $450, which assumes a wage rate of $18 per hour, which is based on information in States' plans for State Administrative Expense funds and FCS-conducted State Management Evaluations.

Tiering will also increase State agencies' sponsor review requirements. The final rule requires that as part of their sponsor reviews, State agencies review the documentation sponsors used to deem children in tier II DCHs income-eligible as well as the documentation sponsors used to approve providers for tier I on the basis of income. State agencies are responsible for ensuring that application forms are completed correctly; that the stated income on each falls below 185 percent of the Federal income poverty guidelines; that proffered documentation of participation in a Federal or State benefits program represents ''official evidence'' of participation in a qualifying program; and that the incomes of income-approved tier I providers were properly verified. State agencies are given the option of performing ''pricing program'' verifications on all income documentation, but it is expected that very few will do so because of the significant time required to conduct such verifications. The agencies are also responsible for ensuring that sponsors used the most current data available for making area eligibility determinations, but are not required to independently verify the determinations. For the average State CACFP agency, it is estimated that performing these reviews amounts to an annual burden of 63 hours, with some States expending much less than this amount and others much more, depending on the size and number of sponsors in the State. This estimated burden is equivalent to $1,134, which assumes a wage rate of $18 per hour.

State CACFP agencies will likely see an appreciable increase in their training and technical assistance burden as the transition to the new two tier system is made. Under the new system, State agencies will have to provide new guidance and training on all new aspects of CACFP introduced by tiering, for example, DCH tiering determinations, new meal counting and claiming procedures, and new data reporting requirements. This burden will likely persist for the first several years the new system is in place. It is believed that the new training and technical assistance burdens represents about 10–20 hours of new burden per sponsor per year for a State agency. For the average State, this implies an annual burden of between 230 and 460 hours (between $4,140 and $8,280) for the first several years of tiering and presumably abating thereafter. The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Pub. L. 104–193) provides some funds to help State CACFP agencies make the transition. It directs the Secretary of Agriculture to set aside $5 million of fiscal year 1997 CACFP funds for one-time grants to State CACFP agencies. These grants must be used to aid States, sponsors, and DCHs with making the transition to the new system. Pub. L. 104–193 allows each of the 54 State agencies to retain up to 30 percent of its total grant for State agency use. If all States agencies retained the maximum allowable, a total of approximately $1.5 million would be retained at the State level, with the remaining $3.5 million going to DCHs and their sponsors.

The interim rule added a new requirement to the management plans that sponsors must submit annually. Now, each sponsor must describe the approach it will use to make DCH tiering determinations. Reviewing this component of the plan will presumably place minimal additional burden on the State agency.

There is the potential that in some States the decreased CACFP reimbursements will lead to an increase in the State-wide average fee charged by providers. This increase may have the effect of increasing State expenditures for subsidized child care, as a State's subsidized care payments are often based on the average fee that providers in the State are charging. Being unable to predict a numerical value for the effect the reimbursement rate cut will have on provider fees, as discussed previously under Costs to Providers, quantifying this potential cost to States is precluded. Neither the final nor the interim rule directs States to increase payments for subsidized child care.

V. Costs to NSLP State Agencies and NSLP School Food Authorities

Under Pub. L. 104–193, State NSLP agencies are required to annually provide a list of all State elementary schools in which at least 50 percent of the enrollment is certified to receive free or reduced-price NSLP lunches. However, these agencies do not currently collect school-level information. NSLP School Food Authorities (SFAs), which are generally school districts, are the only entities other than the schools that collect this data. SFAs are also more able than schools to provide the data to the NSLP State agency. The interim and final rules accommodates this situation by directing SFAs to inform their State NSLP agency of the elementary schools that have at least 50 percent of their enrollment certified to receive free or reduced-price NSLP lunches. It is estimated [10] that roughly 5,000 SFAs will contain the approximately 11,000 elementary schools meeting this criterion, and that the annual average reporting burden on an SFA will be roughly 1.5 hours ($12). The NSLP State agencies will receive the lists of elementary schools from their SFAs, compile and presumably do basic error checking on them, and pass the compiled listings on to the State CACFP agencies. It is estimated that the average NSLP State agency burden associated with this work will be 2.5 hours ($45) annually, using State CACFP agency wage assumptions.

The final rule also requires SFAs to provide sponsors with attendance area boundary information for elementary schools where at least 50 percent of the enrollment is certified eligible for free or reduced price meals. The requirement applies only to schools with defined attendance areas, which excludes magnet schools and all other schools in which attendance is not determined by geographic proximity. It is assumed that, on average, each of the roughly 5,000 SFAs with at least one elementary school having at least 50 percent of its enrollment approved for free or reduced price meals will receive 2 requests annually for attendance area boundary information and that the average time to meet each request will be 2 hours, for an annual burden of 4 hours per SFA ($60, using the table 8 wage assumptions).

