Family and Childcare Trust
Creating a family friendly UK

Call for evidence: review of the cost of providing childcare, Family and Childcare Trust response

Key messages

The Family and Childcare Trust welcomes the Government's decision to review and increase early education funding. Childcare is central to key Government priorities, including improving developmental outcomes for the most disadvantaged children and supporting families to work, and has rightly been the subject of rising investment and several new policy initiatives in recent years. By reforming early education funding, the Government can take a significant step towards aligning the current funding framework with its policy aims.

This response sets out evidence on the cost of high quality care and detailed recommendations. Broadly, we recommend that:

- The benchmark for assessing the reasonable cost of childcare should be the cost to providers of delivering high quality care that supports good developmental outcomes for children and closes the gap in outcomes between the most disadvantaged children and the rest.

- The Department for Education should align the funding framework for free early education with this goal, ensuring that all providers are properly funded to deliver high quality care.

- The Government should use the opportunity presented by significant new investment in childcare over the next two years through free early education, tax-free childcare and Universal Credit to simplify the childcare funding system. To achieve this aim, the Government should establish an independent commission on childcare funding to make recommendations on funding reform and long-term investment.

We have also responded separately to the call for evidence in partnership with Every Disabled Child Matters, Contact and Family and the Special Educational Consortium to set out evidence on childcare costs for children with special educational needs and disabilities.

The cost of high quality childcare

The basis for an assessment of the reasonable cost of childcare should be the cost of delivering high quality care. Ofsted highlighted in its most recent early years annual review that, whilst there are examples of successful services, early years provision is failing to close the gap in outcomes in the first five year between the most disadvantaged children and the rest.[1] We believe that this is because the free early education that is being delivered to children too often does not have the characteristics needed to close the developmental gap. Several recent evidence reviews summarise key characteristics of early care and education that has the greatest impact on children:[2]

[1] Ofsted (2015) *The report of Her Majesty's Chief Inspector of Education, Children's Services and Skills 2015: Early years*. Manchester: Ofsted.
[2] Lloyd, E. and Potter, S. (2014) *Early childhood education and care and poverty*. London: University of East London, International Centre for the Study of the Mixed Economy of Childcare; Mathers, S., Eisenstadt, N., Sylva, K., Soukakou, E. and Ereky-Stevens, K. (2014) *Sound Foundations: A Review of the Research Evidence on Quality of Early Childhood Education and Care for Children Under Three Implications for Policy and Practice*. London: The Sutton Trust.

- Process factors, including relationships between children and practitioners characterised by warmth, responsiveness and pedagogical competency; the stability and continuity of care; home-nursery links; and leadership committed to continuous quality improvement.

- Structural factors, including the proportion of staff with graduate and tertiary early years qualifications; adult-child ratios and group sizes; a mixture of children from different social backgrounds; and access to adequate physical space, including green spaces.

- Stability and duration of attendance: children benefit from stable care patterns with consistent carers. Whilst children benefit from a longer duration of early education, i.e. beginning before age three, full time attendance has no benefit over part time attendance (nor detriment, so long as care is high quality).

Evidence suggests that the developmental gap among children from different background stems from the a range of influences in a child's life, including the economic conditions in which families live, environment factors such as housing, parenting styles and the quality of early education. An effective approach to narrowing the developmental gap must therefore be holistic.

Childcare has significant potential to improve outcomes not only as a protective factor against disadvantage experienced elsewhere in a child's life, but as one of the few effective routes for the state to reach families and affect this wider context and influences on child outcomes. Research evidence suggests that supporting parents bringing up children in difficult circumstances to create a positive home learning environment, and a positive attitude to formal education, must be an absolute priority.

When measured against these characteristics, the current childcare system falls short, and funding is a key constraint on providers' ability to deliver high quality care:

- Early years graduates are relatively sparse, particularly in the private and voluntary sector where graduates make up 13 per cent of staff compared to 35 per cent in nursery schools.[3] Provider staffing is driven principally by provider income: hourly income for private are dramatically different, and this gap is hard to close.

