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JRF Programme Paper

An anti-poverty strategy for the UK

Creating an anti-poverty childcare system

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January 2016

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Executive summary

Around 2.3 million children in the UK are living below the Child Poverty Act 2010 relative poverty threshold, representing one-fifth of all children. By the same measure, eight million working age adults and, overall, over one-fifth of the UK population live in poverty. Following a long-term trend of falling poverty since the mid-1990s, these figures are predicted to rise significantly as planned cuts to welfare budgets deepen.

Reducing poverty is a complex undertaking to which there is no easy answer. A robust body of evidence suggests that publicly funded childcare can help reduce poverty in two key ways:

- high quality early education and effective early intervention can act as protective factors for children against the negative effects of poverty, improving long-term developmental and employment outcomes;

- access to flexible, affordable childcare can reduce pressures on family income and help parents to participate in work, education or training, reducing a family's short- and long-term poverty risks.

Measured against these aims, the UK childcare system currently falls short of fulfilling its potential to help reduce poverty:

Children often do not have access to childcare of the standard needed to improve developmental outcomes.

The difference between pre-school programmes that make a difference to children's outcomes and those that do not is quality. The UK has successfully established funding and regulatory arrangements that mean that poor quality care is rare. However, to improve outcomes, care must meet an extremely high standard that includes: well-qualified, experienced staff able to identify and respond to children's needs; a good social mix of children; a proactive approach to supporting home learning; and strong links with early intervention services.

UK policy, funding and regulatory frameworks for childcare do not deliver this standard of care to most of those children who are at risk of falling behind: many children – particularly those aged under three – do not receive graduate-led care, whilst settings of all types often lack a good social mix of children, an active approach to supporting home learning or strong links with local family and child support services (which themselves are under severe funding pressures). Low wages remain a systemic constraint on quality in the early years.

Families in areas of low parental employment are less likely to have access to flexible childcare.

Childcare access is shaped by a market that is less favourable to families in less prosperous areas. As a result, childcare in the least affluent areas is dominated by maintained providers in schools, the majority of which do not offer daycare, supported by a limited patchwork of voluntary services and childminders. Families therefore often lack access to year-round, flexible daycare. This market particularly fails to meet the needs of parents who work atypical hours. A lack of access to flexible childcare can force parents to choose low quality part-time jobs, trade down roles or leave work altogether, and makes it more difficult for parents at risk of poverty to address skills or education deficits.

Support with childcare costs does not work well for, or provide adequate help to, parents with low incomes.

More help with childcare costs for parents with low incomes will be provided through the government's planned extension of free childcare to 30 hours a week for three- and four-year-olds, and the increase in support to 85 per cent of costs from April 2016 for families eligible for Universal Credit. However, the proposed system of delivering this support is bureaucratic, difficult to navigate for parents and will fail to properly address basic affordability challenges such as deposits and up-front fees. Moreover, Universal Credit will not provide meaningful support or work incentives for many parents – particularly second earners with childcare costs – and there remain significant gaps in support with childcare costs for parents who are jobseeking or building skills through education and training.

An anti-poverty childcare system

The UK has made great strides in the last 20 years in extending access to formal pre-school childcare and creating a universally free early education offer. However, successive UK governments have failed to develop a coherent vision and strategy for pre-school childcare and persistent problems holding back the childcare system have not been addressed. Two principles should be at the heart of an anti-poverty childcare system:

- maximising the potential of high quality childcare to act as a protective factor and improving long-term outcomes for children living in, or at risk of, poverty;

- removing barriers to participation for parents, especially to employment, training and education, created by childcare access or affordability problems.

Our recommendations seek to set out practical and achievable steps towards meeting these goals through a long-term strategy of reform and investment. The proposals seek to transform the UK's current fragmented childcare market into an integrated system that delivers high quality, affordable and flexible care. Our key recommendations are:

1. Funding a decisive shift towards high quality childcare by:

- moving to a fully qualified, graduate-led workforce and equalising wages across private, voluntary and maintained settings, in line with a national pay scale, to support professionalisation of the workforce;

- investing in early intervention through child and family support services and creating direct links between childcare providers and children's centres in order to clarify responsibilities and remove gaps in the early years early intervention framework;

- strengthening requirements within regulatory frameworks that impact on children's development, such as support for home learning; and

- introducing an age-appropriate developmental assessment for children on entry and exit from early education to support children's development.

2. Addressing access and flexibility challenges and creating a truly universal childcare system by:

- replacing the ineffective Childcare Act 2006 'sufficiency duty' with a properly funded entitlement to childcare for pre-school children from age one extending across a full day and for 48 weeks of the year;

- introducing a transparent statutory admissions code of practice for centre-based childcare providers;

- extending the free childcare offer to all two-year-olds at an appropriate pace to deliver high quality places;

- extending properly funded childminder networks offering brokerage and support to childminders; and

- creating an ambitious business development programme to support social enterprises and foster those business models that are most successful in offering high quality care to diverse communities.

3. Extending support with childcare costs for families in or at risk of poverty by:

- removing the parental contribution to childcare fees altogether for families with an income below the relative poverty threshold;

- extending support with childcare costs to jobseeking and work preparation activities, including education and training; and

- establishing a mechanism to pay the deposit and first month of childcare fees up front for parents moving into work.

Our proposals are underpinned by a shift to supply-side funding for pre-school childcare services. The government's approach to childcare funding is not on the right track. Following the roll-out of the tax-free childcare scheme, the 30-hour offer and extended support under Universal Credit, public funding will account for the majority of income for most early years childcare providers, whether they are under public, charitable or private ownership. Yet the childcare funding system is excessively complex, delivers poor value for money and does not offer the means to effectively influence service provision.

International evidence and the best examples of high quality provision in the UK suggest that the most effective approach to funding pre-school childcare is supply-side funding, where investment is made directly in services. This approach provides the means to offer universal access to services and effectively shape quality, affordability and flexibility. Whilst we set out 'second best' options, such as increasing investment in the childcare element of Universal Credit, demand-side subsidies do not offer the same means to achieve integration and deliver improvements in services. The case for supply-funded childcare is simple: it is the most effective means of delivering reliable access to affordable, flexible and high quality childcare regardless of parents' ability to pay.

Our proposals seek to deliver a universal pre-school childcare system; that is, a system that delivers guaranteed access to high quality childcare at a price parents can afford. We have not recommended a universal *free* childcare system. The state cannot, in the near future, afford to subsidise both generous free entitlements for all families and meet pressing anti-poverty investment priorities. An excessive focus on free childcare risks locking the UK into a low quality funding model, distracts policy-makers from investment in early intervention services and will not address fundamental access and flexibility challenges. Whilst targeted increases in free provision can be justified, large extensions to universal free childcare are likely to undermine rather than support anti-poverty policy goals.

Box 1: Simplifying childcare subsidies

A new childcare subsidy scheme should be simple, ensure that the parental contribution to childcare is controlled for those with low incomes, and adequately provide for flexible, high quality care. With these parameters in mind, we propose that the current plethora of schemes offering support with childcare costs should be replaced by a single supply-side funding scheme in the early years. This means that centre-based childcare providers and childminders would be funded entirely by grants similar to those provided for free early education. Parents would pay a simple income-based fee per hour for childcare using an online account (with telephone support). Parents with two- to four-year-old children would still receive 15 hours of free care each week and would use this scheme to purchase additional hours of care.

We propose that care should be free for those with lower incomes and not consume more than 10 per cent of disposable income for families with low to middle incomes. To achieve this, we suggest that fees should start at 50 pence per hour for families with an income over £16,200 and subsequently rise in ten pence increments as income rises. Parents with an income above a certain threshold — we suggest £76,000 — would pay a '100 per cent' subsidy. The hourly fee should be reduced by 50 per cent for each additional sibling attending care, up to three children (with further children free), and income thresholds adjusted for single parents.

This system aims to balance simplicity with the fair targeting of resources. Parents would be able to understand clearly how much they can expect to pay for childcare, whilst the state can ensure that the parental contribution to childcare costs does not rise too high as a proportion of family income. The account system being set up to administer the tax-free childcare scheme offers a simple and flexible mechanism that could be adapted to this purpose in the future.

Simple fee structure

Family income	Up to £16,200	Up to £36,000	Up to £46,000	Up to £56,000	Up to £66,000	Over £66,000
Maximum fee per hour (first child)	Free	£0.50	£1.00	£2.00	£3.00	£4.00
Maximum fee (second child)	Free	£0.30	£0.50	£1.00	£1.50	£1.80
Maximum fee (third child)	Free	£0.10	£0.30	£0.50	£0.80	£0.90

The state subsidy to providers would meet the actual cost of care. This subsidy would be provided directly to providers on a termly basis through a reformed early education and childcare grant. The amount each provider receives would reflect the number of children registered in a setting, the hours of care used and other factors such as the relative needs of children. Unlike the planned Universal Credit and tax-free childcare schemes, this model would allow the government to directly influence provision whilst controlling costs.

This scheme would mean that childcare fees are, in effect, capped. Persistent underfunding has eroded trust among many early years childcare providers and government. To ensure the state contribution adequately meets the cost of care and a sufficient supply of high quality childcare is maintained, we propose that an independent body is established to advise the government and local authorities on funding allocations. The success of a system with regulated fees rests on a properly resourced, responsive and flexible funding system, with a transparent relationship between provider costs and funding.

There are further options for reforming childcare subsidies, but none that are as close to meeting the criteria for an anti-poverty childcare system. The task of designing a single subsidy scheme for childcare is one that properly requires extensive analysis, modelling and consultation. We aim to show how a single, simple subsidy system could address a number of the problems inherent to the current complex subsidy arrangements and propose workable parameters for a new scheme.

A roadmap for reform

From 2017/18, approximately £7.4 billion of public funding will be allocated to childcare spending in England, or around 0.5 per cent of GDP (adjusted for England). Figure 1 sets out the indicative cost of investing in anti-poverty childcare priorities. We estimate that meeting the goals set out in this paper would increase spending by £5.4 billion to £12.7 billion, or 0.85 per cent of GDP. This figure reflects the realistic costs of a comprehensive long-term strategy to address systemic challenges in pre-school childcare. Well-designed investment in childcare can be cost effective through long-term fiscal returns to the state (see Box 3 below) but up-front investment is required.

There are few easy answers to the challenge of investing in childcare. Some funding – we estimate up to £500 million – can immediately be found for the most pressing priorities by ending some existing poor value spending. However, in the longer term new investment is needed to fulfil poverty reduction aspirations. The approach we propose is to focus in the short-term on neglected areas of investment and key pressure points that affect parents with low incomes, and invest at a sustainable rate over a ten-year period to meet expensive policy aims, such as extending free childcare to all two-year-olds and improving early years staff wages.

Our proposals broadly apply across the UK, but each devolved nation has a unique set of circumstances, challenges and priorities that requires each nation to develop a locally tailored childcare strategy. In recent years the devolved administrations have been more proactive than the government in Westminster in developing coherent childcare policies (see Box 5). However, a substantial proportion of childcare funding continues to be controlled in Westminster. This includes the childcare element of tax credits, employer-supported childcare vouchers and the tax-free childcare scheme. Up to £439 million of planned spending on childcare subsidies from 2017 will not be available to the devolved administrations to spend in line with devolved priorities. Through reform, this funding could be fully devolved to free up devolved policy-makers.

Proposed devolved spending (£million)

Nation	Graduate-led high quality free early education	Children's centres and early years services	Pre-school childcare subsidies	Total	Estimated spending in 2017/18[1]
Scotland	£434	£130	£708	£1,272	£756
Wales	£248	£74	£405	£727	£426
Northern Ireland	£150	£45	£244	£439	£257

Box 2: What is an anti-poverty childcare system?

The aim of our proposals is to show how a transformative strategy can be implemented to achieve a high quality childcare system that makes the greatest possible contribution to poverty reduction. This means that:

- All children receive care in a stable, positive and warm environment. Every child attends early education in a socially mixed setting and receives care from an expert, confident and experienced early years professional. Staff in all settings see it as an integral part of their job to identify and support children who are less likely to reach a good level of development, regardless of the child's background.

- Childcare encourages and drives positive engagement by parents with their children's development and is a source of support and advice for home learning. All early years settings work closely with local early years child and family support services, making appropriate referrals and ensuring that families benefit from a full range of universal and targeted services.

- All parents with pre-school children have access to a flexible, year-round childcare place and are able to choose from a number of high quality local providers. Parents have an entitlement to childcare as they do to a school place, supported by a transparent and fair admissions process with a clear route of redress. Parents who work outside 'normal' working hours are able to access childminders and home carers through well-funded brokerage services.

- Parental fees are never a barrier to childcare access: families near to, or below, the relative poverty line do not pay anything for childcare and families earning up to the minimum income standard pay no more than ten per cent of disposable income towards fees. Eligibility criteria for support extend beyond participation in work to jobseeking and work preparation activities, including education and training.

- All early years staff are professionally qualified and paid a comparable wage to their counterparts in schools. Staff work in a professional environment with sufficient mentoring, training and continuing professional development. All providers, whether centre-based or childminders, privately or publicly owned, have a common child-centred ethos and understand their role is to meet the developmental needs of children and support families.

Box 3: The fiscal benefits of investing in childcare

There have been a number of attempts to quantify the potential fiscal benefit of early education and increasing parental employment. Whilst estimates of this nature are inherently stylised and subject to uncertainty, there is good evidence that well-designed investment in childcare can, as part of a wider poverty reduction strategy, be a cost-effective use of public funding.

Cattan, Crawford and Dearden (2014) seek to estimate the potential increase in lifetime earnings for children who attend pre-school. Attending a pre-school on average increases the number of GCSEs a child attains at grades A*-C by 0.8, lifetime earnings increase by an average 7.9 per cent or £27,000 at current values, or £35,000 per household. This compares to a theoretical investment of £9,981 per child in high quality free early education under the proposals set out in this paper (see Appendix B).

A US study by Lynch (2005) reviewed the economic literature on pre-school programmes and estimated the long-term returns of a universal high quality pre-school programme, including benefits realised through lower welfare payments, higher pay and lower costs to the criminal justice and policing system. Lynch suggested that a suitable programme would cost around one per cent of GDP, which is consistent with estimates in this paper. Lynch estimates that the programme would require nine years before annual returns exceed costs. After forty years, Lynch finds the annual returns to be eightfold the programme costs.

Whilst evidence of the benefit of high quality early education programmes on children's long-term outcomes are strong, the relationship between childcare subsidies and maternal employment is more complex. Childcare is a necessary, but not sufficient, condition for work. Alongside childcare, parental attitudes, family-friendly work opportunities, work incentives in the social security system and education opportunities all influence family work decisions. The government submitted a summary of relevant evidence to the House of Lords affordable childcare committee (HM Treasury, 2015b). Studies suggest a negative relationship between the cost of childcare and participation in the labour market: a 10 per cent reduction in the cost of childcare leads to a 1 to 1.4 per cent increase in the employment rate for married mothers.

Reed and Portes (2014) estimate that, in an optimistic scenario where parental employment in the UK rises to the level of the highest OECD performers, £37 billion could be saved through higher tax revenues and lower welfare transfers. Thévenon et al. (2012) looked at the potential fiscal benefits of increased female labour force participation. Thévenon et al. estimate that there is the potential to add 10 per cent to UK GDP over a 20-year period if male and female labour market participation rates were to converge. If half of the gap in participation is closed, GDP growth is estimated to be five per cent. This growth arises from the organic benefits to the economy of the increase in human capital as more women participate in work and the nature of this participation changes, with more women working in skilled roles, avoiding low quality part-time work and experiencing fewer gaps in employment.

There is ample evidence of a potential positive return on well-designed investment in childcare. Each of these studies highlights, however, that the *nature* of investment matters to ensure a return on investment to the public. It is not sufficient to invest in just *any* early education and anticipate a return; the quality and comprehensiveness of the programme is critical. Equally, childcare subsidies will not necessarily support increased parental employment; investment must carefully target barriers to participation for parents. Measured against these broad benchmarks, the current UK childcare system is not well-designed to make a net long-term contribution to public finances.

Figure 1: Overview of recommendations

Note: Full policy costings provided in Appendix B



1. Introduction: Childcare in the UK

The last quarter of a century has seen a dramatic expansion of childcare provision in the UK. Until the late 1990s, formal childcare was limited principally to a patchwork of community nurseries in urban areas set up by voluntary services and local authorities, and a small private nursery market of less than 100,000 places. Childminders were the most common form of childcare provision outside the family. In contrast, in England alone there are now around 18,000 daycare providers offering 800,000 places and the majority of primary schools offer nursery classes for three- and four-year-olds.

The growth and evolution of the childcare system reflects rising demand driven by increasing maternal employment and a series of interventions by government. Beginning in 1994, the government funded support with childcare costs through a £40 childcare allowance introduced as part of the Family Credit (a precursor to the tax credit system). This allowance was increased through successive reforms of tax credits and is now worth up to 70 per cent of childcare costs each week. From 2005, the government also funded support with childcare costs for parents not eligible for tax credits through a voucher scheme, now worth up to £933 per parent each year.

Growing evidence of the benefits of pre-school education led the government to invest in universal free early education, beginning in 1998 with 12.5 hours each week for all four-year-olds. This offer was extended to all three-year-olds in 2004 and to 15 hours each week (or 570 hours each year) for three- and four-year-olds from 2006. From 2013, 40 per cent of two-year-olds have also been offered 15 hours of free early education each week. The government now proposes to extend free childcare for three- and four-year-olds to 30 hours each week, beginning in 2017.

Each UK nation has diverged moderately in the scope of its free early education entitlement. In Scotland, all three- and four-year-olds receive 600 hours of free childcare per year and this offer was extended to 27 per cent of two-year-olds in 2015. The Scottish government has also committed to expanding free provision to 30 hours by the end of the next parliament (2021). In Wales, all three- and four-year-olds are entitled to a minimum of 10 hours of free early education for 38 weeks of the year. Flying Start, an area-based anti-poverty programme, also offers free early education to two-year-olds in Wales, benefitting around a quarter of two-year-olds. In Northern Ireland, children start school aged four, and one year of funded part-time early education is available to three-year-olds for 12.5 hours per week.

Alongside free early education, the Sure Start children's centre programme was rolled out in England from 2004. Since 2006, local authorities have had a legal duty to provide sufficient children's centres, the core purpose of which is to improve outcomes for families with children. There are now approximately 2,800 children's centres in England, down from 3,500 in 2009 (although these figures are contested). Children's centres offer a small proportion of childcare nationally but have an important role in extending access as most are strategically placed in less affluent areas. Importantly, the children's centre network acts as the principal provider of early intervention and family support services and is therefore a crucial complement to free early education.

Scotland does not have a network of children's centres but many Scottish local authorities do fund comparable 'family centres'. Scottish local authorities also have statutory duties to provide early intervention and family support services, which are often delivered through school nursery provision. In Wales, the area-based (rather than centre-based) Flying Start programme reaches around 38,000 pre-school children and consists of support for early language development, an enhanced health visitor programme, parenting support and free

early education. Northern Ireland has a comprehensive Sure Start programme: there are currently 26 Sure Start partnerships in Northern Ireland and 48 Sure Start children's centres.