Comparison of Costs and Benefits

The analysis presented here finds that the DCH tiering structure established by Pub. L. 104–193 and promulgated by the interim and final rules will partially accomplish its objective of targeting Federal child care benefits to low-income children. This targeting will save a projected $1.7 billion in Federal tax revenues over the next 6 years (fiscal years 1997–2002). Non-low-income providers (tier II DCHs providers) and non-low-income families with children in tier II DCHs will bear most of the costs resulting from the Federal

government's $1.7 billion savings. Non-low-income households served by tier I DCHs will be unaffected by tiering. It is possible that some low-income families with children in tier II DCHs may bear some of the costs, but States may offset them by opting to increase child care subsidies. The analysis further finds that while targeting will place new administrative burdens on sponsors, State CACFP and NSLP agencies, and NSLP school food authorities, these burdens are relatively modest.

7. Requirements for Regulatory Analyses, as Established by Regulatory Flexibility Act

The Regulatory Flexibility Act (Pub. L. 96–354) establishes requirements for analyses of regulatory actions that are expected to have a significant economic impact on a substantial number of small entities. Public Law 96–354 was enacted at the urging of small businesses after repeated claims that uniform application of regulations regardless of business size was disproportionately damaging to small entities. It is expected that this rule will have an economically significant impact on tier II DCH providers due to the large decrease in reimbursement rates for meals served in those DCHs. This rule will also affect sponsoring organizations, considered to be ''small organizations'' by Public Law 96–354, although the economic impact on them is expected to be much less than the effect for DCHs.

The specific effects for sponsors and tier II providers were discussed under the Costs to Providers and Costs to Sponsors sections under the Cost/Benefit Assessment of Economic and Other Effects. The interim and final rules implement, to comply with statute and to meet the statutory intent of targeting benefits, the programmatic changes mandated by the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Public Law 104–193). The rule's only economically significant impact is the decreased meal reimbursements for meals served in tier II DCHs. The Food and Consumer Service (FCS) cannot mitigate this effect other than by making targeting less accurate, which would be contrary to the spirit of Pub. L. 104–193. The only other class of small entities affected by this regulatory action is sponsors. The final analysis finds that the costs sponsors will incur in meeting the new program requirements established by the interim and final rules will be about two percent of the payments each sponsor receives from FCS for operating the CACFP in its DCHs. This implies that the rules' economic impact on sponsors is generally not significant and that in the few areas where FCS had discretion, its choices strike an appropriate balance between adhering to Public Law 104–193's intent to target benefits and making realistic demands of sponsors.

Public Law 96–354 mandates that the analyses contain ''a summary of the significant issues raised by the public comments in response to the initial regulatory flexibility analysis, a summary of the assessment of the agency of such issues, and a statement of any changes made in the proposed (final) rule as a result of such comments.'' Six commenters addressed the interim analysis. The preponderance of their comments fall into four categories: They think the assumption that 10 percent of all DCHs will be mixed tier II is too low; they disagree with the conclusion that the total new costs imposed on sponsors by tiering will be less than one percent of the administrative funds the sponsors are paid in a year by FCS; they disagree with the description of tier II providers' likely responses to lower rates and the ramifications of those actions; and they disagree with the assumption that only small sponsors will use actual meal count systems. These areas, plus comments falling outside them, are considered in turn below.

Five commenters said the analysis underestimated the number of mixed tier II DCHs, basing their assertions on their own experience as DCH sponsors. They said the underestimation led FCS to underestimate sponsor burdens associated with mixed tier II DCHs. FCS has previously stated that there are no data on which to base an estimate of the percent of DCHs nationwide that will be mixed tier II. FCS does not believe it is appropriate to alter its assumption based on a very limited number of commenters whose own experience in particular geographic areas suggest that the 10 percent mixed tier II assumption is too low and who did not substantiate their claims with empirical data. It is possible that those whose experience is most at odds with the analysis would be the most motivated to submit comments expressing their disagreement, and that the experiences of other sponsors might suggest that the 10 percent assumption is either generally appropriate or too high. FCS recognizes that effective program administration requires empirical data on the number of mixed tier II DCHs and is currently working with the States to obtain that data.