- Terms and conditions among staff in private and voluntary providers and maintained providers also vary. Pressures on providers mean that relatively few staff working in the private and voluntary sector enjoy sufficient time to monitor children's development, plan care and participate in continuing professional development. Research commissioned by the Pre-School Learning Alliance has helped to substantiate the impact of poor funding on the quality of care delivered to children, taking into account the indirect costs of good quality care.[4]

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[3] Brind, R., McGinigal, S., Lewis, J., and Ghezelayagh, S. (TNS BMRB), with Ransom, H. Robson, J., Street, C. and Renton, Zoe. (NCB Research Centre) (2014) *Childcare and Early Years Providers Survey 2013*. London: Department for Education

[4] Ceeda (2014) *Counting the cost: An analysis of delivery costs for funded early education and childcare*

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- Low pay is also a systemic constraint on quality that makes it difficult for many providers to compete with the education sector for skilled, motivated staff. Staff in maintained providers are paid on average 68 per cent more than their counterparts in private and voluntary providers.[5] This inevitably has an effect on the educational background, motivation and professional identity of staff.[6]

- The fragmented nature of formal childcare provision means that most children will shift between more than one setting between age two and five, creating multiple transitions that often occur without a strong handover framework in place. This issue may particularly undermine care for two year olds who receive free childcare in a private or voluntary setting and move into a school at age three. For maintained settings, extending provision to younger age groups requires investment that many cannot afford to make.

- Falling investment in children's centres and early intervention services is affecting the quality of childcare, particularly in the least affluent areas.[7] For example, the number of children's centres offering directly funded childcare has declined by half since 2009 to around 450: 72 per cent of children accessing directly funded childcare receive graduate-led care but this falls to 34 per cent where provision is delivered by a private or voluntary provider linked to a children's centre.[8] Children with special educational needs and disabilities appear to have been disproportionately affected by funding pressures as the number of Special Educational Needs Coordinators has fallen and childcare provision in children's centres, often used by these children, has declined.

- There is significantly greater social segregation in the early years than in schools and, whilst the most disadvantaged children can often access graduate-led care in schools, research suggests a concentration of children with high needs may undermine progress in improving outcomes in these settings. If more schools were to offer flexible care suitable for parents working full-time, and more high quality private daycare providers were accessible to parents with low incomes, this issue would be less acute.

- Free early education is not fulfilling its potential to support parents to participate in work, education or training and improve a family's living circumstances. Patterns of care are dictated by services rather than parents' needs; for example, some 43 per cent of children receive free care in blocks of three hours each day, five days a week, and less than a third of settings offer care for more than 38 weeks of the year. Stable patterns of care are best for children. However, there is far more scope than is

[5] Ibid
[6] Mathers, S., Eisenstadt, N., Sylva, K., Soukakou, E. and Ereky-Stevens, K. (2014) *Sound Foundations: A Review of the Research Evidence on Quality of Early Childhood Education and Care for Children Under Three – Implications for Policy and Practice*. London: The Sutton Trust; Department for Education (2013) *More great childcare*; Department for Education (2012) *Foundations for Quality – The independent review of early education and childcare qualifications: Final report*. London: Department for Education
[7] Children's Commissioner (2015) *Changing the odds in the early years: A discussion paper on tackling poverty in the early years*
[8] Department for Education (2015) First statistical release, *Provision for children under 5 years of age: January 2015*

currently being utilised through funding levers to ensure that free early education supports working parents.

2. The childcare market and costs to providers

The Family and Childcare Trust collects annual data on childcare costs, which provides insight into provider business models.[9] There are substantial variations in price between the different regions and nations of Britain. But there are also differences in price between different local authorities within regions and also within local authorities themselves. Within London a parent in the most expensive local authority would pay £123 more per week or £6,400 per year for a part-time nursery place for an under two, compared with a parent in the cheapest local authority. Even in the North East of England, which is a more economically homogenous region, childcare costs for a part-time nursery place for a child under two is £49.96 more expensive per week – or £2,600 per year – In the most expensive local authority compared with the cheapest.

