

# Underwriting Child Care Centers

## An Overview

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Low Income Investment Fund

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# Revenues

- Child care revenue rates vary greatly
  - Quality of child care provided
  - Age of the child being cared for (infants most costly)
  - Location of the program and local market
  - Needs of the child (special needs children higher)
  - Income of families served

# Typical Revenue Sources

- Parent Fees/ Tuition
  - Study the history closely
  - Influenced greatly by location & local market
  - Target population critical
  - Late payments and bad debt a critical factor
  - Vacancy rates critical-- despite what borrower says
    - Adjust if expansion planned

# Contracts (Center Based Subsidies)

- Direct contracts to child care centers
  - Typically set annual amount, renewed 1 – 3 years
  - Limited income eligibility
  - Can be split between multiple sites
  - Pro-rated to children served
  - New contracts, if any, very competitive
  - Parents may share in cost
  - Waiting lists may prioritize certain families

# Contracts (Head Start)

- Head Start- direct contracts
  - Negotiated based on cost, set annual amount
  - Payment for making services available
  - Significant standards & administration
  - New contracts, if any, very competitive
  - Income eligibility very low
  - May be combined/wrapped around other funding
  - Debt service allowed as part of contract
  - Capital dollars available on a competitive basis

# Voucher (Parent Based Subsidies)

- Used for all types of care (exempt, family, center)
- Vendor payment to provider
- Maximum payments based on rate ceiling for area
- Provided on a reimbursement basis
- Majority of welfare to work dollars in vouchers
- Often contingent on continuing eligibility and performance of family

# Note About Subsidies

- Income eligibility requirements differ
- For example, a family of 4 in CA
  - \$18,100 per year Head Start (federal poverty)
  - \$39,000 per year subsidized center or voucher (75% of state median income)
- Note: may be significantly lower than housing subsidy levels, especially in high cost areas
  - \$54,900 for 60% or area median income in SF

# Child Care and Adult Food Program

- Administered by US Dept. of Agriculture
- Capped, tiered reimbursement for meals & snacks meeting nutritional standards
- Eligibility determined by:
  - Location
  - Children served
  - Organizational status
- Providers often forget to show this revenue

# Other Public Funding

- There are a range of other potential public sources for core child care services or enhancements provided in the form of vouchers or contracts
  - Special Needs Children
  - Homeless children & families
  - Mental or primary health consultation
  - Social services
  - Staff compensation or development

# Fundraising

- To meet base expenses and/or boost quality
  - Foundations
  - Corporations
  - Events
  - Individual Donors
- Scrutinize track record & competition
- Analyze capacity of development staff
- Beware of the impact of capital campaigns on operating fundraising

# Transportation

- Fees for transporting children typically on per ride basis
- Frequently used for community based after school programs
- Break out corresponding expenses to understand profitability

# Revenue Considerations

- Discount projections, rarely assume more than 90% enrollment & collections
- Craft a conservative, monthly phased ramp-up
- Government reimbursements take 30 -90 days
- January and September are critical months for starting or expanding
- Don't count second and third shift revenues

# Revenue Considerations

- Economies of scale and ratios are an issue
- Serving an age range can be risky, but lucrative
- The more diverse the better
- Scrutinize each source closely for
  - Trends
  - Future risks
  - Local environment
  - Contingency plans

# Expenses

- Child care expenses vary greatly due to several factors
  - Location of the program and regional costs
  - Quality of child care provided
  - Age of the child being cared for (infants most costly)
  - Needs of the child (special needs children higher)

# Expense Rules of Thumb

- **Payroll 55% - 80%**
  - Very labor intensive sector
  - Enriched programs tend to have more staff
  - Recruitment costs should be budgeted on-going
- **Occupancy 8% - 25%**
  - Utilities tend to be high
- **Food 4% - 10%**
  - Full day programs have higher costs
- **Materials/Supplies, Professional Dev. 1% - 6%**

# Expense Notes

- Subsidy sources for food or care do not always meet the full cost , especially in high cost areas
- Analyze expenses as fixed (rent,mortgage, insurance) and variable (staff, food) to determine a break even enrollment, especially for new or expanded programs
- Economies of scale and ratios are a factor

# Factors Impacting Cashflow

- **Child care margins are thin so small changes can have big impacts**
  - Number of children enrolled
  - Days of attendance
  - Collections (receipt & timing)
  - Unplanned increase in expenses (energy crisis or worker's comp)
  - Employment trends in immediate area
  - Fundraising fluctuations and competition

# Case One: San Jose Day Nursery

- Experienced nonprofit corporation
- \$433,000 construction loan converting to a \$275,000 mini-permanent (10 term/20 amortization)
- 1<sup>st</sup> Trust Deed (27% LTV as is, 12% proposed)
- 40 new slots, 100 enhanced for moderate and low income families

# Development Budget Rules of Thumb

## General Information

- Development costs vary greatly by location, type of program, ages to be served
- Few comps are available
- Lots of finishes, fixtures and necessary equipment make child care expensive
- Durability critical—kids are hard on buildings!

# Development Budget Rules of Thumb

## Predevelopment

- Environmental due diligence
- Permits, fees and consultation with licensing & fire marshal

## Hard Costs

- Note grading, undergrounding, utilities for portables
- Playground structures, rubber matting are costly
- 10 - 15% contingency recommended

# Development Budget Rules of Thumb

## Landscaping

- Can be significant for play areas

## Equipment & Supplies

- Adequate, age appropriate equipment & materials must be in place prior to opening

## Relocation

- Account for costs of moving twice, rent
- Account for lost income for days of move(s)

# Development Budget Rules of Thumb

## Staffing

- Some staff on board before opening

## Working Capital/Start Up

- 3 months operating must be on hand to cover expansion or new program

## Project Managers/Consultants

- Strongly encouraged

# Development Budget Rules of Thumb

## Marketing & Enrollment

- Typically under budgeted by providers
- Standard and alternative methods work
  - Business cards, advertising, signs, brochures, flyers, yellow pages, website
  - Church bulletins, doctor's offices, playground bulletin boards, automobile signs, newspaper articles, public speaking