In England and Wales, the Childcare Act 2006 introduced a requirement for local authorities to ensure there is sufficient childcare for working parents 'as far as is practicable', and local authorities have statutory duties to produce periodic assessments of childcare sufficiency. In practice, however, direct intervention in the childcare market is limited. There is no comparable 'sufficiency duty' in Scotland but local authorities are required to consult with parents in planning free childcare and to take a strategic view of childcare accessibility. In Northern Ireland, there is no statutory requirement for local authorities to seek to provide sufficient childcare. However, through work to prepare a new childcare strategy, the Northern Ireland Executive recently committed to identify gaps in childcare provision and make funds available to regional childcare partnerships to address those gaps.

Since 1998, state investment in childcare has grown from less than £1 billion to over £5 billion. Cumulatively, government support has dramatically expanded the formal childcare market. The nature of this expansion has, however, been relatively *ad hoc*. Although funding for free early education is provided through local authority grants to providers, parents are usually able to choose where their child attends daycare nursery (as long as a provider is willing to offer a place), so the offer is effectively a form of cash or 'demand-side' support. In combination with other demand-side subsidies, such as tax credits and vouchers, new childcare places have therefore been created relatively organically through an expansion of voluntary and private daycare nurseries, new sessional pre-schools and new nursery classes in primary schools.

The unplanned nature of the expansion of childcare provision has led to a significant degree of fragmentation in provision, with a schism between the maintained sector, where care is teacher-led, staff are paid within a public sector pay framework and work within their school's professional framework, and the private and voluntary sector, where a minority of settings are led by a qualified graduate, staff wages are considerably lower and working conditions are variable. Private and voluntary providers are subject to less stringent quality requirements than maintained settings. For example, every maintained nursery school is required to employ a teacher with a special education needs qualification but non-maintained settings are not. Crucially, links between private and voluntary settings and early intervention services tend to be less strong than those among schools due to weaker institutional relationships.

All UK nations have a similar mixed market of public, private and voluntary childcare provision. Daycare providers make up just over one-third of early years childcare places (two-thirds of these providers are private providers and one-third voluntary or maintained services). Childminders and sessional pre-schools, the majority of which are voluntary services, each provide a further ten per cent of places. Schools provide the remaining early years places, largely through nursery and reception classes for three- and four-year-olds. There are some minor differences across the UK. In Scotland and Wales, there are fewer private and voluntary sector nurseries per head of population than in England (and so proportionally more public sector nurseries). In Northern Ireland, there is significantly less centre-based childcare than elsewhere in the UK.

Increasing access to childcare has helped support the rising proportion of mothers in work. Between 1996 and 2013, the percentage of married mothers in work rose by five per cent, cohabiting mothers by 11 per cent, single parents by 17 per cent. A number of factors underpin this trend, including particularly rising gender equality within families, education and the workplace and improved work incentives through tax credits. As only 50 per cent of families have access to regular informal childcare, and even fewer access to full-time informal care, improved access to childcare is also a crucial factor that underpins this trend.

The challenges childcare poses for policy-makers are now very different to those in 1990. The UK has a mature childcare system that has some strengths, such as near universal participation in early education, which are recognised internationally. But childcare provision also remains inadequate when measured against some basic policy goals. Free early education is not supported by an unambiguous commitment to high quality care, so outcomes for children can be disappointing. Many parents who would like to work still find it difficult to access affordable, flexible childcare beyond the free offer. The demand-funded evolution of the childcare system has led to a greater degree of social segregation in early years services than is apparent in the school system. In these respects, the UK system does not compare well to leading examples in Scandinavia and elsewhere in Europe.

It is easy to consider investment in childcare as benefitting the least well-off, but it is far from clear that this has always been the case. Families experiencing persistent poverty, or multiple disadvantages, can benefit from childcare provision with specific characteristics – well-qualified, well-trained staff and close links with family support services – that services often do not deliver. Financial assistance with childcare costs has also tended to benefit parents with low to middle incomes who are already in work rather than target parents at the greatest distance from the labour market. Flexible childcare services are critical to creating opportunities for families but cash subsidies have not done enough to develop the market for flexible childcare where demand is weak.

One effect of the rise in working mothers has been to steadily increase the political profile of childcare. The emphasis of public debates about childcare tends, however, to fall on childcare costs rather than whether investment is delivering the type of provision the UK most needs. Childcare has an uncertain status: it is widely recognised, particularly through free early education, as a public good but at the same time is often considered a marketised commodity for which a fee should be paid. Public debate often does not distinguish between pre-school childcare services and care for older children; in practice, these pose very different challenges for families and policy-makers.

Childcare policy-making can be disjointed. During the last parliament, three government departments developed significant and expensive childcare policy initiatives at different times. Decisions that all influence the same provision were made separately and on a seemingly *ad hoc* basis. England has not benefitted from a national childcare strategy since 2004, whilst the devolved nations, all of which have prepared childcare strategies in recent years, are constrained by the continuing control of childcare subsidies in Westminster.

Despite the progress that has been made in the last two decades, the UK childcare system continues to represent an unfulfilled opportunity. Childcare provision is flawed in many respects, but functions well enough for government to defer difficult policy challenges. This report argues that, in order to realise a childcare system that is successful in reducing poverty, it is to these challenges that policy-makers must turn.

The report is divided into three sections. The first section briefly summarises the potential impact of childcare on poverty and discusses where the current childcare system falls short of its potential to help reduce poverty. The second section sets out policy recommendations that are most likely to be effective in reducing poverty and looks in more detail at simplifying the childcare subsidy system. The final section of the report sets out a roadmap for a new childcare strategy. Our recommendations broadly apply across the UK; where there are differences in policy among the devolved administrations, we have noted these in the text.

Figure 2: Childcare spending in England from 2017[2]

Policy	Description	Amount (£million)
Free early education	15 hours of free early education each week for all three- and four-year-olds, and 40 per cent of two-year-olds Expansion of early education for three- and four-year-olds to 30 hours each week (beginning 2017)	£2,990 £990[3]
Childcare element of working tax credit and Universal Credit (UK)	85 per cent of eligible childcare costs for working parents from April 2016 for children aged up to 12 (or 17 for disabled children)	£1,590 (£1,320 England)
Sure Start children's centres	Local authority spending on Sure Start children's centres	£760
Tax-free childcare scheme (UK)	20 per cent of childcare costs up to £2,000 each year per child aged up to 12 (or 17 for disabled children)	£845 (£701)
Employer-supported childcare voucher scheme (UK)	Income Tax and National Insurance relief on childcare payments up to £933 per year for basic rate taxpayers, which can be used to purchase childcare for children aged up to 15 (or 16 for disabled children)	£640 (£531)
Tax relief for workplace nurseries (UK)	The cost of a place in a workplace nursery is exempt from Income Tax and National Insurance (this includes linked providers as well as on site provision)	£210 (£174)
Total		£7,466

Sources: HMRC, 2014a, 2014b and 2015; Department for Education, 2015b and 2015c; Stewart and Obolenskaya, 2015; HM Treasury, 2015a

2. Childcare and poverty

This section of the report examines the characteristics of families with young children at risk of poverty. We then briefly set out where the current UK childcare system falls short of its potential to help reduce poverty.

Poverty risk factors for families with young children

In order to identify appropriate anti-poverty childcare policy options, we first look at families at risk of poverty. The following working definition of poverty is used by the Joseph Rowntree Foundation:

> *When a person's resources (mainly their material resources) are not sufficient to meet their minimum needs (including social participation).*

We use this working definition and consider as widely as possible how childcare affects poverty risks. For example, families may live in poverty because a parent cannot access suitable affordable childcare and is unable to work. Equally, where parents do work, compromises made to maintain childcare arrangements can undermine long-term prospects: examples include 'backsliding' to a less senior or less skilled role, avoiding taking on responsibilities or participating in development opportunities that might conflict with childcare arrangements, or choosing low quality but flexible part-time work. A series of government sponsored reviews, including the Marmot Review, *Fair Society, Healthy Lives* (2009), the *Review on Poverty and Life Chances* led by Frank Field (2010) and the Independent Review on Early Intervention led by Graham Allen (2011) have reinforced that children's early years are critical to their long-term prospects and poverty risk as adults, whatever their background.

Figure 3: Children in poverty[4]

	Percentage of children in poverty	Number of children (million)
Relative poverty (before housing costs)	17	2.3
Relative poverty (after housing costs)	28	3.7
Low income and material deprivation	13	1.7
Severe low income and material deprivation	4	0.5
Total		13.4

Figure 4: Percentage of children in poverty by family work status

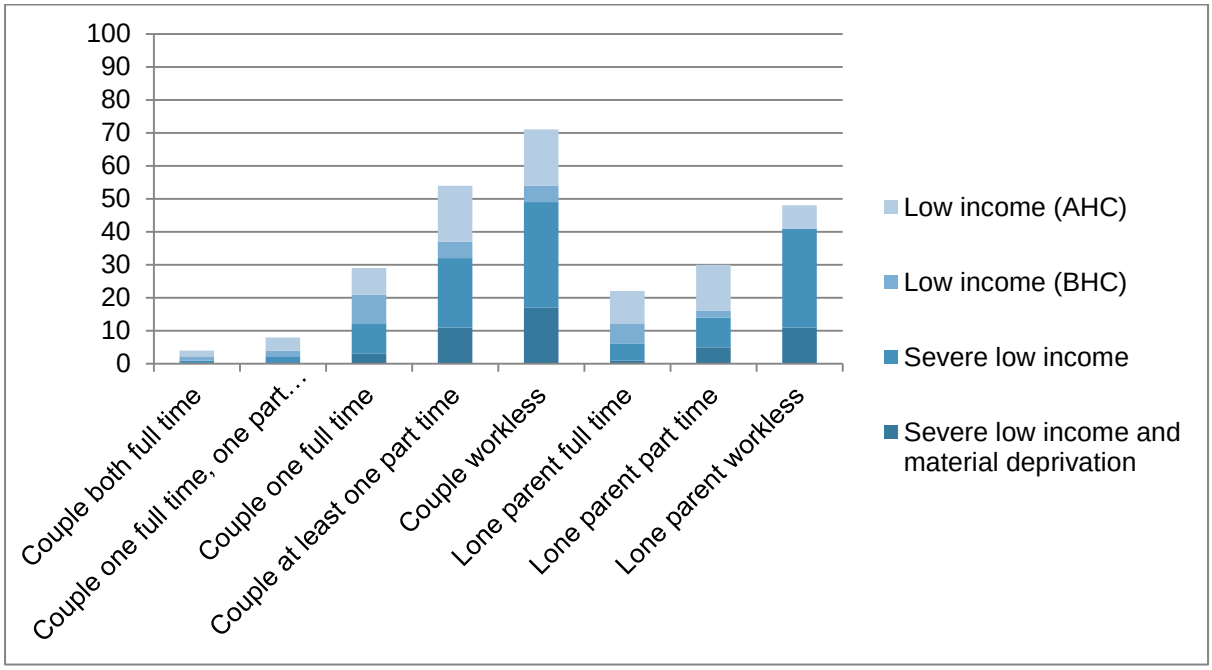


Figure 5: Percentage of children in poverty by number of children in family

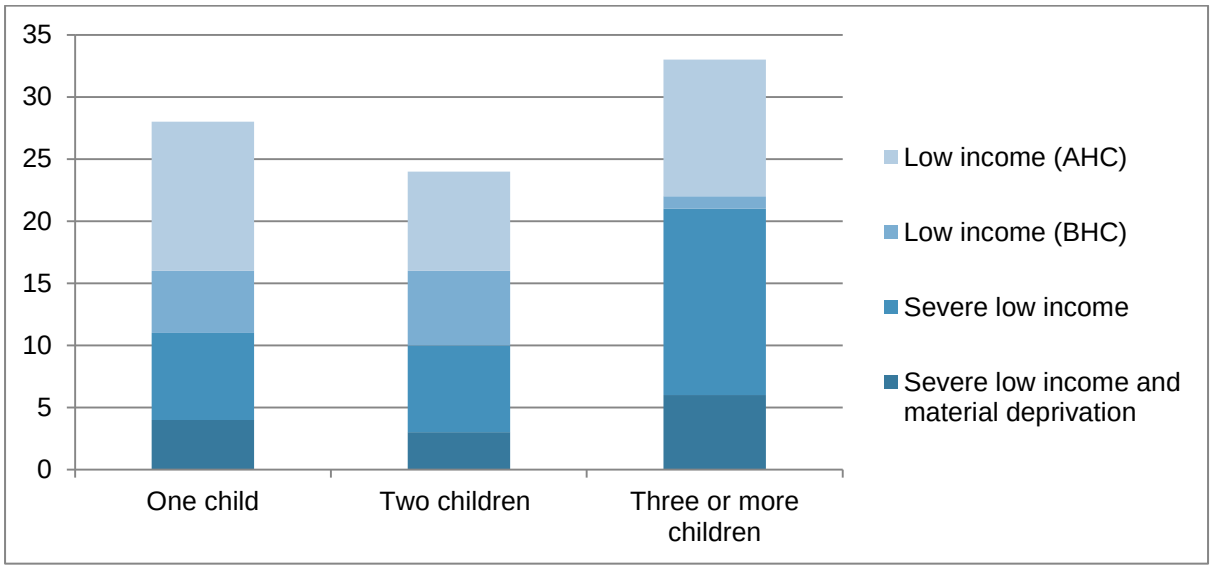
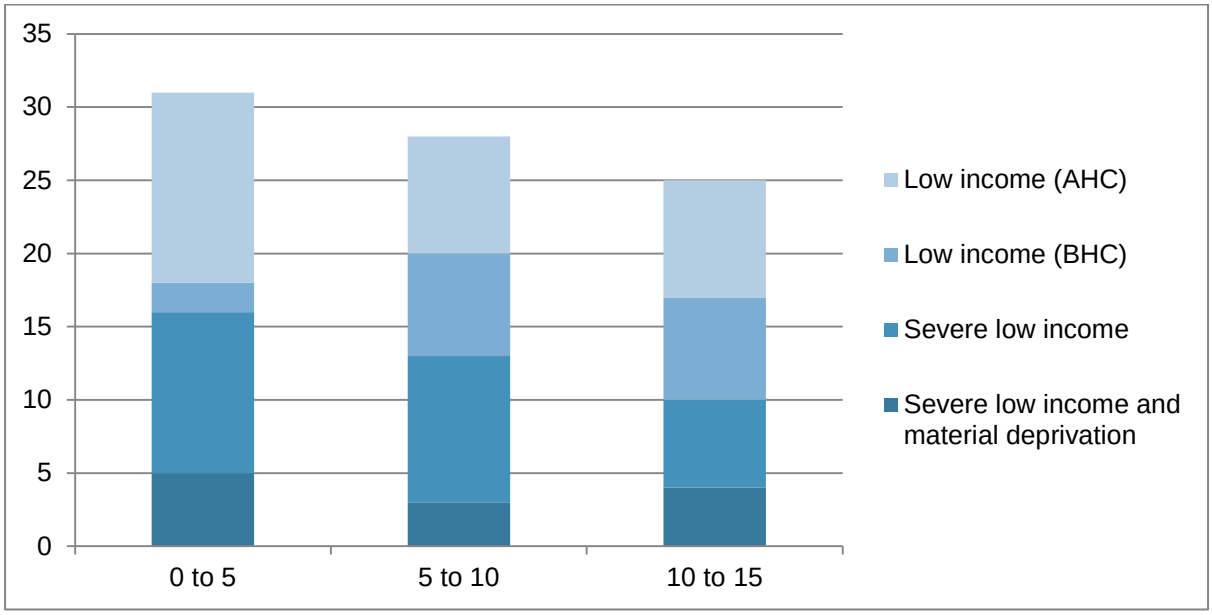


Figure 6: Percentage of children in poverty by age of youngest child



Source: Department for Work and Pensions (2015) *Households Below Average Income – an analysis of the income distribution 1994/95 – 2013/14*, Supporting data tables

The Child Poverty Act 2010 indicators can be used to look at the characteristics of families with children in, or at particular risk of, income poverty. Poverty is closely associated with work: eight per cent of children in families where both parents work, and at least one parent works full-time, fall below the relative poverty line compared with 29 per cent in families where only one parent works full-time. The families at the greatest risk of poverty are those where no parent works, or no parent works full-time. Working single parents have a greater poverty risk than couples but, due to higher in-work support through working tax credit, are less likely to fall below the Child Poverty Act relative poverty threshold than a couple where only one parent works (i.e. a lower proportion of single parents working full-time are in poverty than couples where one parent works full-time). However, this measure of income is likely to underestimate the higher cost of living for single parents. Couples benefit, for example, from shared rent and lower childcare costs.

Large families with three or more children are more likely to be in poverty, as are families where at least one parent has a disability. Families where the youngest child is not yet five have a higher poverty risk due to the implications for the working status of parents. Ethnicity is correlated to some degree with poverty risk. Children from a Pakistani, Bangladeshi, African or Caribbean British and non-Chinese Asian background are over-represented, whilst children with Indian, Chinese and white British backgrounds are under-represented.

Barnes and Lord (2013) examined the links between poverty, economic status and skills. Among families in poverty, there were four typologies:

- male breadwinner couples where the father is working full-time and the mother is looking after children and/or working part-time;
- out-of-work, low-skilled single parents;
- out-of-work couples with low to medium skills, usually where at least one parent is seeking work; and
- families in a variety of work situations with low or no skills.

Barnes and Lord note that the experience of poverty is not static and, in thinking about approaches to reducing long-term poverty, it is important to look at both families currently living in poverty and families at risk of poverty. The two most significant poverty risk factors for parents with children are being out of work and having low or no skills. Barnes and Lord note that the availability and accessibility of childcare may be a key barrier in both cases, but also highlight many parents' desire to stay at home.

Broadly, child poverty data suggests that participation in work is vital to avoid poverty, but that the nature of this participation is also critical: working for prolonged periods in low skilled occupations will not necessarily help parents achieve a decent standard of living. The childcare system must therefore not only support parents to work but, alongside flexible work policies, provide sufficient flexibility to support parents to progress in work and foster access to education and training. The increasing importance of education levels and skills to long-term employment prospects also seems to reinforce the importance of high quality early education as a platform for children's development.

How well does the current childcare system help to reduce poverty?

This report builds on an evidence review, *Early childhood education and care and poverty*, written by Eva Lloyd and Sylvia Potter of the University of East London (Lloyd and Potter, 2014), a summary of which is provided in Appendix A.

High quality childcare and effective early intervention

Currently, a gap opens in average developmental outcomes for children from different backgrounds by the time they reach school. In 2013, 36.2 per cent of children eligible for free school meals were assessed as reaching 'a good level of development', as measured by the Early Years Foundation Stage Profile test administered in reception class, which compares with 55.2 per cent of children not eligible for free school meals (Department for Education, 2014). This translates into a development gap of a year and a half between the most and least disadvantaged children by the time they reach age four. The development gap is variable around the country, with the proportion of children reaching a good level of development ranging from 60 per cent in some London boroughs to as low as 18 per cent elsewhere (Ofsted, 2014).

The situation in the rest of the UK is hard to assess; both Scotland and Northern Ireland do not measure development at school entry, and children in Wales do not receive a developmental check until age seven. However, there is evidence from targeted research that suggests that similar development gaps persist across the UK (Save the Children Scotland, 2012; Welsh Government, 2014).

Lloyd and Potter (2014) highlight that the achievement gap among children from different background stems from the context of a child's life and a range of influences 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 this 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.