We have mapped prices and quality in a number of London local authorities and we have found that the private and not-for-profit day nursery market comprises four distinct types of business:

- A small number of 'luxury' nurseries, some of which are single settings and others run by large national nursery chains. They charge high prices and offer extra services, for example, early starts or organic food. Many of them have opted not to take two year children who qualify for free early education. As might be expected, these nurseries are the most expensive and are almost always located in prosperous areas.

- 'Standard' day nurseries which offer 8am – 6pm childcare but few extra services. They comprise the largest group of nurseries and are found in all areas. They have maintained quality and generally offer places to two, three and four year olds who qualify for free early education. This group of providers includes single settings, smaller regional chains of 2-10 nurseries, as well as some of the larger privately-owned day nursery chains. While the care they offer is similar across this group, there is a considerable variation in the prices they charge.

- Social enterprises, which are often run by charities, or sometimes by not-for-profit companies, employer or user-owned mutuals and cooperatives. Some of these nurseries have a defined social mission and some are located in deprived areas. Some children's centre nurseries that were formerly run by local authorities are now run as social enterprises. They are more likely to offer high quality provision and their business model enables them to offer income-contingent fees for parents. This means that low income or targeted parents receive fee discounts.

- The 'strugglers' which comprise about 15 per cent of nurseries and are disproportionately located in deprived areas. While their fees tend to be lower, they may face quality or profitability problems.

Price variations are sometimes a consequence of the stratification described above. Differences in pay and other operating costs can also cause price variations. There are other

[9] Rutter, J. (2015) *Childcare costs survey 2015*. London: Family and Childcare Trust

reasons: in some areas there is much more subsidised public sector provision in some local authorities than in others. As public sector provision is generally less expensive, this factor can account for price variations: in London, for example, nursery provision for a child under two is £25.98 per week more expensive in the private and voluntary sector.

There is also a link between childcare supply and its cost, which can also contribute to price variations. Childcare operates on a regulated free-market principle. Increased demand is meant to increase supply and help keep prices competitive and affordable. If prices increase, the implication is that supply is lower than demand, which our survey shows is the case in some parts of Britain.

Differing levels of public subsidy also cause price variations. There are significant variations in the hourly rate that providers receive from local authorities to deliver free early education. Within the North East, for example, the hourly rate allocated by the Government for three and four year olds in 2014-2015 ranges between £3.49 and £4.67 per hour.[10] Over the course of one year, a nursery getting the higher level of funding will get £673 more to deliver free provision than one receiving the lower level.

Funding for free early education in private and voluntary settings in England has historically been too low. Not only has funding not been sufficient to support providers to deliver high quality care, funding has not always covered provider costs. For example, in 2014/15 the two year old offer, which has benefitted from more generous funding than for three and four year olds, was funded at around £4.80 on average per hour outside London compared to £7.20 per hour in Wales. This has led to many providers in England choosing not to participate in the two year old offer, contributing to low take-up. Alternatively, where the money nurseries receive from local authorities does not cover costs, nurseries rely on working parents to purchase extra hours on top of their existing free provision, and at a higher price, in order to cover costs. This can make childcare expensive and also accounts for price variations for nursery provision.

Early years' providers also operate other cross-subsidies which can cause price variations. The parents of three and four years olds may cross-subsidise childcare for babies, where higher staffing requirements can make childcare too expensive for local families. These price variations are important and matter to families, because they mean that parents in neighbouring areas have large differences in their childcare costs that cannot be offset by differences in wages.