Four commenters indicated the analysis underestimated the total costs of tiering imposed on sponsors; the interim analysis found that total new costs would be approximately 1 percent of the total administrative payments sponsors receive from FCS during a year. The 1 percent figure is the sum of several new costs imposed by tiering. FCS divided the new burdens/costs imposed on sponsors into four categories. For each category, FCS estimated to the best of its ability—using study data, program data, and program knowledge—the burdens/costs which that category of new burdens/costs would impose on sponsors. After these estimates were completed, FCS decided the new burdens needed to be compared to some metric to assess the relative magnitude of the total new burden. It was decided to compare the sum of the new burdens to total annual administrative payments made to sponsors, which produced the 1 percent figure contended by the commenters. FCS did not assume the new burdens would amount to 1 percent, rather the 1 percent was the mere summation of several calculations, each to estimate the new burdens/costs in a particular category. Since commenters asserted that 1 percent is too low, without being more specific as to what aspects of the intermediate calculations (burden calculations) are perceived to be deficient, FCS has decided to retain the burden estimation procedures used in the interim analysis. FCS did re-consider the wage rate used for employees of DCH sponsors. Data obtained from sponsors [9] suggest that the $8 hourly rate used in the interim analysis is too low, and that an hourly rate of $15 is more appropriate, which is used in this analysis.

Three commenters were dissatisfied with the discussion of how tier II providers may respond to the lower reimbursement rates and the consequences of their response. One commenter argued that the analysis was wrong in saying that tier II providers may decrease expenditure on ''non-essentials'', such as books and games, because these items are essential for childhood development. FCS was not making an evaluative statement on the materials necessary for providing a developmentally appropriate child care environment, but rather suggesting that some providers may view such items as non-essential in order to cut costs and stay in operation. The same commenter argued that tier II providers are not capable of absorbing a decrease in meal reimbursement rates. FCS agrees that there would be little profit left if the provider absorbed the total loss; however, some providers whose income is not limited to child care may be in a position to absorb a rate cut and may

choose to do so. Finally both commenters took issue with the statement that healthier food could be obtained for less money. The commenters appear to have misinterpreted a statement in the analysis which said that with decreased tier II meal reimbursements, providers may choose to buy lower quality food whereby the nutritional quality of the provider's meals would suffer, but that it is also possible for a provider to change the types of foods purchased and buy foods that are less expensive and of a higher nutritional quality than the more expensive foods purchased previously. The comments interpreted the statement as saying meals of higher nutritional quality can be obtained by purchasing cheaper, lower-quality foods. Rather, FCS believes that higher meal cost does not always result in more nutritious meals.

Two commenters expressed their belief that the interim rule is incorrect in assuming that only small sponsors will choose actual meal count systems because some States require sponsors to collect actual meal counts from DCHs. Under the interim and final rules, States may require that DCHs keep actual counts and may require that DCHs provide these counts to their sponsors, but States are prohibited from directing their sponsors to use an actual counts system, which means States cannot direct their sponsors to calculate reimbursement amounts according to DCHs' actual meal count records and the documented income-eligibility status of each enrolled child. If a sponsor chooses a simplified count system and is in a State that requires DCHs to submit actual counts to their sponsors, the sponsor would calculate mixed tier II DCH reimbursements by applying either claiming percentages or blended rates to meal count totals by meal type. FCS has no evidence that an appreciable number of medium and large sponsors would choose to self-impose the additional burden associated with actual counts when, compared with simplified count systems, actual counts do not reduce the probability of sponsors making reimbursement calculation errors; do not produce, over time, higher payments to DCHs; and do not allow providers to calculate the reimbursement they are due with any greater accuracy. Therefore, this analysis retains the interim analysis's assumption that an insignificant number of medium and large sponsors will opt for an actual meal count system.

In response to the six comments received on the initial regulatory flexibility analysis, FCS has made no changes to the final rule. However, FCS has made changes to the analysis in response to public comment, including changing the labor wage rate assumptions used to calculate the costs associated with the new sponsor burdens. Furthermore, FCS recognizes the need to obtain empirical data on the number of mixed tier II DCHs in operation and on the characteristics of sponsors using actual counts systems.

The Pub. L. 96–354 also requires that the final analysis estimate the types of professional skills necessary to meet the final and interim rules' reporting and record keeping requirements. The new reporting and record keeping required by this rule require no skills beyond those necessary for current program reporting and record keeping requirements.

Pub. L. 96–354 further requires that analyses describe the steps taken by the promulgating agency to minimize the economic impact on small entities. Specifically, the ''analysis shall also contain a description of the steps the agency has taken to minimize the significant economic impact on small entities consistent with the stated objectives of applicable statutes.'' There are no significant alternatives available to FCS that both (1) accomplish the stated objectives of Pub. L. 104–193 and (2) minimize any significant economic impact on small entities. FCS has attempted to adapt the rules based on comments received in response to the interim rule. Changes made by the final rule to the interim, in response to comments, were described in the section title *Summary of Changes to Interim Analysis.* All three reduce burdens; two reduce burdens on DCH sponsors, and the third reduces burdens for State CACFP agencies. All three changes should make the two tier system easier to implement and administer. In addition, the preamble to the final rule provides an in-depth discussion of how the final rule reflects the comments received on the interim rule.

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