Drawing on Lloyd and Potter (2014), it is possible to summarise key characteristics of childcare that has the greatest impact on disadvantaged children:

- 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 staff qualifications, adult-child ratios and group sizes, a mixture of children from different social backgrounds, and access to adequate physical space such as green spaces.

- Duration of attendance. Disadvantaged children benefit from a longer duration of early education, i.e. beginning before age three, but full-time attendance has no benefit over part-time attendance (nor is it detrimental, so long as care is high quality).

These factors are inter-dependent and are all necessary to secure the benefits of early education for children. There is some research into the effectiveness of the free early education offer which suggests that this policy has had a limited effect on outcomes for children (Blanden et al., 2014). The House of Lords Affordable Childcare Committee inquiry noted that there is a lack of robust data evaluating the effectiveness of free early education. The committee found that there is sound evidence of the effectiveness of high quality early education in improving children's outcomes, particularly for the most disadvantaged children, but that the government has failed to align the policy with the evidence of the characteristics of high quality care (House of Lords, 2015).

Recent research in England suggests that early years provision in maintained schools serving the most disadvantaged children is of comparable quality to schools that serve the more advantaged children (Mathers and Smees, 2014). Outside school settings, however, there is a pronounced negative quality gradient, with private and voluntary providers located in poorer areas scoring lower on quality measures that are important to improving outcomes for disadvantaged children, such as staff-child interaction, support for learning, language and literacy, and provision for diversity and individual needs. Ofsted grades are a less robust measure of quality than the research measures used by Mathers and Smees, but do serve to highlight general trends in quality. In January 2015, some 15 per cent of children receiving free early education in England were attending in settings judged by Ofsted to be in need of improvement or inadequate (Department for Education, 2015).

Children in the most disadvantaged areas are more likely to receive early education in a maintained setting. However, even in the most disadvantaged areas between 25 and 50 per cent of children access the offer in private and voluntary settings (Gambaro et al., 2013). Notably, 95 per cent of children eligible for the early education offer for two-year-olds in England, which was conceived as an early intervention measure, attended settings in the private and voluntary sector (Department for Education, 2015). This is because few schools have historically offered nursery facilities suitable for two-year-olds or have been offered support to expand their facilities to accommodate two-year-olds. This fragmentation of settings is problematic, as it causes children targeted by early intervention policies to move through multiple settings and transitions before they begin school.

In January 2015, 49 per cent of three- and four-year-olds and 45 per cent of two-year-olds, accessing the early education offer in England at a private or voluntary setting, benefitted from direct contact with graduate staff. In Scotland, 60 per cent of three- and four-year-olds receive teacher-led care and 74 per cent have 'non regular' support from teachers (National Statistics, 2014). The Welsh Government does not publish comparable data on the proportion of children receiving free early education with access to teacher-led care, but workforce survey data suggests a similar level of performance. There is significant variation among local authorities with, for example, 13 per cent of children attending private and voluntary settings in Newham accessing graduate-led care compared with 78 per cent in Knowsley.

Figure 7: Ofsted grades by area, all non-domestic early years provision

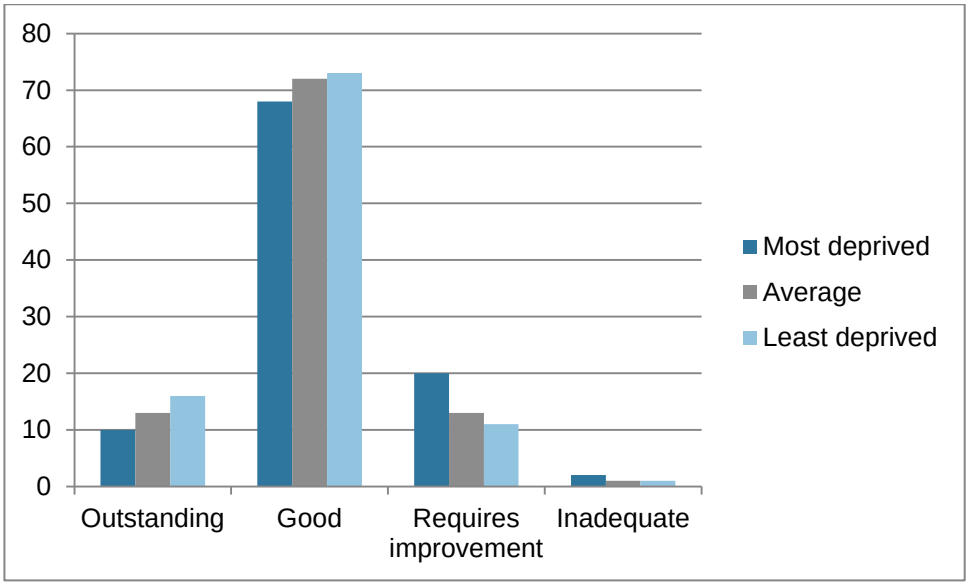
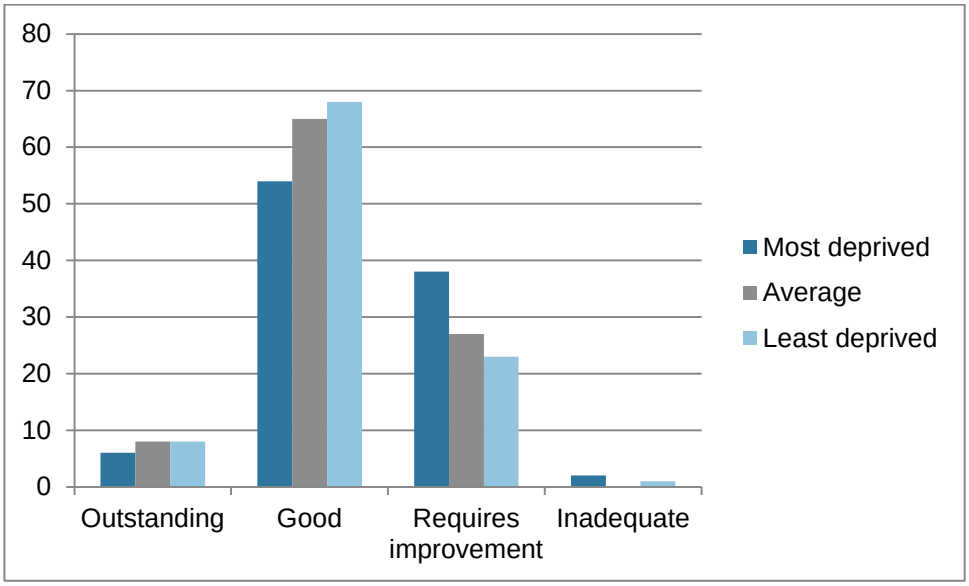


Figure 8: Ofsted grades by area, childminders



Source: Ofsted Data View, inspection data as of 31 March 2015; childminder inspection data as of 31 August 2013

Figures 7 and 8 illustrate the quality gradient between the most and least disadvantaged areas in England. The Ofsted rating of the setting in which a child receives early education may, however, not be a good predictor of the child's education development by the time they reach school. The Early Years Foundation Stage (EYFS) inspection framework focuses on structural factors to the relative neglect of 'process' quality factors such as the quality of interaction between staff and children. This means that Ofsted ratings do not capture all the elements of quality that are predictive of outcomes for children (Mathers et al., 2012). The EYFS framework is also not specifically designed to measure the presence of interventions that aim to improve outcomes for disadvantaged children. For example, the EYFS refers to

supporting the home learning environment but offers little guidance as to what this should mean or how success can be measured. Ofsted noted some of these issues in its most recent annual early years report (Ofsted, 2014). These issues are mirrored in devolved regulatory arrangements, which are also undermined by the separation of 'care' and 'education' standards that have been integrated under the EYFS in England.

The Nutbrown Review provided a coherent set of recommendations in England to drive workforce development in the early years, but many of its most important recommendations have not been pursued by the government (Department for Education, 2012a and 2012b). These include a phased plan to require all early years staff working 'within ratio' (that is, excluding those in training or volunteers) to have a tertiary early years qualification by 2020; to create parity between teaching qualifications in the early years and those in schools; and to consider ways to increase the proportion of graduates in the early years.

The devolved administrations have each set out more detailed workforce development plans: in Wales through a ten-year plan for the development of the early years workforce published in 2014; in Scotland through an ongoing independent review of the early learning and childcare workforce; and in Northern Ireland through the Bright Start Workforce Development Programme. However, the devolved administrations are constrained in the pace of quality improvement as funding allocations for early education follow from policy decisions in England.

Quality cannot be fully understood without taking account of wage levels, which have implications for the educational background, motivation and commitment of staff (Mathers et al., 2014; Department for Education, 2012a; 2012b). Early years staff are among the lowest-paid professional groups in the labour market; non-supervisory staff in private and voluntary daycare providers earn on average £6.80 per hour whilst senior managers earn £11.20 (Brind et al., 2014). Staff in maintained settings fare comparatively well, with staff in the same categories earning £9 per hour and over £20 per hour respectively. In the context of anti-poverty strategies, it is clearly significant that the majority of early years staff – 98 per cent – are women and many will be parents themselves. The childcare workforce is substantial: around 600,000 staff work across childcare settings (including childcare for school-age children), many of those are part-time. The level of pay the government subsidises is therefore itself a significant influence on poverty.

Children's centres

The children's centre programme has entered an uncertain phase. Sure Start children's centres and their devolved equivalents continue, alongside health services, to be the principal driver of local early years early intervention through child and family support services. This includes, for example, child and maternal health and health visitor services, maternal and infant mental health services, parenting programmes, social work, and training and employability services. Whilst evaluation of the children's centre model is ongoing, there is little question about the importance of the services the programme is designed to deliver, and effective integration of these services, in improving outcomes for children (Wave Trust, 2013). The intention of the children's centre programme in England was to ensure that every family had access to these services by establishing 3,500 centres nationally. Funding retrenchment has seen the number of children's centres fall – there are now approximately 2,800 children's centres – and, as a result, an increasing shift from universalism to targeted approaches. (All children's centres target families within populations with specific services: the challenge of offering a 'universal' service is therefore to reach all families in order to offer targeted services to those who stand to benefit from specific interventions.)

Various sources show steep cuts in spending on children's centres and early intervention services. The Early Intervention Grant, from which the majority of funding for children's

centres is drawn, fell dramatically in value between 2010 and 2015. Estimates of the scale of funding reductions in England over this period range from 55 to 32 per cent (Stewart and Obolenskaya, 2015; Barnado's, 2015; National Children's Bureau, 2015).

The striking nature of these cuts reflects, in part, a diversion of a significant proportion of early intervention funding to the free childcare offer for two-year-olds. This redirection of funding is problematic: pilots for two-year-old offers demonstrated that the most effective programmes developed partnerships with parents and made links with family support and early intervention services (Gibb et al., 2011; Georgeson et al., 2014). The aim of the two-year-old offer is to improve outcomes for the children targeted, but this policy is unlikely to prove effective if free early education is funded at the cost of wider early years services. There is evidence that early years early intervention is not as effective as it should be, due in significant part to patchy implementation of best practice standards (Wave Trust, 2013).

Scotland does not have a children's centre network, though there are many comparable family centres. Instead the Scottish Government has set out a policy framework, the Early Years Framework, which ties together early years providers from all sectors and wider child and family support services. The approach developed by the Scottish Government arguably has the potential to be more joined up than the fragmentation of children's centres, maintained childcare provision in schools, and private and voluntary childcare provision in England. However, less focus on centre-based models and co-located services may also lead to the failure to build integrated teams and services and under-investment in targeted early intervention services. In the absence of robust research, it is difficult to assess the relative merit of these different approaches and each may be potentially successful.

In Wales, the Flying Start programme reaches around 31,000 children aged three and four (there are approximately 170,000 children under five in Wales). Flying Start consists of support for early language development, an enhanced health visitor programme, parenting support and free early education for two-year-olds (in addition to the free early education offered to all three- and four-year-olds in Wales). The Flying Start model has been criticised because it is area-based: all children in an area receive free services, including early education for two-year-olds, regardless of income. This approach has the benefit of universalism but also means many disadvantaged children and families outside Flying Start areas do not benefit from help. Flying Start is in a process of expansion, with the Welsh Assembly Government aiming to reach 36,000 children by 2016. The complementary Families First programme, which is not area based, aims to improve outcomes for families, especially for those in poverty. Families First has a broader remit than Flying Start, covering, for example, supporting families into employment, health targets such as immunisation rates and reducing homelessness. It also has more flexibility than Flying Start in the scope of local services.

Affordability

Figures 9 to 15 illustrate the impact of childcare costs on families with pre-school children. The greatest financial 'crunch point' for families tends to arise when one or more children are aged under two (and, therefore, don't have access to free early education) and both parents are working. Support through Universal Credit will be relatively good at holding costs below 15 per cent of disposable income, except where families exceed the maximum childcare element caps, as is the case in London (where high housing costs also reduce disposable income significantly). Increasing childcare support for such families would help reduce income poverty but other options such as reducing the Universal Credit taper rate or introducing a second earner's work allowance are needed to significantly improve family incomes.

Figure 9: Income after childcare, couple earning the National Minimum Wage with one pre-school child[5]

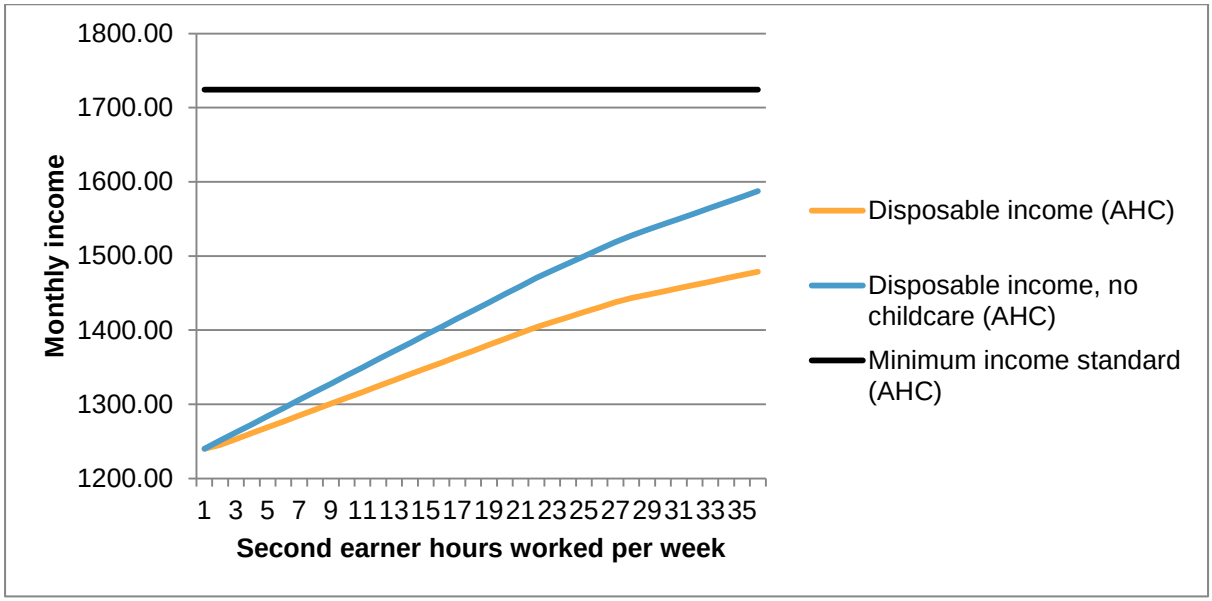


Figure 10: Income after childcare, couple earning the National Minimum Wage with two pre-school children

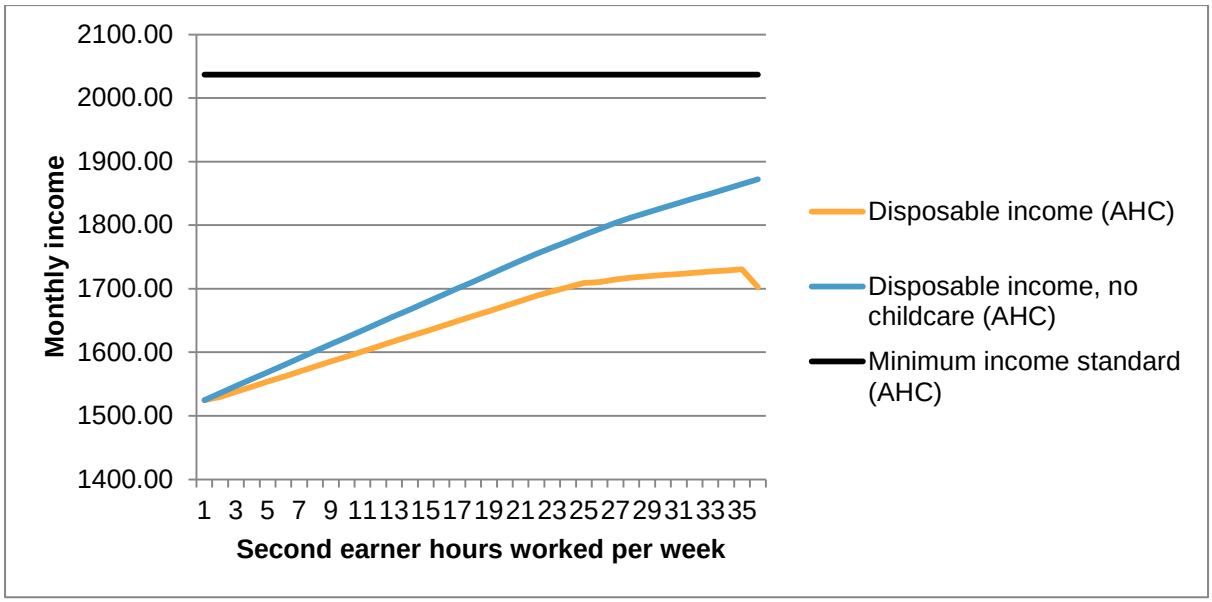


Figure 11: Income after childcare, couple earning the National Minimum Wage with three pre-school children[6]

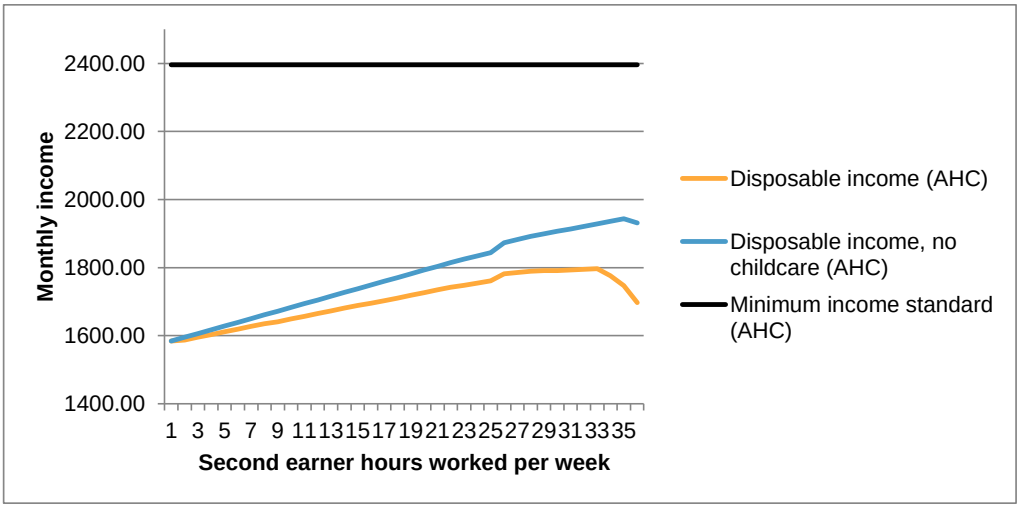


Figure 12: Income after childcare, single parent earning the National Minimum Wage with one pre-school child