The roll out of the 30 hour offer will increase the influence of free early education funding as opportunities for providers to cross-subsidise will be reduced. Most childcare providers are highly sensitive to small changes in income or outgoings. Unless the Government addresses funding shortfalls, this is likely to have an impact on childcare sufficiency as fewer daycare providers will be able to use parental fees to buffer pressures on costs. The business models of providers are likely to become more precarious and providers that might consider a transition to a daycare model may be less likely to do so.

A small number of private or voluntary provider groups have developed business models that utilise efficiencies of scale, such as deploying staff flexibly across more than one setting, to achieve more with limited funding. Providers such as the London Early Years Foundation have developed innovative models – cross-subsiding not only within but across settings to

[10] Department for Education, Early years benchmarking tool

use profits from one area to meet social need in another – that we would like to see replicated more widely. However, such models rest on the careful selection of sites where parental employment is high and demand for childcare is strong, which means that they cannot be replicated universally. Even the most efficient providers are constrained by funding parameters; few voluntary providers, for example, are able to compete with wage levels in maintained provision.

3. Recommendations

1. The Department for Education should establish a simple and transparent means of ensuring that early education funding allocations are distributed fairly to local authorities.

Allocations should be set based on a wider basket of indicators than is currently the case and consistently for two, three and four year olds. An allocation formula should, like the formula for the two year old offer, include an area-based factor taking into account local fixed costs and wages, and a deprivation factor using national indicators such as the IDACI index bandings and prior attainment (using schools data) as well as direct influences on costs such as the number of children who are looked after or have additional language or SEND needs.

In re-allocating funding, the Department should avoid undermining settings such as nursery classes in schools which benefit from the highest funding rates. Some local authorities have a higher proportion of maintained settings than private or voluntary providers, and therefore benefit from a higher funding allocation. These settings often cater to the most disadvantaged children and are taking on an increasing role in quality leadership in childcare. Rather than remove resources from some of the most important providers in the system, the Department should use new investment to address inequities in funding.

2. The Early Years Single Funding Formula should be revised and strengthened to provide a clear framework that promotes quality and flexibility.

The Department should set a clear minimum standard for funding, based on the cost of delivering high quality care, that reduces the variation in local authority funding rates. Base rates should be set by provider type and explicitly recognise the additional cost of daycare, which should be funded at a minimum in proportion to hours of free care as a proportion of the hours offered by a provider (i.e., meeting a proportion of a provider's costs in line with up to 15 hours or, in future, up to 30 hours of care). The Department should itself publish guidance on funding rates, and consider setting minimum rates in regulations, to achieve this. If necessary, the Department should conduct detailed research with providers to establish appropriate baseline figures.

The EYSFF should also include a mandatory deprivation supplement based on a nationally consistent indicator, and an additional needs element that recognises the additional costs associated with children with SEND or who speak English as a second language. A further supplement should be linked to the proportion of early years graduates in a setting working directly with children, extending to two year olds as well as three and four year olds.

3. The Department should set an explicit goal that every setting will become graduate-led within ten years.

The Graduate Leader Fund established a model for supporting a variety of providers to train staff but did not address the fundamental challenge of meeting the additional long-term cost of a graduate salary. In future, the EYSFF should explicitly meet this need through a mandatory graduate supplement for providers delivering graduate-led care to children. Alongside the EYSFF, local authorities should be required to offer a pool of funding to support early years staff to access graduate training to ensure a continued throughput of qualified early years graduates (including both direct qualification costs and the cost of extra staff to cover time spent in education).

4. The Department should increase funding for the Early Years Pupil Premium.

Initial feedback from providers suggests that the EYPP is a welcome stream of funding that can be put to constructive use, but is currently set at too low a level to allow many providers to provide effective interventions. The EYPP must not become a means of compensating for under-funding of quality and flexibility in free childcare: addressing qualifications and flexibility priorities should be the purpose of the EYSFF framework, whilst the EYPP, like the school base pupil premium, is used to pursue specific interventions to improve outcomes for eligible children.