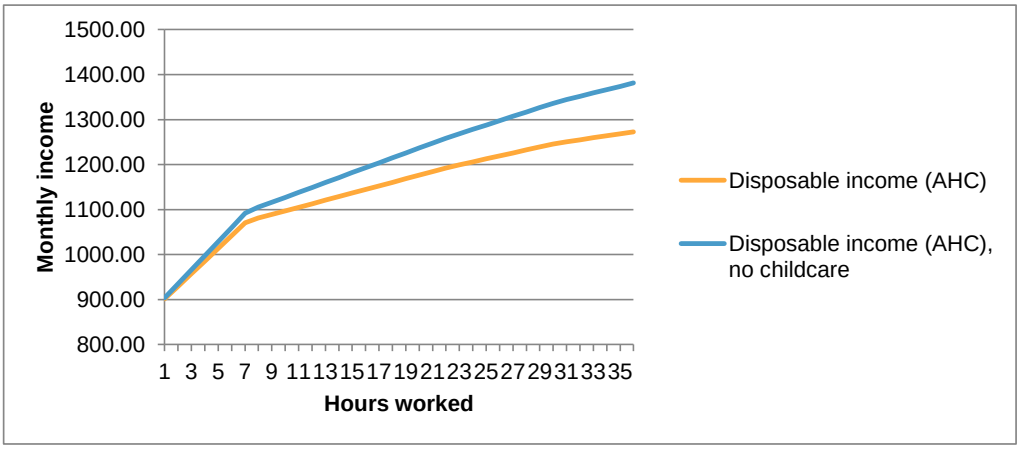


Figure 13: Income after childcare, single parent earning the National Minimum Wage with two pre-school children

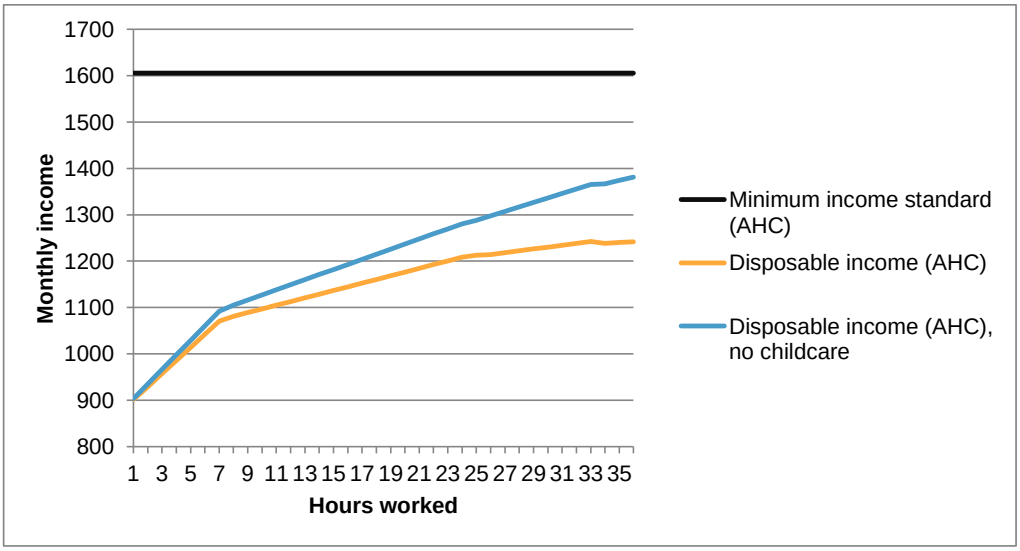


Figure 14: Income after childcare, single parent earning the National Minimum Wage with three pre-school children

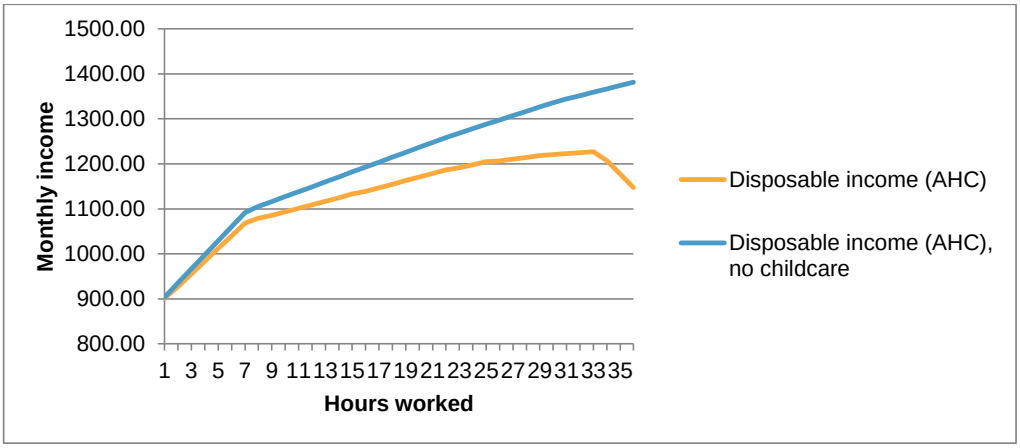
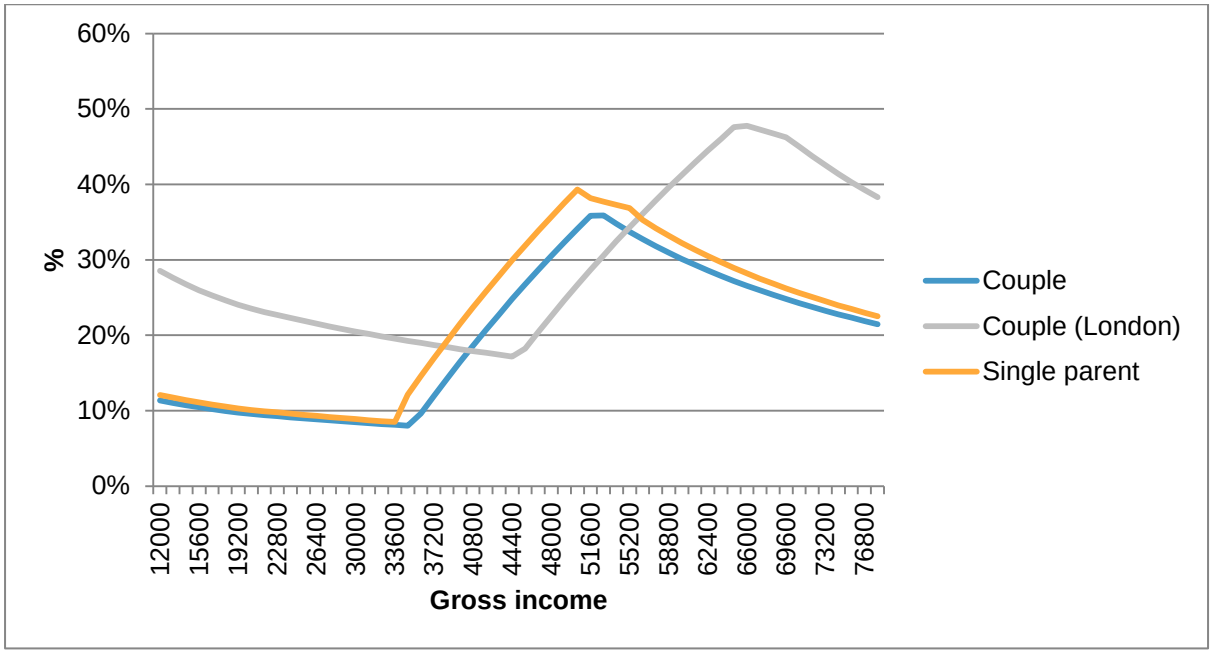


Figure 15: Percentage disposable income spent on childcare, family with two pre-school children[7]



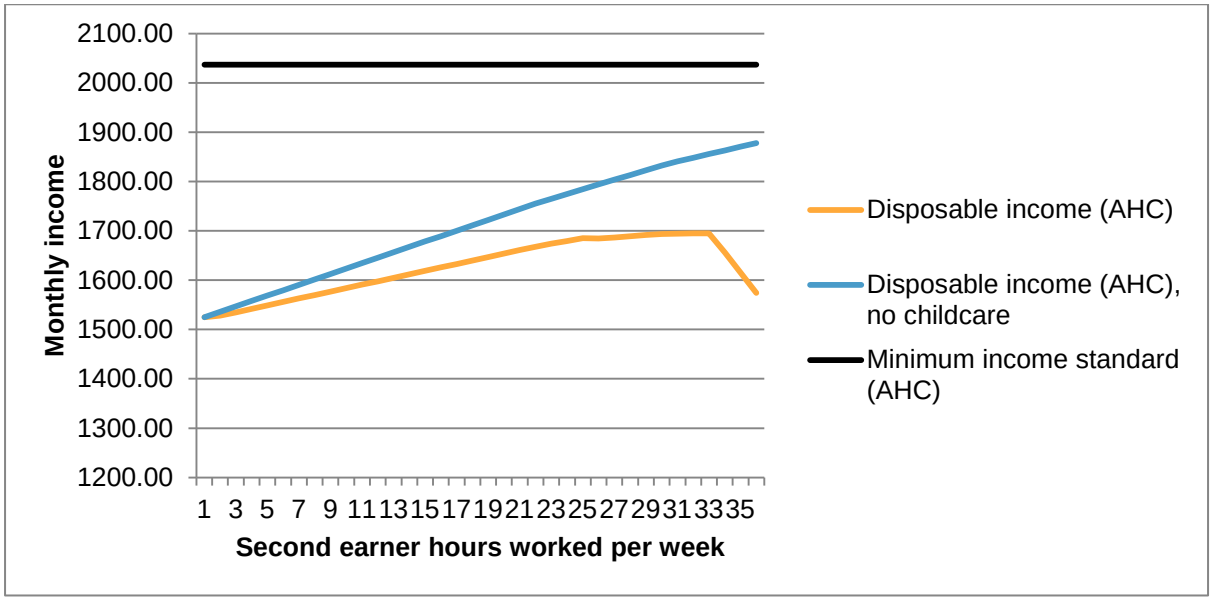
Specific groups of families will be affected in different ways by the structure and limitations of support through Universal Credit. Families who live in London and the South East may in particular be affected by the childcare element caps, whilst families with more than two children will be affected by both this cap and the government's decision to limit the childcare element to the first two dependent children. Figure 16 sets out the impact of childcare element caps in different regions of Britain for families purchasing full-time childcare. The table illustrates the impact of extending free childcare to 30 hours: most parents with a child, age three or over, are now unlikely, for the foreseeable future, to be affected by the caps, unless they live in London. Table 8 illustrates how the combination of high childcare costs and capped support affects a family with two pre-school children in London. It is harder for this family to move above the poverty line through work and incentives for the second earner are minimal.

Figure 16: Impact of Universal Credit childcare element caps on families using full-time childcare[8]

Region		One child	Two children	Three children
East of England		177.6	216.3	274.67
East Midlands		190	228.79	290.63
London		243.2	284.87	378.7
North East		176.8	215.32	271.04
North West		170	206.81	267.4
South East		213.2	259.37	325.47
South West		183.6	222.75	284.29
West Midlands		180.4	217.03	279.4
Yorks and Humber		154.4	187.61	249.99
England (regional average)		187.6	227.83	292.58
Scotland		176	266	289.9
Wales		166.8	259.95	259.67

= Costs lower than cap
= Costs exceed cap by less than £10
= Costs exceed cap by more than £10

Figure 17: Income after childcare, couple earning the National Minimum Wage with two pre-school children in London[9]



Working tax credit statistics suggest that fewer than five per cent of families using the childcare element of tax credits claim the maximum amount of allowable childcare costs for at least one child (HMRC, 2015).[10] However, the number of families claiming the maximum allowable amount of childcare costs may be a poor measure of the number of families affected by the cap, since any families affected would not appear in these figures if the cap makes claiming childcare support and working economically unviable. If the childcare element caps do not rise, the number of families captured by the cap will gradually rise. The issue illustrates that it is difficult to achieve a balance between controlling costs and meeting the fair costs of childcare, taking into account regional variations, within the relatively blunt structure of the Universal Credit childcare element.

These family models also do not take into account the practicalities of arranging childcare, which may create additional obstacles and challenges for parents returning to work. There is some evidence that take up of support with childcare costs is lower than might be expected: in 2011, a HMRC review found that around 81 per cent of eligible parents were accessing the childcare element of tax credits (HMRC, 2011). This figure is for parents who are using childcare and do not claim support, presumably usually because they are not aware support is available. There may also be parents who might consider using more childcare, but are discouraged because childcare fees must be recovered through tax credits, which entails the risk of tax credit under- or over-payment and subsequent problems for family budgeting. There is some evidence that families with low incomes are more likely to be isolated from information about childcare support and that there is a need to improve parental understanding of the support and services on offer (Campbell-Barr and Garnham, 2010).

New challenges will be presented by Universal Credit. Parents will receive a Universal Credit payment one month in arrears, which means that they will need to pay not only the first month of childcare fees, but also any deposit and registration fee in advance. Unless the date of the Universal Credit payment and the date on which a monthly childcare fee is paid are aligned, families could also experience ongoing difficulties meeting childcare fees from a limited household budget. Families who have fluctuating childcare costs may also find the Universal Credit system cumbersome because they will often have to meet a spike in fees, such as holiday childcare costs, and recover this additional spending in arrears. These

issues are discussed in detail in the recent Citizens Advice Bureau report *The practicalities of childcare* (Citizens Advice Bureau, 2014).

The government has created a budgeting advance facility for Universal Credit that will allow parents to take out an interest-free loan of up to £812, which is paid back over up to 102 weeks. The scheme is only available to parents with an income of less than £3,600 in the last six months, or £2,600 for single parents, and only one budgeting advance can be taken out at a time. These requirements will exclude the majority of families from the facility and limit the utility of the scheme to families who must meet advance fees that may often exceed the maximum amount (particularly where families have another need for the budgeting advance).

Support with childcare costs in Universal Credit is linked directly to work participation. There is no entitlement to cover jobseeking itself, interview preparation and training such as short courses. The discretionary Jobcentre Plus Flexible Support Fund may provide *ad hoc* support to parents with childcare costs, but is typically used for low-cost support such as attending an interview. National expenditure through the fund, which is used broadly to support jobseekers to move closer to work and is managed at a local level, was £122.3 million in 2012-13.[11] There is no data available on the proportion of the fund that is used to support families' childcare needs.

Whilst free childcare may help parents with two- to four-year-olds to access work preparation and jobseeking activities, the flexibility of this support is limited by patterns of early education – typically morning or afternoon sessions – which parents must usually give notice to change. There is also childcare support available for students, for example in England through dedicated schemes such as the Childcare Grant for undergraduates or Care to Learn, which provides childcare help for college students aged under 20. However, this assistance helps specific groups of parents and does not offer the flexible support needed by jobseekers and many older parents seeking to address education and skills gaps.

Access and flexibility

Pre-school childcare outside of free early education is principally used by working parents: couples where both parents are in work use a median of 26 hours of childcare each week and single parents in work use a median of 35 hours each week. Around 44 per cent of pre-school children receive childcare from two or more providers, most commonly through a combination of centre-based and informal care. Childminders are used by six per cent of working parents with pre-school children, whilst one per cent of parents report using nannies or au pairs. Half of parents say that they have access to regular informal childcare with a family member, ex-partner or friend; just over one-third of parents with pre-school children regularly use informal care.

There is strong evidence of unmet demand for work among parents. A 2013 survey of work decisions among parents with children, commissioned by the Department for Work and Pensions, found that 54 per cent of parents with a youngest child aged zero to two and 60 per cent with a youngest child aged three to four wanted to find work or work longer hours where they and their partner did not already work full-time (Borg and Stocks, 2013). This preference was perhaps unsurprisingly strongest for parents with low incomes.

Parenting preferences and norms vary widely and effective public policy must recognise this diversity and the valid choice to parent young children (Judge, 2015). Participation in low quality work is not a silver bullet to reduce poverty and policy should seek to frame incentives for parents in a long-term context. Introducing excessive pressures on parents to work, and increasing stigma, may exacerbate rather than mitigate stresses within families that contribute to poor outcomes. An effective anti-poverty childcare system is an enabling

system that widens opportunity and supports parents to realise their aspirations. Alongside access to childcare in order to work this means, for example, a network of early years support around the family and help with childcare to build skills, access education and develop work readiness.

Recent evidence suggests that free early education has had a relatively small impact on mothers' employment. Brewer and Crawford (2010) found a small, but significant, positive effect on the employment rate of single parents after their children started to receive free early education at four years, although this effect was not achieved by free early education alone. More recent analysis of the expansion of free early education to three-year-olds showed that this intervention led to a rise of about three per cent in the employment rate of mothers whose youngest child was age three, with a further three per cent starting to look for work after their child received this provision (Brewer et al., 2014a). The authors concluded that better qualified women among this cohort of mothers were more likely to move into work. Beyond this study, we lack robust evaluations of the effect of childcare subsidies – including free early education, tax credits and vouchers – on parental employment.

Survey evidence suggests there are several principal barriers to work for parents with pre-school children, including access to a job with suitable hours, meaningful financial incentives and sufficient education or skills (Huskinson et al., 2014). Childcare also remains a significant barrier. Among mothers not in paid work with pre-school children, one in five state that childcare issues prevent them from working, whilst among working mothers with low or no qualifications, thirty per cent say that they would work longer hours if they could arrange good quality childcare which was convenient, reliable and affordable.

Access and flexibility problems relate primarily to the relative lack of flexibility in the hours of care available in many providers and the lack of availability of places for children under three. Poor access to affordable, flexible daycare for families on low incomes presents a significant policy challenge. Working parents with pre-school children who do not have access to informal care generally need access to a daycare place or a childminder. Both are less prevalent in areas of concentrated disadvantage due to limited commercial interest and the difficulty of operating sustainably with lower demand and lower margins (Dickens et al., 2012). The universal early education offer ensures access to a childcare place for children in specific age groups but, particularly in schools and sessional providers, these places may be available only for a limited number of hours at specific times.

In 2013, uptake of universal three- and four-year-old provision stood at 96 per cent of eligible children in England and 98.5 per cent in Scotland, although there are some differences in take-up among local authorities (there are currently no comparable figures for Wales and Northern Ireland). Uptake for two-year-olds is lower, standing at 58 per cent of eligible children in England in January 2015, although in some urban local authorities uptake was considerably lower. In Wales, the uptake of free early education among children who qualify for Flying Start provision is above 80 per cent in most local authorities. In Scotland, there are much larger variations in the uptake of free early education for two-year-olds living in workless families with uptake as low as 10-20 per cent of eligible children in some local authority areas.

The current pattern of early years services in the UK reflects two historical trends: the post-war development of early years provision in schools and voluntary settings to serve disadvantaged children, particularly in urban areas, and the growth since the late 1990s of a large private daycare market to meet demand driven by parental employment. Whilst the investment in maintained pre-school care is positive in itself, the more recent market-based evolution of services means that in many areas a schism has developed between voluntary and school-based childcare providers, which tend to offer parents a limited choice of hours,

and private daycare providers, which serve parents in employment and offer more flexible 'full' daycare hours.

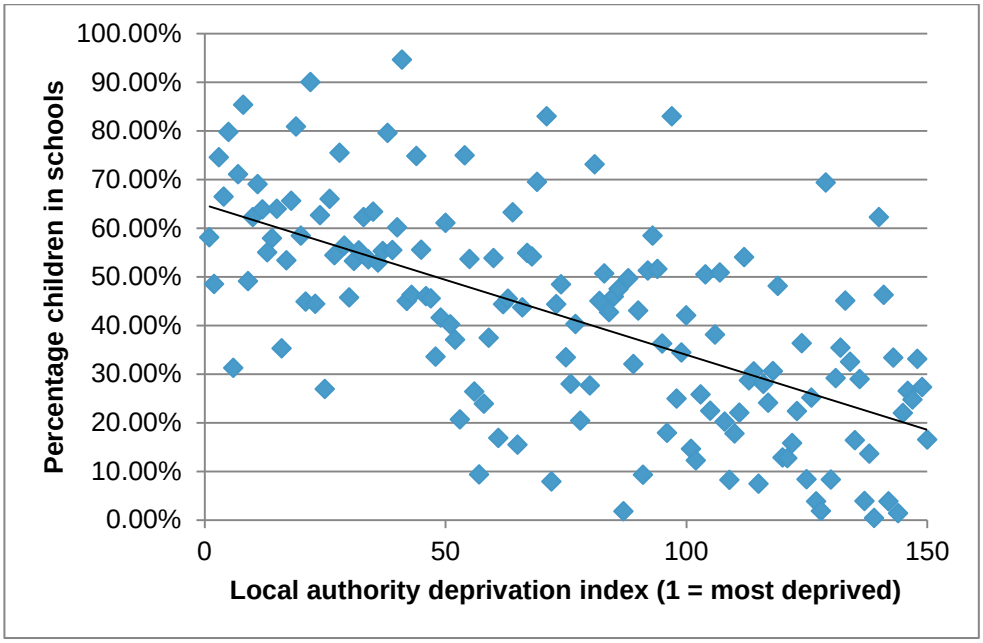
Figure 18: Number of early years providers by type (England)

	Total	30% most deprived areas (% total)	70% least deprived areas (% total)
Full daycare	17,900	4,500 (25%)	13,500 (75%)
Sessional	7,100	1,800 (26%)	5,300 (74%)
Childminders (working)	46,100	8,300 (18%)	37,800 (82%)
Nursery schools	400	250 (63%)	150 (37%)
Primary schools with nursery and reception classes	7,600	3,000 (39%)	4,600 (61%)
Primary schools with reception by no nursery class	8,800	1,100 (13%)	7,700 (87%)

Source: Brind, R., McGinigal, S., Lewis, J., and Ghezelayagh, S. (TNS BMRB), with Ransom, H. Robson, J., Street, C. and Renton, Z. (NCB Research Centre) (2014) *Childcare and Early Years Providers Survey 2013*

Figure 19 illustrates the correlation, though far from uniform, between local authority deprivation and the proportion of children in nursery classes. This data is presented at a local authority level and may mask a stronger likelihood that children will attend a nursery class in less affluent areas. These trends appear to be similar across the UK. However, little comparable data is available in the devolved administrations.

Figure 19: Three-year-olds in England in maintained early education provision by local authority deprivation



Source: Department for Education statistical release, *Provision for children under 5: January 2015*; English Indices of Deprivation 2010

There is currently no national data on the proportion of nursery classes that operate extended hours and offer the same flexibility as daycare providers. (The Department for Education recently committed to publishing information on extended hours as part of the schools performance tables, but it is not yet clear if this data will extend to nursery classes.) A survey of primary schools commissioned by the Department for Education in 2014 found that 53 per cent provided access to both before- and after-school care and 15 per cent also provided access to holiday childcare (TNS BMRB, 2014). However, these figures do not distinguish between early years and primary school age provision. Few nursery classes and sessional settings provide care for children aged under three (less than three and nine per cent respectively), whereas around 18 per cent of places in daycare providers are for under-threes (Brind et al., 2014).

Survey data suggests that more than twice as many families where both parents work use daycare compared with families where neither parent works. Conversely, twice as many families where neither parent works use a nursery class attached to a school as families where both parents work (Huskinson et al., 2014). When parents are asked about the primary reason for using a particular childcare provider, 77 per cent of parents using a nursery class see the reason for using the service as 'child related' and 33 per cent as 'economic' (parents can choose both reasons); for day nurseries these proportions are inverted, with 82 per cent of parents mentioning an economic motivation and 43 per cent child-related reasons.

Rising demand from working parents for daycare has driven a long-term decline in sessional provision, as these providers convert to daycare (Brind et al., 2014). However, the number of sessional providers is actually rising in the most disadvantaged areas, with 1,800 providers in the 30 per cent most deprived areas in 2013 compared with 1,600 in 2011. In contrast, the overall number of sessional providers fell from 6,300 to 5,300 between 2011 and 2013 in the 70 per cent least deprived areas. Demand for sessional provision in the most disadvantaged

areas is being driven by the roll-out of the early education offer for the most disadvantaged two-year-olds. As one of the policy rationales for the offer is to support parental employment, the need to fall back on sessional models to create sufficient places is problematic. Ideally, new places would be flexible enough to support working parents.

Childminders are also less common in the most deprived areas with 18 per cent of the total number of registered childminders in the 30 per cent most deprived areas (Brind et al., 2014). Childminders are important to working parents with complex childcare arrangements (for example, because they have two or more children of different ages), who prefer a home-based care environment or only have access to short hours of centre-based childcare provision.

3. An anti-poverty childcare system

This section of the report sets out concrete steps UK governments can take to create a childcare system that contributes to an effective poverty reduction strategy, taking into account Lloyd and Potter's (2014) recommendations and our analysis of the strengths and weaknesses of current childcare provision. We have pursued a 'modular' approach, setting out a package of reform, within which individual policies might be pursued as stand-alone options. We look, in turn, at high quality early education and the role of childcare in effective early intervention, improving childcare access and flexibility, and financial support for parents. Finally, we set out how simplifying childcare subsidies can help to achieve poverty reduction priorities.

Prioritising high quality early education and effective early intervention

Lloyd and Potter (2014) highlight that many childcare settings, particularly in the private and voluntary sector, lack the key elements of high quality care. There are four quality priorities to realise the potential of childcare to improve outcomes for the most disadvantaged children:

- increasing the proportion of early years graduates and qualified staff (those with at least a tertiary early years qualification) in childcare settings;
- supporting the pedagogical capability of the early years workforce through training and continuing professional development;
- ensuring providers deliver effective interventions to support development and prevent children from falling behind; and
- ensuring all childcare settings have strong links with family support and specialist early intervention services.

Early years graduates

A national Graduate Leader Fund operated in England from 2007 to 2011 (following on from the similar 2006-07 Transformation Fund). The national evaluation of the Graduate Leader Fund found the scheme had a positive impact. Settings that gained a graduate made significant improvements in quality and the presence of a graduate added value over and above their individual contribution through setting-wide improvements in practice and planning (Mathers et al., 2011). More recently, research into quality among providers serving disadvantaged children found that one of the key factors in high quality private and voluntary provision was the presence of an early years graduate (Mathers and Smees, 2014).

The Graduate Leader Fund ended in 2011 but the Department for Education has encouraged local authorities to continue to provide incentives for private and voluntary providers to develop graduate provision using the early years funding block. As a result, the number of graduates in settings has continued to increase. The proportion of three- and four-year-old children receiving the early education offer in direct contact with a graduate rose from 34 per cent in 2010 to 48 per cent in 2014 (Department for Education, 2014). However, the proportion of staff with a graduate-level qualification in daycare settings – 13 per cent – continues to significantly lag behind maintained settings where between 35 and 40 per cent of staff have a graduate qualification (Brind et al., 2014). Moreover, despite recent progress, at the current rate of increase, private and voluntary settings will not become fully graduate-led for around 20 years.

Given the evidence of the role of graduates and properly trained staff in supporting good outcomes for the most disadvantaged children, the government should prioritise making the early years a graduate-led, fully qualified profession. Many local authorities no longer operate graduate incentive schemes or have scaled back support, putting greater pressure on providers to absorb the additional cost of graduates directly or through parental fees. The cost of graduates is significant – graduate staff are typically paid more than a third more than staff with a tertiary qualification – and it is unlikely a significant increase in the proportion of graduate staff is sustainable without identified funding.

UK governments should prioritise transforming pre-school childcare into a graduate-led profession by establishing new training incentives and supporting providers with costs whilst their staff are training. Governments should also end ambiguity about quality requirements in early education by incorporating qualification incentives into the free early education funding framework. This means setting statutory requirements that require providers to employ qualified staff and adjusting funding allocations to ensure that a qualified workforce is properly funded.

Recommendation: UK governments should commit to a fully graduate-led early years workforce, supported by funding to meet training and wage costs

Cost: £200 million rising to £500 million

Funding for free early education

The Pre-school Learning Alliance commissioned research in England into the cost of high quality care in private and voluntary settings that helps to substantiate the funding shortfall between current funding levels and the investment needed to sustain a high quality model (Ceeda, 2014). One key aspect of quality is that all staff have a tertiary early years qualification. However, funding shortfalls are not simply an issue of qualifications. Characteristics of effective settings that may be absent where funding is insufficient include time spent reviewing each child's development, working with a child's parents and professionals outside the setting, and staff participation in continuing professional development.

The drivers of improvements in child outcomes relate to the skills, knowledge and experience staff bring to their role. Providers have raised concerns that an excessive focus on increasing the presence of qualified staff may place too much emphasis on young professionals and graduates, many of whom are inexperienced, and also neglect the pathway towards a skilled, confident and effective workforce. An excessive emphasis on qualifications also risks neglecting the development needs of experienced staff in the sector who often spend the most time with children. In addition to ensuring that early years graduates are supported into the profession at a sustainable rate, UK governments should also consider what can be done to improve professional development and support for the early years workforce.

Ceeda found that the funding shortfall per hour between average allocations by local authorities to providers and the actual cost of high quality care is on average 21 per cent for three- and four-year-olds, and 18 per cent for the two-year-old offer (Ceeda, 2014). Some settings are able to offset this shortfall by cross-subsidising care using fees from additional hours purchased by working parents. Other settings are simply unable to deliver high quality care. One of the reasons daycare settings serving high concentrations of disadvantaged children can struggle to achieve high quality care is that they are least able to cross-subsidise using parental contributions.

In addition to adjusting early education allocations to reflect the cost of graduate-led care, governments should recognise the additional costs of a high quality delivery model, in which, staff spend an appropriate amount of time monitoring children's progress, planning care and activities, liaising with parents and other early years services, and accessing continuing professional development. Many staff, including those with early years qualifications, do not feel they are well prepared to work with children with additional needs, engage and support families, and for multi-agency working (Georgeson et al., 2014), key aspects of care needed to work effectively with children most at risk of falling behind their peers.

Recommendation: Early education funding should be increased in order to fund high quality care

Cost: £425 million (assuming a universal two-year-old offer)

The Early Years Pupil Premium

The 2014/15 House of Lords Affordable Childcare Committee inquiry highlighted particularly that it is a false economy to invest in early education that is not of sufficient quality to improve outcomes for children (House of Lords, 2015). Alongside the evidence that it is the most disadvantaged children who benefit most from high quality early education, the committee recommended the government consider ways to target resources at the most disadvantaged children and noted that the Early Years Pupil Premium (EYPP) is available to achieve this.

The introduction of the EYPP is a welcome development that provides a meaningful socio-economic supplement for early education funding for the first time at a national level. However, there is a risk that the EYPP will become a stop-gap solution to inadequately funded early education and will be invested in meeting basic standards rather than in additional support for children. If settings are not already graduate-led, it makes sense for providers to use the EYPP to fund highly qualified staff, but this, in turn, means such settings will not be able to use the EYPP to deliver targeted interventions to children. The EYPP's central purpose, like the Pupil Premium in schools, should be to deliver specific interventions to improve outcomes for children who are less likely to do as well as their peers.

At present, the EYPP is too low – £300 per child each year – to allow providers to achieve a meaningful impact on outcomes and should be increased. As learning emerges on the impact of the EYPP and how it can be used effectively, this figure can be adjusted.

Recommendation: The Early Years Pupil Premium should be increased to £600 per child and extended to the two-year-old offer (and introduced in the devolved administrations)

Cost: £128 million

Early years regulatory frameworks and the home learning environment

Lloyd and Potter (2014) highlight that high quality care must promote home learning and positive attitudes to education. This is one of the key areas that distinguishes children from disadvantaged backgrounds who do well from those who struggle in school. New parents receive developmental advice through the NHS Start4life programme and a minority then receive ongoing support from health visitors or a voluntary service such as Home Start. Support and encouragement for parents beyond those experiencing serious problems can, however, peter out as children enter a critical stage of development. The free two-year-old offer in England, particularly, has been under-utilised as a mechanism to engage parents,

despite clear evidence from pilots that the most effective programmes seek to engage both a child and their parents (Gibb et al., 2011).

Early years staff are well-placed to encourage parents, provide families with materials and ideas, monitor progress and facilitate participation in local activities. Discussing a child's learning at home should be a routine and non-stigmatised activity. Support for home learning can be proportionate: for most parents, this support will be helpful (and optional), consisting of an additional discussion point in the regular meetings with staff that already occur. For parents who may not have a high level of awareness of how they can support their child's development, perhaps because they have not had a strong parenting role model themselves, establishing a visible norm and providing support will help to support positive parenting. This would also help ensure that opportunities to help families through wider family or early intervention services are identified and acted upon.

Recommendation: Duties in the Early Years Foundation Stage framework and devolved equivalents to support home learning should be clarified and strengthened

Children's centres

UK governments must also set a clear long-term pathway for children's centres and their devolved equivalents. Both Lloyd and Potter (2014) and Eisenstadt (2011) argue that a universal children's centre platform is essential to reach the neediest families. Wide participation in non-stigmatised programmes provides the means to reach those who benefit from additional support. The Coalition Government took a *laissez-faire* approach to the children's centre programme, allowing local authorities increasing latitude to choose the scope of children's centre networks. This approach may have been the best way to help local authorities use diminishing resources well, but has left a widening gap between the aspiration of universal early years provision and the reality of increasingly narrow targeting of services.

Early years services must particularly reach families when children are aged between zero and two, which is a critical period for a child's development (Wave Trust, 2013). Health visitors have the lead role in reaching families who may benefit from support before the beginning of early education. The recent expansion in health visitor numbers and the clear aspiration of an effective universal service is a positive development that should continue to be supported by UK governments. Where families receive support from a health visitor, this usually consists of five visits: four between conception and the child's first birthday and one subsequent visit when the child is aged between two and two and a half. Families with high needs may receive a more intensive visiting programme or, if the parent is aged under 20, support through the Family Nurse Partnership.

Health visitors play an invaluable role but are dependent on, and not a substitute for, key interventions, including intensive parenting support, stop smoking and substance misuse programmes and mental health services, as well as less intensive support such as parenting classes, nutrition advice and informal parent-child activities designed to promote secure attachment and positive parenting. Cuts to early intervention funding mean that the health visiting programme is not being supported by the suite of interventions needed to realise the programme's potential impact on families.

A lack of clear direction for children's centres also risks an increasing disconnection between free early education and specialist early intervention and family support services. The aims of free early education and the children's centre network in improving outcomes for the most disadvantaged children cannot be separated. Children's centres remain ideally placed to act as hubs supporting local childcare providers through access to specialist family and

children's services. Close links between children's centres and childcare providers also maximise the reach of children's centres.

The UK has made a substantial investment in the children's centre network. This network is at risk of becoming less effective due to budget cuts, which tend to foster a shift from preventative to reactive services, and a lack of a clear vision from government. Returning to a universal model and putting children's centres at the heart of early years networks would capitalise on the potential of children's centres, and the universal early education offer, to work in tandem to create comprehensive early intervention networks that reach every child and family.

A universal children's centre network requires a new approach. In England, the government's ambition has been to create sufficient children's centres for every child to access services. This aim was codified in legislation through the Childcare Act 2006 and through an initial target of 3,500 centres (which was achieved in 2009). However, austerity measures led to a retrenchment in services and, from 2009, services have been increasingly narrow and targeted. The devolved governments have faced a similar dilemma: where resources decline, it may be more effective to focus on developing fewer, more effective children's centres than to sustain a services that are 'hollowed out'. This inevitably means, however, a shift away from a universal model.

There is no easy answer to the challenge of ensuring intensive child and family support services reach all families that could benefit from support. We agree that it makes sense to focus resources on children's centre models that have been shown to be effective rather than spread funding too thinly. There are, however, also opportunities to develop new models that utilise the wider early years assets including schools and nurseries to reach children who do not fall within the reach of children's centres. Support services through early years provision are not a substitute for evidenced children's centre programmes, particularly in areas of high need. However, it does not make sense to fail to maximise early years assets to deliver a meaningful universal offer. Integrating child and family support services with childcare settings would create significant new opportunities in areas where the reach of children's centres is absent or limited.

There are, therefore, two key challenges the government must address: first, an effective universal early years model must be developed that balances strategically placed children's centres with alternative networked models linked to early years provision. Second, investment must be increased to properly fund a universal network.

Relevant regulatory frameworks should also be updated to integrate free early education and wider early years services. In England, the Early Years Foundation Stage framework and the children's centre inspection framework can be revised to encourage a closer working relationship between childcare providers and children's centres. This might include, for example, a requirement for a member of staff in early years settings to act as a liaison and work with the children's centre to reach target groups. Broadly, statutory guidance should create a tight framework where the roles of providers and children's centres are aligned around the same aims: providing high quality early education to all children, identifying children or families who may benefit from additional support, and providing an effective range of early intervention services.

Recommendation: UK governments should clarify the status and aims of children's centres (or devolved equivalents), ensuring that funding is sufficient to provide universal early intervention and family support services

Cost: £560 million

Early years developmental measures

Both Ofsted and the Social Mobility and Child Poverty Commission have highlighted that new arrangements must be established in the early years for monitoring children's progress to support a rigorous approach to early education (Ofsted 2015; Social Mobility and Child Poverty Commission, 2014). From 2014, the government in England introduced a baseline assessment in reception class, with the intention of making it easier to observe the success of primary schools in supporting children's development. This has, however, undermined delivery of the Early Years Foundation Stage Profile assessment in reception class, which will no longer be a statutory requirement. There is also scope to develop the now universal development check children receive at age two and a half so that it is possible to understand how children progress from that age. Early years providers must be able to understand to what extent they are succeeding in supporting children's development and in closing developmental gaps for the most disadvantaged. There is understandably concern among some professionals and parents about introducing formal testing in the early years. These arrangements must therefore be carefully designed with professionals and children to be age-appropriate and focused on suitable developmental measures.