5. The Department should identify new capital and revenue funding to support childcare providers to increase flexibility.

It is unrealistic to expect local authorities or providers to expand childcare places without some additional public funding. Many settings will incur new costs if they are to offer 30 hours of childcare each week: for example, some sessional providers may need to seek new premises and school-based providers may require adaptations to facilities. This will particularly the case if providers seek not only to offer 30 hours of care but to do so flexibly within a full daycare framework. We would encourage the Government not to limit this funding to the roll out of the 30 hour offer and establish a policy of supporting as many providers as possible to offer flexible daycare to children aged one to four.

6. The Department should establish a statutory mechanism for local authorities to collect annual provider costs data.

The limited evidence available on the cost of childcare to providers undermines effective policy making at a local and national level. A number of local authorities have periodically gathered some cost information from providers to inform a review of the EYSFF. However, many local authorities simply propose and consult on a new EYSFF formula, or update the formula without consultation. The only way the Government and local authorities can determine whether the funding system is working is to obtain the data needed to understand the impact of funding rates on the services providers deliver. The Department could use the statutory framework established by the Childcare Act to update information regulations, learning from the templates developed by the most proactive local authorities.

7. The Government should invest in local authority early years early intervention services.

It is a false economy to invest in childcare subsidies whilst drastically cutting investment in children's centres and early intervention services. We welcome the Government's decision to consult on the future of children's centres and encourage ministers to use the opportunity to clarify how children's centres and childcare providers should work together in future, and how the former will be properly funded to deliver universal services.

8. The Government should establish an independent commission on childcare to make recommendations on funding reform and long-term investment.

The Family and Childcare Trust remains of the view that a wider review of childcare funding is needed. The current childcare funding system has evolved on an ad hoc basis and is no longer fit for purpose. Pre-school services are influenced by a number of funding streams – notably, free early education, the childcare element of tax credits and childcare vouchers – but the design of these schemes is not coordinated to deliver agreed outcomes. Whilst the Government can improve the situation through investment in, and reform of, free early education funding, it will be extremely difficult for the Government to deliver shared aspirations for childcare – high quality, affordable and flexible care – through the present fragmented funding system.

Several developments mean that the need for a wider review of childcare funding has become pressing. First, the Government's commitment to several new streams of investment in childcare within the next two years – the 30 hour offer, the tax-free childcare scheme and an increase in support under the childcare element of Universal Credit – has highlighted the fragmented nature of the current funding system. The Government itself is subsidising excessive costs that are caused by poor policy-making. This is money that could be saved and re-invested in improving the quality and availability of childcare. We agree with the recommendation of the recent House of Lords Affordable Childcare Committee that the Government should examine whether the new tax-free childcare scheme provides an opportunity for a single mechanism for childcare subsidy.

Second, alongside the 30 hour offer, the Government is legislating through the Welfare and Work Bill to introduce stronger conditionality requirements for working tax credit and Universal Credit. Parents with children aged three of over will be expected to seek work for at least 16 hours each week, and those with children age two will be expected to participate in work preparation activities. The new £23,000 benefits cap will also force an increasing number of parents with pre-school children to seek work. This will put greater demands on the childcare system, but the Government does not yet have an effective strategy to meet these demands.

Finally, the introduction of the national living wage will have significant consequences for childcare provision, where a high proportion of staff are paid below the living wage. If the Government does not act, there will be significant pressures on providers that result in higher costs to parents and could lead to significant disruption in the childcare market. The Government should assess at an early stage how it can ensure that the NLW does not lead to a sharp increase in childcare costs for parents.

There is a strong political consensus in favour of investment in childcare to meet broadly shared policy aspirations. However, the Government has not undertaken an effective, coordinated or sufficiently rigorous review of childcare funding to properly design a funding system that will deliver on these aspirations in future. The Family and Childcare Trust recommends that the Government establishes an independent commission to make recommendations on funding reform and long-term investment.