Recommendation: UK governments should work with professionals and children to design an age-appropriate statutory assessment that ensures all children receive a developmental check on entry and exit from early education

Ofsted's role in assessing quality

Lloyd and Potter (2014) note that validated research scales such as the Infant/Toddler Environment Rating Scale and the Early Childhood Environment Rating Scale produce a more in-depth assessment of the different aspects of quality for different age groups associated with longer-term positive outcomes. Ofsted ratings, on the other hand, focus more on structural features of settings such as management and leadership arrangements. Lloyd and Potter add that this effect is most pronounced for the assessment of quality for children aged under three, where settings rated 'good' or 'outstanding' by Ofsted were virtually never rated as high quality when measured by the appropriate validated research instrument for under-threes. The aspects of quality regulators already measure are important. However, more finely grained structural and process quality measures could be better incorporated into standards and inspection frameworks.

There is currently too much ambiguity about the respective roles of local authorities and regulators in monitoring and supporting quality improvement in early years providers. Regulators do not currently have the funding or capacity to monitor providers outside of the four-year inspection cycle, nor provide intensive support for those providers most in need of improvement. Cuts to local authority funding are making it increasingly difficult for them to fulfil this role. Asking regulators to both inspect and deliver quality improvement programmes also creates a potentially unhelpful conflict between a regulator's role in challenge through formal inspection and the less formal relationship required for effective quality monitoring and support. The most effective route forward is to strengthen requirements in early years regulatory frameworks and in turn clarify how local authorities will work with providers to drive quality improvement, ensuring clear, distinct and properly resourced roles for both regulators and local authorities.

Recommendation: Ofsted and devolved regulators should align early years inspection frameworks with appropriate process quality measures

Improving wages for private and voluntary sector staff

In England, pay in maintained early years providers for all staff is 68 per cent higher than in private and voluntary settings (Brind et al., 2014). Low wages in childcare undermine care for children. Skilled workers are discouraged from considering a career in the early years and motivation among staff is often low (Mathers et al., 2014; Department for Education, 2012a and 2012b). Staff in maintained settings also benefit from better terms and conditions, and fewer work on temporary or flexible contracts. These differences mean that staff in private and voluntary settings are less likely to receive sufficient support and professional development.

Low wages among childcare workers contribute directly to working poverty, with an estimated 40 per cent of staff earning less than the Living Wage (Living Wage Commission, 2012; 2014). The large gap between average wages in the maintained and non-maintained sectors implies a substantial cost to narrow and remove the wage gap. Analysis of improving wages among social care workers suggests the cost of wage increases to the state is significantly offset by savings through lower welfare transfers, higher tax receipts and the wider social benefits of poverty reduction (Gardiner and Hussein, 2015). The net cost of improving wages for childcare staff in private and voluntary settings would be lower than the direct cost once such savings are taken into account.

To ensure that improvements in funding are passed on to staff rather than used to increase profitability, governments could introduce an early years pay scale that providers must adopt as a condition of accessing public funding. The NHS Plan offers an example of a strategy to improve wages over time. Nurses receive pay increases of five per cent year-on-year over an extended period (Department of Health, 2000). Pay transformation in the NHS also offers an example of pay rises linked to a modernisation programme to improve professional practices. UK governments could learn from this experience and work with the childcare sector to develop pay agreements that set out shared aims.

The scale of the difference between maintained and non-maintained wages means that closing the pay gap is a considerable undertaking. Increasing early education funding, as we have outlined, to increase qualification levels would help offset the costs of salary improvements. Even so, the long-term cost of closing the wage gap would be substantial; potentially up to £2 billion at current staffing levels. Levers to improve wages, such as introducing an early years pay scale, would be difficult to implement without undesirable effects on prices within the current funding system. A supply-side funding structure, discussed in the next section of this paper, would provide governments with the means to improve wages for staff in private and voluntary settings over time without passing on the cost to parents.

Given the range of pressing priorities for investment, early years wages can only realistically be improved incrementally. A ten-year strategy would allow the wage gap to be addressed through manageable year-on-year pay rises that see a significant and visible improvement in working conditions for staff alongside an agenda for improved qualification and quality standards. Governments would help early years staff significantly by sending the clear message that they should be paid in line with their status as education professionals and move towards meeting this aim, even if a wage gap persists for some time.

Recommendation: UK governments should implement an early years workforce strategy and pay transformation programme to improve staff pay among private and voluntary sector childcare providers

Supporting parents through accessible, flexible childcare

The early education offer has been successful in establishing minimum access to formal early education in every area of the country. However, much of this provision continues to be sessional or nursery class models that are insufficiently flexible for working parents. Private and voluntary daycare providers are less common in less affluent areas and often do not have sufficient capacity to cater to the needs of the most disadvantaged children. Private providers may also charge premium fees for flexible care, which poses affordability problems for working parents.

An early years admissions code of practice

UK governments should establish a clear principle of fair and inclusive admissions practices across all publicly funded childcare providers as a starting point for a new approach. This can be achieved by creating a transparent statutory admissions code of practice that requires providers to treat parents equally regardless of their economic circumstances. This would ensure for-profit provision is integrated into an equitable system where providers benefitting from public funding cannot cherry pick families in the pursuit of profit. An admissions framework would not only ensure that income is reinvested in accessible services before a profit can be realised, but would help stop economic segregation, as far as possible, and foster a good social mix in settings.

An early years admissions code of practice must be more flexible than the school-based admissions framework. Children join early years settings at different points in the year and parents should not be put under pressure to put their child in formal childcare at age one because they think this is necessary to secure a nursery or school place. A setting level process is likely to be appropriate rather than a process coordinated by local authorities. However, to be effective there must be meaningful enforcement through a right of appeal to the local authority.

Nursery classes in schools are already bound by the School Admissions Code. Many private and voluntary providers operate admissions policies; some of these reflect good practice in maintained settings whilst others are explicitly business-oriented and prioritise children whose parents wish to purchase the greatest number of hours of care. A national framework can be modelled on existing good practice and the School Admissions Code. To work well in fostering inclusive models and a social mix of children, the code of practice should require that providers:

- must prioritise certain children (such as those who are looked after);
- may prioritise other groups of children (such as those eligible for the EYPP);
- must not place any other conditions on admission beyond a minimum number of regular sessions, based on children's well-being and provider sustainability; and
- have clear arrangements for administrative fees and deposits that protect parents from excessively high up-front fees.

Parents should be encouraged, though not required, to place their child in a setting at the beginning of a term so that children can be integrated into stable care. An admissions code of practice may result in some providers seeing more children admitted, who attend for fewer hours. In many cases, providers will be able to absorb these costs. However, we also suggest elsewhere that the childcare subsidy system must recognise there is a financial premium for providers which are inclusive in their admissions practices and offer flexibility in the hours of care used by parents. These costs should be recognised in the design of the subsidy system.

Recommendation: UK governments should develop a statutory admissions code of practice for children accessing early years provision in centre-based providers

Promoting social enterprises in childcare

The childcare market must change to meet the needs of families. At the moment, public funding is subsidising profit in settings that are under no obligation to serve a range of families. There are strong incentives for these providers to focus on higher income parents. This leads to a schism between for-profit providers, which through location, fees or admissions practices, seek to serve relatively prosperous working parents, while voluntary and maintained providers operate in areas of concentrated disadvantage. This leads to income from fees leaving the sector as profit when this income could be reinvested in settings.

Many of the providers that are most successful in meeting need in disadvantaged areas are those that are not-for-profit, operate multiple settings and use fee structures to cross-subsidise among settings. Provider groups such as Co-operative Childcare and the London Early Years Foundation have developed business models that use economies of scale to serve disadvantaged communities by cross-subsidising fees among settings, investing in shared quality support and deploying staff flexibly across settings. These models should be exploited, as far as possible, to realise efficiencies that can be re-invested in higher quality, more flexible services, or lower fees.

Childcare should be a vibrant, community-oriented social sector but risks becoming a commodified industry that amplifies economic inequalities. There are many private providers offering high quality care and seeking to operate inclusive business models. The government must, however, ensure that all for-profit businesses achieve high standards of inclusiveness and that there is a level-playing field for social enterprises seeking to use opportunities for cross-subsidy.

The greatest barrier to further exploitation of social enterprise models is the fragmented nature of nursery provision. There are a relatively high proportion of single-site providers – around three quarter of daycare providers in England – and few incentives for providers which are commercially viable to link with providers which are less successful, or to expand into commercially challenging areas. Expanding social enterprises have sought capital investment and worked with advisors to develop viable business plans. To foster the expansion of group social enterprise providers, the government should create a fund where providers can bid for seed funding to develop business plans and, subsequently, investment to support expansion and growth.

The government has recently made up to £45,000 available to individual childcare providers through the Childcare Investment Readiness Fund. This fund, which is capped at £500,000, should be expanded and explicitly targeted at improving provision in areas of disadvantage. We suggest that this can be achieved through a rolling programme consisting of a more substantial pool of seed funding – £8 million allows up to 150 providers each year to access investment readiness funding – and a larger pool of £50 million, available over three years, providing match funding for new schemes. These amounts can be revisited after three years and draw on learning from the scheme.

Box 4: London Early Years Foundation case study

The London Early Years Foundation (LEYF) is a social enterprise providing nursery care to over 3,000 children in 34 nurseries across London. LEYF was established as the Westminster Health Society in 1903 and initially provided health visiting services for mothers and children in London. The Society expanded into nursery care during the Second World War and shifted its focus to early education, as health conditions improved in the post-war decades. In 2006, the charity, then named Westminster Children's Society, became a social enterprise in order to reduce dependence on potentially vulnerable grant funding and become financially self-sustaining and was renamed the London Early Years Foundation.

LEYF has a strong child-centred ethos, defining its mission as 'to change the world one child at a time'. An 'impact model' identified LEYF's work as focused on five core aims:

- providing free nursery places in the most disadvantaged parts of London;
- providing high quality, research-based nursery care, in partnership with communities;
- supporting parents to extend their children's learning at home;
- providing apprenticeships; and
- campaigning for early years policies that are in the best interests of children and families.

Around one-third of parents whose children are attending a LEYF nursery receive some form of financial support from LEYF. Nurseries are able to offer free places for a period when parents are returning to work, or experience short gaps in employment, and LEYF is one of the minority of nursery chains in London offering free places to the most disadvantaged two-year-olds. LEYF provides this support by cross-subsidising places within and across settings, reinvesting profits from relatively well-off, fee-paying parents. In addition to ensuring access for parents with low incomes, this approach has the virtue of creating a social mix of children in settings, ensuring children and parents of different backgrounds mingle and underpinning high quality care.

LEYF developed its financial model through support from the Social Business Trust, working with the consultancy service Bain to test and develop its business model, and currently has a £10 million turnover. LEYF has obtained funding of £1.25 million from Big Issue Invest, Bridges Ventures, Clearly So and the Social Business Trust to expand into additional London boroughs and aims to more than double the number of children it reaches to 7,000 by 2017.

Sources: Lyon, Fergus and Fernandez, Heather (2012) *Scaling up social enterprise: strategies taken from early years providers*. Birmingham University: Third Sector Research Centre

Recommendation: Each UK government should establish a well-funded social enterprise programme to promote inclusive pre-school nursery provision

Cost: £58 million (£8 million annual seed funding; £50 million three-year match funding pool)

A childcare entitlement

Where communities are economically segregated, there are limits on the potential of an admissions framework and social enterprise models to address gaps in provision (Dickens et al., 2012). Providers that wish to offer flexible daycare services in less affluent areas may find it difficult to break even, because demand is present but realistic fees do not cover the cost of the service. The UK can learn from countries that have been most successful in

removing barriers to work arising from childcare and establish a childcare entitlement. An entitlement would be a guarantee of access to a flexible childcare place, but parental fees would be dictated by the childcare subsidy system.

An entitlement has the potential to support parental employment without carrying the same cost as large extensions to the free early education offer. Where daycare provision is already good, there would be limited need for investment. Resources would be directed towards developing flexible daycare provision in areas which are currently poorly served. There is a case for extending the free offer from 38 to 48 weeks, but this is likely to carry significant deadweight costs where new investment subsidises existing provision rather than extends services. Instead, local authorities can work directly with providers that do not offer daycare to 'pump prime' flexible provision and, where necessary, subsidise care on an ongoing basis. This is a technically more challenging but more proportionate solution.

The UK can learn from Germany, which in the 2000s established a daycare entitlement for parents in work, training or education for children aged between three and six. In 2013, the entitlement was extended to children aged zero to three. The German entitlement is administered by federal regions (*Länder*) with some latitude in implementation, such as a degree of variation in the hours parents are able to access (Bock-Famulla and Lange, 2013). The German government has provided substantial financial support to federal regions to create new places to meet demand and cover operating costs. Fee income continues to be the main source of income for providers; support from *Länder* is proportionate to the assistance providers need to meet demand.

Policy strategies developed to create free early education places in the UK could be adapted to underpin a childcare entitlement, particularly for children not yet age two, and for nursery classes and sessional providers to move to full daycare models. These include:

- providing capital funding to allow providers to expand places or move to new premises;
- providing time-limited revenue funding to support providers to meet viable expansion plans;
- providing ongoing revenue funding to support sustainability in areas where there is demand for childcare, but viable fee-dependent business models cannot be developed due to low wages or low levels of parental employment;
- offering guaranteed minimum hourly rates for childminders to ensure that there is a sufficient pool of flexible childminders to meet short-term fluctuations in demand and address gaps in centre-based provision, particularly for zero- to two-year-olds; and
- developing childminder and home childcare brokerage networks to promote vibrant local markets for flexible, ad hoc childcare.

We estimate the cost of delivering an entitlement by examining the cost of place creation to meet unmet demand for flexible childcare services (see appendix B). It is unlikely to be feasible to deliver a meaningful entitlement immediately and services should not expand faster than the ability of local communities to develop high quality provision. Rather, UK governments should prioritise access in the least affluent areas and roll out an entitlement over several years.

It is not realistic to establish a similar strong statutory entitlement to childcare for parents who work 'atypical' hours; that is, during early morning, evenings (or nights) and weekends. However, the government should strengthen statutory duties on local authorities to provide sufficient options for these parents. This can particularly be achieved by funding childminder networks, improving brokerage services and offering a supplement for childminders who work during evenings and weekends.

Recommendation: UK governments should introduce a statutory entitlement for parents to childcare during the working week, supported by a duty on local authorities to promote flexible provision

Cost: £578 million initially falling to £250 million after six years

Access to high quality childcare for children with special educational needs and disabilities

Children with disabilities or additional needs are less likely to have access to high quality, flexible childcare and are often charged more than parents with non-disabled children for care (Contact a Family et al., 2014). These children are more likely to fall behind their peers before they start school, contributing to worse long-term outcomes and an increased poverty risk (Department for Children, Schools and Families, 2010; Jones, 2010). Recent research suggests that children with disabilities make less progress over the early years than their non-disabled peers with similar levels of cognitive skills (Parsons and Platt, 2014 – provisional working paper). Early years provision has a particularly important role in redressing this situation by ensuring that children with additional needs do not fall behind at the earliest stage. However, providers often struggle to provide inclusive services because of a number of problems, which includes a lack of specialist SEND (special educational needs and disabilities) training for early years staff, limited funding to support adaptations to facilities and the absence of a funding mechanism to support one-to-one care or additional supervision where needed.

A comprehensive solution is needed to address the challenge of developing inclusive childcare provision for children with disabilities and additional needs. Children with high needs tend to be concentrated in a small proportion of specialist settings, such as maintained nursery schools and children's centres, which are directly funded by a local authority. Whilst it is appropriate for local authorities to develop specialist provision to meet the needs of the small proportion of children with high needs, these settings may also be the only resort for children who could be included in high quality mainstream settings. This creates an unnecessary segregation of provision, limits access and choice for the parents – accessing flexible daycare is often particularly problematic – and may not be cost effective. Specialist settings are often forced to ration care because they are over-subscribed. The lack of support for inclusion in mainstream childcare can also put excessive pressure on short-breaks budgets, as parents turn to respite services to meet needs that could be met through childcare provision.

To address these problems, each UK government should create an inclusion support strategy for the early years. This programme should:

- increase the number of special educational needs coordinators (SENCOs) so that all early years settings have, or have easy access to, the expertise needed to cater to children with additional needs;
- fund training for non-specialist early years staff to ensure they are skilled to care for the individual children admitted to settings;
- fund appropriate physical adaptations to premises; and
- fund one-to-one care or additional staff where needed.

These programmes should be underpinned by a clear statutory framework, linked to the admissions process, that guarantees children with additional needs access to the same range of settings as any other child. Currently, parents with disabled children have no entitlement to access childcare at a mainstream provider and they, or a childcare provider, must apply to access limited support budgets with little guarantee of assistance. Expectations for inclusion are as a result much too low. Early years provision should be

inclusive by default and families and providers should be entitled to appropriate support to make inclusive provision a reality.

Recommendation: Each UK government should roll out a funded statutory inclusion framework that ensures children with special educational needs and disabilities are able to access a wide range of high quality childcare settings at no additional cost

Cost: £251 million

Childminder networks

Whilst childminders deliver a relatively small proportion of free early education, their role in doing so is important. For example, they often care for children with additional needs. While the number of registered childminders has been declining, childminders will continue to have a critical role in supporting parents with children under two, those who work atypical hours, and those whose children attend formal childcare at a school or sessional provider and require 'wrap-around' care.

Unlike staff in centre-based provision, childminders may have limited access to professional support and development opportunities. The main form of support for childminders is participation in a childminder network, which offers support to childminders through training, shared materials (such as toy libraries) and mentoring, usually for a fee. The status of childminder networks remains ambiguous and the quality and service offer of networks can vary wildly. Participation in a network with a quality improvement programme is associated with higher quality care but, at present, only around half of childminders are members of a suitable network (Otero and Melhuish, 2015).

UK governments can support childminders by ensuring that high quality networks are available to childminders and deliver appropriate support. This means ensuring that childminders delivering free early education have access to graduate-led networks. There is also scope to use networks as the basis for enhanced brokerage services to develop local markets for flexible childcare. It is likely that sufficiently well-organised fee-free networks will be attractive to the majority of childminders. However, given the importance of high quality care to children's outcomes and the reality that most childminders will not have a graduate qualification, it may be appropriate to require childminders delivering free early education to participate in a network.

Recommendation: Governments should fund graduate-led childminder networks for all childminders delivering free early education

Cost: £26 million

The role of the free early education offer

International evidence suggests that universal early education provision ensures greater uptake than targeted provision for specific disadvantaged groups (Gambaro et al., 2014). There are a number of reasons for this; for example, there is no stigma attached to the use of universal provision and it is easier to disseminate messages about entitlements. Lloyd and Potter (2014) also argue that universal provision in which special attention is given to the most disadvantaged children and families is the most effective means of reaching families in poverty. The authors note that the provision of free early education in England after 1998 increased uptake of all forms of early education and childcare among deprived families, who were least likely previously to use it. Free early education provision has also, in some cases, enabled the earlier identification of special educational needs and child welfare problems, thus enabling packages of support to be put in place sooner.

A criticism that has been made of investment in free early education is that it carries significant 'deadweight' cost. Investment through the free offer has, to some extent, replaced parental spending that would have occurred anyway. This approach could be defended on the grounds that free childcare has bolstered parental incomes, which has benefits for child outcomes. But it is not at all clear if childcare subsidies are an efficient or well-targeted way to achieve this in comparison to wider welfare support. Blanden et al. (2014) estimated that 82 per cent of three-year-olds who became entitled to free early education in 2000 were already in receipt of such provision.

There is little educational benefit to extending free hours beyond 15 hours. Quality, stability and duration in months of attendance matter more than the hours of care a child receives each week (Parker, 2013). There is also little evidence that beginning early education before age two benefits children, whatever their background (however, accessing other forms of support maybe beneficial for some children).

UK policy-makers should also be mindful that no country has built a high performing childcare system around universal free hours. For example, the basis of Nordic early years models, where parents have a legal entitlement to childcare, is that most parents do not enjoy any free care and pay a fee (although typically low by comparison with the fees paid by parents in the UK). The risk of relying on ever greater extensions to free childcare is that pursuing this approach will spread resources thinly, locking the UK into a low quality funding model and preventing an appropriate targeting of support for the most disadvantaged.

We do not therefore recommend large expansions to the early education offer, which are likely to be harmful to the prospects of investment in poverty-reducing childcare priorities. Nor, however, can we recommend moving away from a core universal offer. Lloyd and Potter (2014) set out evidence that universal provision has significant benefits for reaching the most disadvantaged children and promoting a social mix of children, which is an important aspect of high quality care. The offer is also critical in underpinning the supply of sufficient childcare places across the country. If the offer were to be withdrawn, or eligibility restricted to a proportion of children, the supply of childcare would be affected. UK policy-makers should seek to achieve a balance between the number of hours that provide the benefits of universalism and poorly targeted expansions of the free offer that consume resources that could be better directed to meet specific quality, access and affordability goals.

We believe that there is sufficient evidence to justify moving to a universal early education offer for two-year-olds. It is a concern that the roll-out of the two-year-old early education offer appears to have been achieved through provision that is less mixed than for the three- and four-year-old offer. A number of local authorities, particularly those in London, are also experiencing difficulties creating enough places for eligible children because providers are opting out of the offer. Moving to a universal offer would encourage provider participation and help ensure that the essential components of high quality early education are in place, including mixed social groups. A universal offer also has important benefits for identifying children with additional needs and de-stigmatising the offer.

Given the range of investment priorities, we suggest that, as a first step, the two-year-old offer should be extended to 60 per cent of children (and each devolved administration should aim to match this offer). This would encompass all families at risk of poverty and may encourage providers who have opted out of the targeted two-year-old offer to consider offering provision to this age group.

One way to pay for an extension to the two-year-old offer would be to redirect planned spending on free early education. Extending the free offer to 30 hours for three- and four-

year-olds does not represent the best use of resources to reduce poverty. However, it is clearly unlikely the present government will reconsider this policy. In the longer term, a new childcare strategy would provide the opportunity to look again at the best way to distribute funding for free childcare.

Recommendation: UK governments should provide 15 hours of free early education for all children aged two to four

Cost: £912 million

Universal credit and childcare

Outside the early education offer, there are a number of short- and medium-term measures that would ensure childcare costs do not contribute directly to poverty. There are ways to improve the contribution the childcare system makes to support more parents with low incomes to move into work, access higher quality or better-paid roles, or increase their hours of work.

Previous reviews of childcare and poverty have emphasised that, for families living in poverty, there is an important difference between charging any fee at all for childcare and providing care free of charge (Waldfogel and Garnham, 2008). This seems to be because providing parents with free hours rather than a complicated subsidy is most effective in sending a clear message to parents. Other evidence similarly suggests that large reforms that are well understood are most likely to have an impact on work incentives and net incomes for families (Blundell, 2014).

The free early education offer has this benefit of clarity and simplicity but, as discussed elsewhere, expanding the offer to cover more hours and address gaps for one- and two-year-olds is unlikely to be affordable alongside other anti-poverty priorities. We propose that, in addition, to the early education offer, the government should offer free childcare to families with an income below the poverty line. Alongside a legal childcare entitlement, this would send a clear signal that childcare costs will not be a barrier to work or training and encourage parents to seek to maximise their economic opportunities without worrying about childcare costs or access. The additional cost of this step is relatively modest because the parents affected would usually be entitled to the 85 per cent childcare element under Universal Credit. The implied cost is therefore the remaining 15 per cent of childcare fees.

This step would bring support back to a level comparable with that currently offered to parents who are eligible for childcare disregards in Housing Benefit and Council Tax Benefit - in addition to the childcare element of Working Tax Credit – up to 95.5 per cent (The Children's Society, 2012).

Recommendation: The government should increase the childcare element of Universal Credit to 100% for families with an income below the Child Poverty Act 2010 relative poverty threshold

Cost: £150million

A second, related, issue is the challenge parents face meeting up-front childcare costs and budgeting during the transition to work. In addition to any deposit or registration fee, nurseries typically require up to six weeks of fees paid in advance. This can be a substantial barrier to securing a childcare place and taking up an offer of employment. Even where parents can meet these fees, the substantial one-off expenditure may create further budgeting challenges and hardship. The planned Universal Credit budgeting advance of £812 will not be available to many parents and appears unlikely to meet the full cost of a

deposit in many cases. The advance may also not be effective for parents in poverty ,who may be unwilling to take on a significant additional burden of debt or have already used the advance for another purpose

The Department for Work and Pensions should establish a facility to pay up-front fees and deposits, including at least six weeks' fee in advance. This would ensure that the family's first childcare payment is made after an initial paycheck. This would remove a practical impediment to arranging childcare, avoid parents accumulating debt when they take up a job due to the Universal Credit system of payments in arrears, and allow parents to build revenue from employment before they receive a first significant childcare bill.

Recommendation: The Department for Work and Pensions should establish a facility to pay any up-front childcare fees for parents eligible for the childcare element of Universal Credit

Cost: £30 million

The childcare element cap under Universal Credit will mean that parents working full time will increasingly not be able to claim support for 100 per cent of their childcare costs. The planned tax-free childcare scheme, in which each child is entitled to up to £2,000 of support each year, has further highlighted the flawed nature of a *de facto* two-child cap. The rationale for the cap is not clear. The cap is, in practice, likely to have little influence on expenditure per hour of childcare since the cap has no influence on maximum costs until the upper threshold is reached.

The two-child cap is also in stark contrast to successful international examples where *more* rather than less support is provided to large families to ensure the overall costs of childcare are kept down and parents are supported to work regardless of the number of children they have. The government should be pragmatic and recognise that generous support with childcare costs for one child is irrelevant, if support for a whole family is insufficient to remove the constraint on participation presented by childcare costs. Unfortunately, the government's recent decision to restrict the child element of Universal Credit to two children reinforces the current approach.

Addressing this issue is relatively straightforward. The government could up-rate the childcare element cap of £760 to the maximum current average cost of childcare each week in Britain, which is £980 for 40 hours. Future up-rates would be in line with childcare price inflation. This single cap could be applied to each child in a family and the two-, or more, child cap of £1,108 be removed. This step would be fair, is likely to be relatively low-cost because a small number of families are affected and would maintain strong work incentives for parents.

Recommendation: The government should increase the Universal Credit childcare element cap to £1,000 per child and remove the two-child cap

Cost: £112 million

Families where at least one parent has no formal skills or has low formal qualifications are at greater risk of poverty (Barnes and Lord, 2013). Childcare support for college students is provided largely through discretionary funds (there are formal schemes for parents under 20 and those accessing undergraduate courses) and colleges themselves dictate eligibility criteria and the scope of support. A brief survey by the authors suggests that these schemes can be generous, covering up to 100 per cent of costs, but often have limitations. For example, one college offers no childcare help with evening classes, one college limits support to one child and another cannot confirm eligibility for support until 'within eight weeks' of the start of term. Limited resources mean that these schemes tend to target

families with particularly low incomes, which may prevent low- to middle-income families, who remain at risk of poverty, from addressing skill deficits.

Unless training happens to coincide with early education hours (and all a parent's children are aged two, three or four), parents are dependent on informal care or limited discretionary support. A parent attending an evening class would, for example, not be able to use the early education hours, which cannot be used after 7pm, to pay for childcare. The Universal Credit system (and present tax credit system) also makes no formal allowance for childcare for jobseekers or those building skills through courses not covered by other schemes.

In 2008, the government created the Free Childcare for Training and Learning for Work scheme that offered childcare to help unemployed parents access education, ranging from short refreshers to formal qualifications. Eligibility criteria for the scheme included a family income below £20,000 and a partner in work. The government estimated that providing free childcare to 50,000 parents at the time would cost £75 million. The scheme was initially rolled out in 67 local authorities with the highest concentrations of eligible parents, and there were plans to extend the scheme to all local authorities. However, fiscal constraints meant that the scheme was short-lived.

Another example of a similar scheme can be drawn from Sweden, which in 2001 introduced a mandatory offer of 15 hours free childcare each week to parents who are unemployed. Evaluations of this policy suggest the offer has been successful in improving the work prospects of unemployed mothers, principally because the support allows parents with childcare responsibilities to increase the intensity of their jobseeking activity (Vikman, 2010).

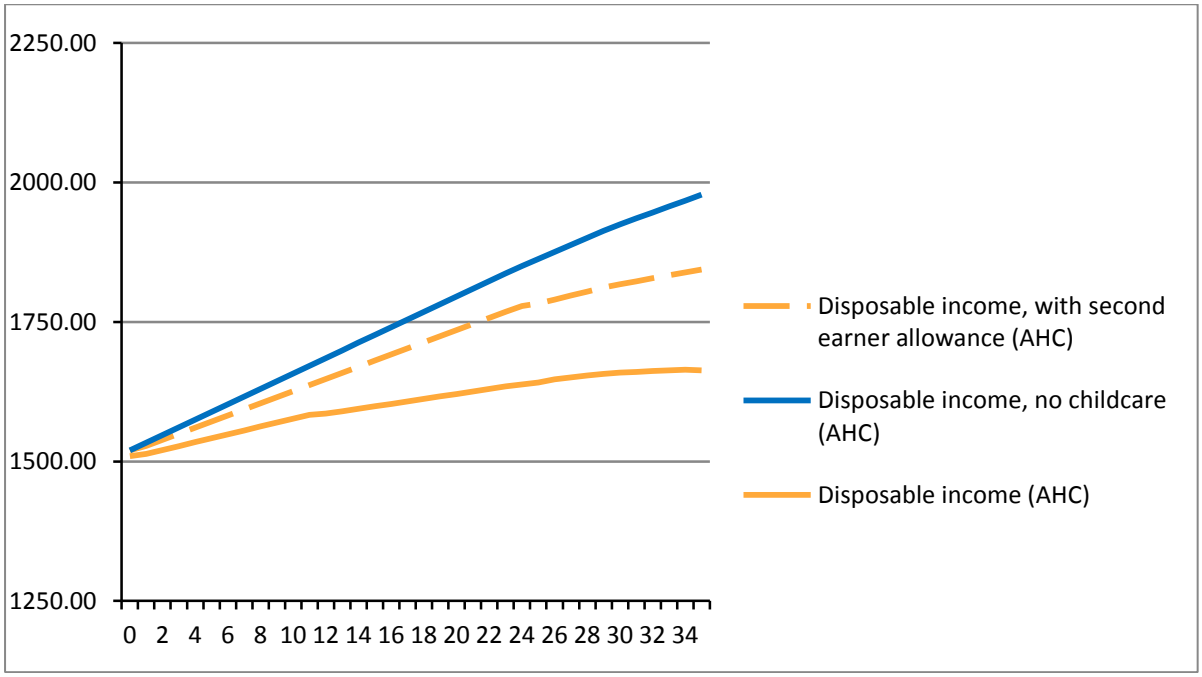
A system in which limited support is available to parents who are not in work beyond the early education offer is failing to maximise the potential of childcare support to help parents who wish to do so make the transition into work. To ensure that parents are able to proactively address skills gaps and devote time to jobseeking, the Department for Work and Pensions should provide access to the Universal Credit childcare element for parents who are not in work where this clearly benefits a parent's prospects of moving into and progressing in work. The claimant commitment for parents with pre-school children does not require that the primary carer in a family seeks to work but does require that parents undertake to 'prepare for work'. As the Department develops the claimant commitment under Universal Credit, it can link expectations of parents in meeting this commitment with reciprocal childcare support.

Recommendation: The childcare element of Universal Credit should be extended to jobseekers and parents participating in work preparation activities, including education and training, who do not have access to another childcare support scheme

£170 million

Finally, the government could improve work incentives for families at risk of poverty by introducing a second earner disregard in Universal Credit. Under the Universal Credit system, each couple receives a work allowance disregard. For single earner couples, the full allowance is set against the earning partner's income. This means that if a second earner moves into work there is usually no remaining amount of the work allowance to apply to their income. As a result, little or none of a second earner's income is 'protected' in the same way as a proportion of the first earner's income is protected by the work allowance. The effect is to create a high marginal effective tax rate and poor work incentives for second earners. Figures 9 to 15 illustrate the impact of the Universal Credit taper on work incentives for second earners.

Figure 20: Impact of Universal Credit second earner work allowance (£210) for a couple earning the National Minimum Wage with two pre-school children[12]



The Coalition Government acknowledged that the structure of Universal Credit prioritises work incentives for single earner couples and single parents. The rationale for this approach was simply that ministers believed it makes sense to use the available funding to first encourage at least one parent in a family to work. Creating a second earner disregard would presumably have meant the Universal Credit work allowances would be set at a lower level, undermining this goal. While understandable, this approach entrenches a single earner model which in many cases is not sufficient to move a family above the poverty threshold. A single earner model also encourages long-term absence from employment for second earners that reduces lifetime earnings and increases a household's long-term poverty risk.

The government estimated the cost of introducing a second earner disregard to be £430 million for a £1,500 annual allowance (£125 each month) or £780 million for a £2,500 allowance (£208 each month).[13] The cost of introducing the disregard is high because it would apply to all elements of Universal Credit – it is not a measure targeted specifically to offset childcare costs. A second earner disregard is also not targeted at families with the lowest incomes as it only affects families with sufficient earnings to have their Universal Credit award tapered. Given the growth of in-work poverty, creating a second earner work allowance is, however, an increasingly relevant approach to poverty reduction. Figure 20 illustrates the effect on work incentives of introducing a second earner disregard of £210 each month.

Another option would be to adjust the Universal Credit taper rate, which is currently set at 65 pence of each pound earned above the work allowance. The Centre for Social Justice proposed that a taper rate of 55 pence represented the best balance between affordability and sustaining effective work incentives and the recent Resolution Foundation review of Universal Credit reiterated the merit of a shallower taper (Centre for Social Justice, 2009; Finch, 2015). Adjusting the Universal Credit taper to this level would, however, be more expensive than a second earner work allowance (costing around £3 billion) and would be less well targeted if the policy goal is to create work incentives for second earners or reduce childcare costs. As discussed later in this report, reform of childcare subsidies would provide

the opportunity to set a separate taper for childcare subsidies. This would be more affordable than an adjustment to the Universal Credit taper and would specifically target families with childcare costs.

Recommendation: The government should introduce a second earner allowance in Universal Credit sufficient to create realistic work incentives for second earners moving into work

Childcare subsidy reform and supply-funded childcare

The UK's complex system of demand-side childcare subsidies is poorly suited for anti-poverty strategies. The fragmentation of funding and 'cash in hand' nature of support provides government with limited tools to achieve desirable poverty reduction policy goals. In contrast, high performing international systems use a unified supply-side funding system to coherently drive progress towards quality, access and affordability policy goals. This section of the report explores how the UK's childcare funding system could be simplified and proposes parameters for a more effective approach.

To illustrate approaches to childcare funding from which UK policy-makers might draw lessons, we have summarised three international examples. These examples illustrate subsidy models that differ from the UK's but operate within a mixed market of provision that is comparable to the UK context.

New Zealand

In New Zealand every child aged three and four receives 20 free hours of childcare each week. An additional subsidy covers up to 30 hours of care per child aged 0 to 6 each week (30 hours in total, so 10 additional hours for three- and four-year-olds). For full-time care, this subsidy typically covers between half and two-thirds of a provider's fees. Provider fees are not capped and parents must make up the difference between the subsidy rate and the provider fee.

The subsidy structure is notable because it removes the division between education and care and allows the New Zealand government to use funding to promote improvements in access and quality, both within the free early education offer and for parents who use additional hours of care to support employment. The subsidy includes:

- a basic rate dependent on service type and the percentage of staff qualified as teachers;
- additions for the staff-child ratio (according to a child's age) and service type (sessional/full daycare);
- an equity top up for socio-economic status and special educational needs; and
- a monthly equity top up for language and isolation (rurality).

There are potential weaknesses of the approach adopted in New Zealand in an anti-poverty context, including the absence of an income gradient within the subsidy structure – all parents receive the same flat rate subsidy – and a 30 hour cap that means that parents working full-time pay proportionately more for care. The principal success of the New Zealand model has been in aligning funding squarely with a high quality funding model and dramatically increasing the proportion of early years graduates leading care. New Zealand has, however, a similar fragmented childcare sector to the UK and this approach has been less successful in increasing flexible service models.

Figure 21: New Zealand ECEC subsidy structure

Provider type	Basic rate per hour	Equity top up per hour	Equity top up monthly
Centre-based daycare	Free 20 hours for 3- and 4-year-olds $8.34 to $11.43 (depending on % teachers present) Additional hours: $3.83 to $6.70 (depending on age and % teachers present)	$0.21-$0.97 (socio- economic) $0.19-$0.47 (special needs)	$410.81 (language) $99.95-$290.45 (isolation/rurality)
Sessional	Free 20 hours: $4.67-$6.29 Additional hours: $3.35 to $4.84	As above	As above
Home carer (childminder – must belong to network)	Free 20 hours: $4.42 (meets 'quality' training requirements) Additional hours: $3.92 (standard)	As above	As above

Source: New Zealand Ministry of Education (2014) *New Zealand Government ECEC Funding Handbook*

Norway

Of the Nordic nations, the Norwegian example of supply-led funding in a mixed childcare market is particularly relevant to policy challenges in the UK. Unlike other Nordic examples, Norway achieved universal access to kindergartens relatively recently and has done so through a mixture of public and private provision (there is a roughly even split of public and private childcare provision in Norway). The Kindergarten Act 2005 set out a clear objective to provide childcare of high quality at a low price to parents. The Act established a framework for a legal entitlement to a daycare place from age one which Norway achieved in subsequent years through an expansion of kindergarten places. The kindergarten model, which fosters pedagogical approaches to care alongside full daycare, and the guidelines set

out in the Kindergarten Act mean that this expansion has occurred through settings with a strong child-centred culture as well as sufficient capacity to meet the needs of working parents.

All childcare funding in Norway is devolved to municipalities, which must subsidise sufficient places and provide financial support to parents within a broad national framework. Municipalities do so through a supply-funded system where providers are reimbursed with block grants depending on the number of children present and factors such as their age, level of need and days per week spent in care. There is no separate national subsidy system comparable to the tax credit subsidy or voucher scheme in the UK: parents typically pay their contribution to fees directly to providers. Parents have an entitlement to a daycare place within four weeks of application and children with disabilities or under the care of child welfare services are prioritised. A school-like admissions system operates and children most often join a kindergarten at the beginning of a school year. Parents retain flexibility over how much childcare they use; for example, choosing between two and five days each week and morning and afternoon sessions.

Maximum daycare fees are set each year by the Norwegian parliament and in 2014/15 were 2,405 Norwegian *krone* per month (around £216). Nationally, around 80 per cent of funding is met by national and local government and 20 per cent by parental contributions. Local municipalities negotiate reimbursement rates with providers through grants. Parents receive a 30 per cent discount for second child and a 50 per cent discount for each further child, in addition to any income subsidy. Municipalities must offer subsidies for families with low incomes but operate varying models: for example, Oslo sets a lower maximum fee of 856 *krone* (£77) for families with income of less than £17,200, whilst Trondheim stipulates that childcare fees cannot be more than 85 per cent of family income minus household expenses. Municipalities are obliged by the Kindergarten Act to invest equally in public and private kindergartens. Parental choice is more constrained than in the UK (parents usually select their top five kindergarten preferences in order during the admission process, as they would a school) but in practice parents have better access to a variety of high quality, flexible providers.

Norway has demonstrated that it is possible to marry a supply-side funding model with a mixed market of public, not-for-profit and voluntary provision and has succeeded in increasing the use of childcare by low-income families (Ellingsaeter, 2014). No childcare system is perfect and there are vibrant public debates in the Nordic states, for example, about issues such as the proportion of graduates in settings, take-up of childcare by the most disadvantaged families or the appropriate balance of formal and parental care.

Australia

Australia currently has a complex demand-side subsidy system suffering from similar problems to those evident in the UK. In 2013 the Australian government asked the independent Australian Government Productivity Commission to examine and identify future funding options for a childcare and early childhood learning system. The Commission has now published its final report (Australian Government Productivity Commission, 2014).

The Commission's recommendations propose combining Australia's current demand-side childcare funding streams (the Child Care Rebate, Child Care Benefit and the Jobs Education and Training Child Care Fee Assistance) into a single means-tested subsidy covering between 85 per cent and 20 per cent of the 'deemed cost of care' per hour, with a linear taper operating from $60,000 (around £31,000) to $250,000 (around £130,000). Parents would access this subsidy through an online account system, with the subsidy transferred directly to providers. The Commission proposes that a body is set up to

determine the reasonable hourly cost of care, using past fee data, that allows for differences in the cost of supply by age of child and type of care.

Children with additional needs would receive additional supplements, as in the New Zealand system. Notably, however, the Commission proposes a separately funded inclusion support programme to ensure that children with disabilities are able to access childcare places. The additional needs subsidy would provide a measure of support to providers admitting children with additional needs, but the system would recognise that providers catering to children with high needs will need separate and relatively expensive support in a minority of cases. Another notable element of the Commission's proposals is a viability assistance programme for providers in rural or deprived areas. The Commission has suggested that assistance is provided on a rolling three-year schedule so that the case for support is re-assessed periodically.

The approach outlined by the Commission utilises the capacity within government to manage a complex subsidy system to resolve a number of problems. The funding system would be complex for government to operate but should, in practice, be relatively simple for parents. The proposed subsidy model incorporates supplements (though not quality supplements as in the New Zealand model) and is complemented by separate interventions to address specific access problems. The model also offers a way, using a periodic independent assessment of prices, to balance the need for government to fund care at a sustainable level with cost controls.

The Commission was given a remit to make funding proposals within Australia's existing childcare funding envelope and benefited from its ability to undertake detailed modelling work over a long period, allowing it to fine-tune a subsidy model intended to maximise work incentives within this budget. The downside of this approach is a relatively neutral position towards quality improvement and therefore many of the issues covered by this report (which largely lay outside the remit given to the Commission by the Australian government).

Supply-funded childcare in the UK

Drawing on anti-poverty priorities and learning from alternative funding models, our recommended approach is a shift to a supply-funded childcare system. Lloyd and Potter (2014) set out the evidence that a supply-side funding model is the most effective way of achieving wide coverage of accessible and affordable services and ensuring government can influence the quality and affordability of care. Supply-side funding is embodied by the 'Nordic model', associated with clear entitlements for parents, a strong role for local government in commissioning services and a strong ethos of quality supported by a high proportion of graduates in settings and professional wage levels.

Supply-side funding means establishing funding arrangements designed specifically for centre-based pre-school services and childminders. These providers would become funded through a grant based on the number of children attending and the hours of attendance, and other factors such as the socio-economic background and needs of children. Most parents would still make a contribution to childcare costs, but this contribution would be shaped by a nationally agreed fee framework.

Figures 22 and 23 illustrate how the proposed model would affect early years funding structures in England. The free childcare offer is funded through the Dedicated Schools Grant, whilst funding for children's centres and additional investment local authorities may choose to make in childcare is drawn from the Early Intervention Grant (which is also used to fund a variety of services including, for example, family support, teenage pregnancy and young offender services). Non-maintained services are substantially dependent on parental fees to top-up this funding.

This funding structure limits the service offer for many providers serving the least affluent parents. Whilst the government and in turn local authorities have substantive control over funding for free childcare, the ability of parents to top up funding to a sufficient level to fund a 'full' daycare service is a matter of market economics. Demand-side funding streams such as the childcare element of tax credits and childcare vouchers (or, in future, tax-free childcare) do not provide for direct influence over services.

Figure 22: Current childcare funding system (England)

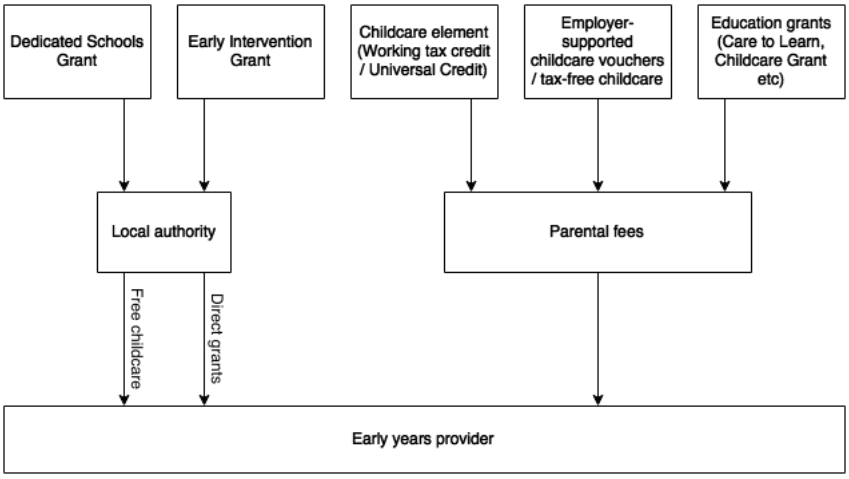
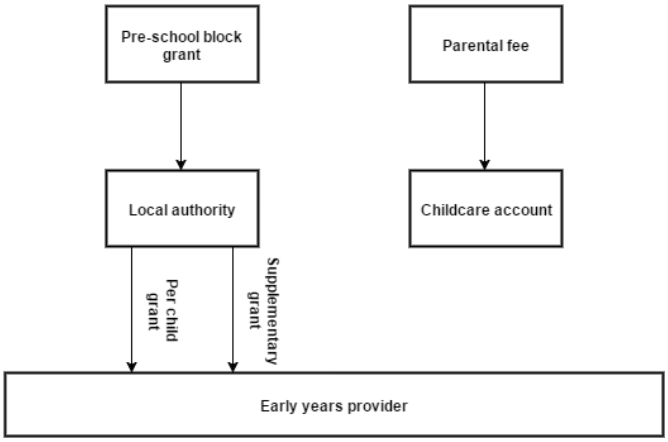


Figure 23: Proposed early years funding model



A supply-funded approach is a natural extension of goals that already sit at the heart of childcare policy and builds on recommendations in this paper, such as a legal childcare entitlement and an admissions framework, which demand greater involvement by local authorities in funding and commissioning childcare. It is possible to deliver a childcare entitlement within a demand-side funding system, but this is likely to be a compromise – a stronger version of the current Childcare Act sufficiency duty – by comparison with the Nordic approach of an absolute legal entitlement. A supply-funded approach allows government to use its role as the primary funder of childcare to guarantee access and promote stable, high quality provision.

Supply-funded models in Scandinavia rest on a higher overall level of public funding and a roughly 80-20 split of funding between government and parents. The Nordic systems are also egalitarian in the sense that relatively equal amounts are spent per child regardless of their parents' income. In the UK, public spending is lower, the split of funding between parents and the state is closer to 50-50, and a significant proportion of support for parents with low incomes is means tested. We have recommended investment that would bring UK investment in childcare to a level that makes supply-side funding a viable option. Without this level of investment, supply-side reform is, however, unlikely to be a realistic option. In this context, it should also be borne in mind that the Nordic nations tend to invest a greater proportion of early years spending in services such as kindergartens rather than cash transfers to parents (OECD, 2012). The UK could, in part, bridge this potential funding gap by pursuing a less egalitarian fee structure that requires a greater contribution by those who are well-off.

Integrating education and care funding

All childcare funding affects the same provision for families. It does not make sense to have one funding scheme, the childcare element of tax credits, designed solely around employment objectives and another scheme, free early education, designed around education objectives (let alone a third scheme in the form of childcare vouchers, and in future the tax-free childcare). The government's decision to offer 30 hours of free childcare to three- and four-year-olds has further highlighted the tensions within the present funding system.

A new subsidy scheme should be designed to coherently drive both care and education goals. This goal can best be achieved through a single subsidy that incorporates well-designed supplements. Such supplements are not new to early education funding. Local authorities may currently incorporate supplements into free early education funding in line with the nationally Early Years Single Funding Formula (EYSFF) framework. The EYSFF does not set specific proportions or amounts, but provides a framework within which local authorities must work. The current EYSFF guidance requires (Department for Education, 2014):

- a locally-determined, transparent formula;
- a single base rate for all providers, or different base rates for different types of providers, according to unavoidable cost differences (the number of base rates must be kept to a minimum);
- a deprivation supplement for three- and four-year-olds (not required for two-year-olds);
- that any supplements help drive positive outcomes for children;
- there should be a single base rate with no supplements for free early education for two-year-olds; and
- that any supplements are based on a count of children attending provision.

In practice, local authorities use formulas utilising supplements to varying degrees. There are also inherent limitations on a system in which supplements can only be present within the free early education offer. If children attend full-time care the influence of supplements may be limited: whatever additional support providers receive for the 15 free hours of care is diluted if they are unable to charge comparable fees for additional hours.

Figure 24 illustrates a proposed evolution of the EYSFF model that could be applied to all funded hours. The base rate for the subsidy can be set by provider type (daycare, sessional and childminders) and the child's age (in line with regulatory ratios). The base rate allows government to influence the minimum standard of provision in a setting. Accessing funding would be conditional on a minimum proportion of qualified staff and paying staff in line with a

national wage framework. A deprivation supplement would help meet additional costs in less affluent areas and a quality supplement, conditional on meeting qualification requirements, would incentivise providers to increase the proportion of graduates employed. Additional supplements may be added for children with language needs, disabilities or special educational needs. However, support for these latter groups of children also requires dedicated funding outside a subsidy.

Figure 24: Proposed subsidy structure

Core cost (varied by child's age and provider type)	Socio-economic supplement	Quality supplement (graduate-led care; % staff qualified to level 3)	Additional supplements (SEND; language)

A unified subsidy need not be provided on a per hour basis for centre-based providers. It may make more sense to provide grants based on the sessions a child attends. By and large, parents in centre-based settings already pay per session rather than per hour. This is necessary for provider sustainability and encourages stable caring patterns for children. An hourly subsidy could continue to be available to childminders, whose hours are likely to be more variable. The most effective approach to a supply-funded subsidy model would need to be established through piloting and consultation with providers.

One reason there are fewer full daycare providers in areas with higher concentrations of parents, who do not work or have low incomes, is that providers face difficulty developing sustainable business models. A subsidy structure that recognises the additional fixed cost of daycare and incorporates a deprivation supplement for all hours purchased (rather than only free hours) would provide a further means of encouraging an expansion of flexible daycare in areas where such provision is less common. This would particularly help incentivise maintained and voluntary providers, which tend to focus on early education, to expand provision across a full day and to younger age groups (which do not receive early education funding). It is likely, however, that local authorities will need to complement per child grants with sustainability grants to develop sufficient flexible services across all areas.

Box 5: Daycare provider case study

We use a stylised example of a daycare model to illustrate the challenges providers operating in areas of disadvantage face and the potential benefits of a reformed subsidy scheme. Assuming costs in line with a high quality, flexible model, providers must meet demanding occupancy targets under current funding arrangements. This helps to explain why daycare is most prevalent in areas of relative prosperity and many schools and voluntary providers have not made the transition to full daycare.

We use the average daycare setting size of 48 and assume 24 of these places are for over-threes, 12 for two-year-olds and 12 for one-year-olds, in line with survey data. We also use a flexible, year-round model of operation, with opening hours of 7.30am to 6.30pm each day for 48 weeks of the year. We estimate staff costs using a high quality model in which the setting has two graduate leaders, and all staff have a tertiary early years qualification. We assume one non-graduate member of staff manages the setting and does not normally have supervisory responsibilities for children. Four of the further non-graduate staff members are supervisory.

	Nursery one (low occupancy)	Nursery two (high occupancy)
Percentage of parents purchasing additional hours	50%	75%
Income from free early education	8 two-year-olds at £5.16/hr: £23,500 19 three- and four-year-olds (80% occupancy), all children eligible for the Early Years Pupil Premium, at £4.19/hr: £45,400 + £5,700 10 three- and four-year-olds eligible for 30 hour offer: £23,900	4 two-year-olds at £5.16/hr: £11,800 19 three- and four-year-olds (80% occupancy), no children eligible for the Early Years Pupil Premium, at £4.19/hr: £45,400 14 three- and four-year-olds eligible for 30 hour offer: £33,400
Income from fees	Under-2s: £4.62/hr Over-2s: £4.39/hr One year olds: £35,700 Two year olds: £44,400 Three and four year olds: £61,500 Total: £141,600	Under-2s: £4.62/hr Over-2s: £4.39/hr One year olds: £79,800 Two year olds: £70,000 Three and four year olds: £107,100 Total: £256,900
Staff wages (FTE)	Manager (£20,500) Graduate (2 * £19,600): Supervisory (4 * £15,900): Non-supervisory (4 * £13,600): £177,700	Manager (£20,500) Graduate (2 * £19,600): Supervisory (4 * £15,900): Non-supervisory (4 * £13,600): £177,700

Non-wage staff costs	£35,100	£35,100
Non-staff costs (such as rent, insurance, facilities, equipment and materials, utilities and IT)	£63,600	£63,600
Total expenditure	£276,400	£276,400
Total income	£240,100	£347,500
Net position:	-£36,300	£71,100

The case study illustrates the difficulty of operating a flexible daycare service offering high quality early education where demand for daycare exists but is less strong than in areas of high parental employment. We have erred on the side of caution in assuming similar costs for each nursery. In reality, a nursery serving a disadvantaged community is more likely to have higher costs. Children are more likely to have additional learning needs, requiring more staff time, and staff are also more likely to spend time supporting parents. Providers are more likely to need, or want, to reduce fees and to subsidise meals and refreshments or activities and trips. These settings are also likely to aim to offer fee discounts and offer meals and refreshments for free, each of which has an additional cost for the nursery. (Equally, stylised occupancy figures probably overstate income in nurseries that benefit from high proportions of parents in work.)

A nursery might seek to bridge the funding gap by employing less qualified staff, charging higher fees or employing minimum booking requirements to boost occupancy. Each, however, would influence access to the service and its impact for the most disadvantaged families. As discussed elsewhere in this paper, consolidating back office costs and reducing staff costs by employing some staff flexibly across settings could also help to bridge funding gaps. Although this case study is of a daycare service, these figures also help illustrate the challenges faced by nursery classes or sessional providers seeking to extend their hours of operation.

Bridging this gap in a way that is effective and good value for the taxpayer is difficult. Across the board increases in early education funding or fee subsidies risk solving the problem in a manner that represents poor value for money. A supply-funded system utilising targeted supplements would afford a more viable and cost-effective mechanism to support sustainability among daycare settings in areas of low parental employment. In particular, extending and increasing the Early Years Pupil Premium to all hours (rather than only free hours) would close the gap substantially, potentially making the setting sustainable with limited direct support from a local authority.

Sources: Eurostat; Ceeda (2014); Brind et al. (2014); Brind et al. (2012)

Parental fees in a supply-funded system

Supply-funded childcare would afford the opportunity to manage the parental contribution to childcare costs rather than leave this judgement to a market that does not always deliver outcomes consistent with public policy aims. Ideally, the subsidy system would achieve the

simple goal of providing a clear incentive for parents to work, or take steps toward work through education and training, ensuring childcare costs are never a barrier to participation.

Designing a subsidy structure that meets this goal presents some practical challenges. The childcare element of tax credits is calculated not only as a percentage of costs – currently 70 per cent and 85 per cent from 2016 – but may be tapered once family income exceeds a certain limit (around two-thirds of parents have their working tax credit award tapered this way). Many parents receiving the childcare element of tax credits do not therefore receive a straightforward subsidy. Tax-free childcare accounts on the other hand are designed to provide a flat-rate subsidy of 20 per cent. Figure 25 illustrates how this system translates into a notional single subsidy (tax-free childcare does not offer the full 20 per cent subsidy in this example because the notional family spends more than the £10,000 annual cap on childcare costs under the scheme).

Figure 25: Percentage childcare costs met, couple with two pre-school children[14]

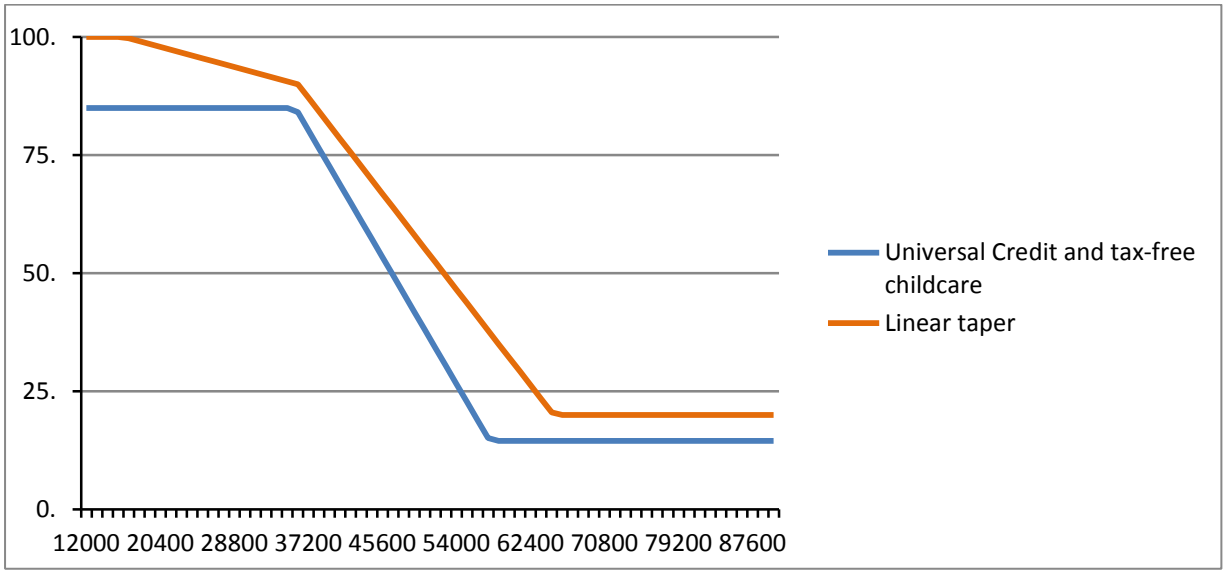
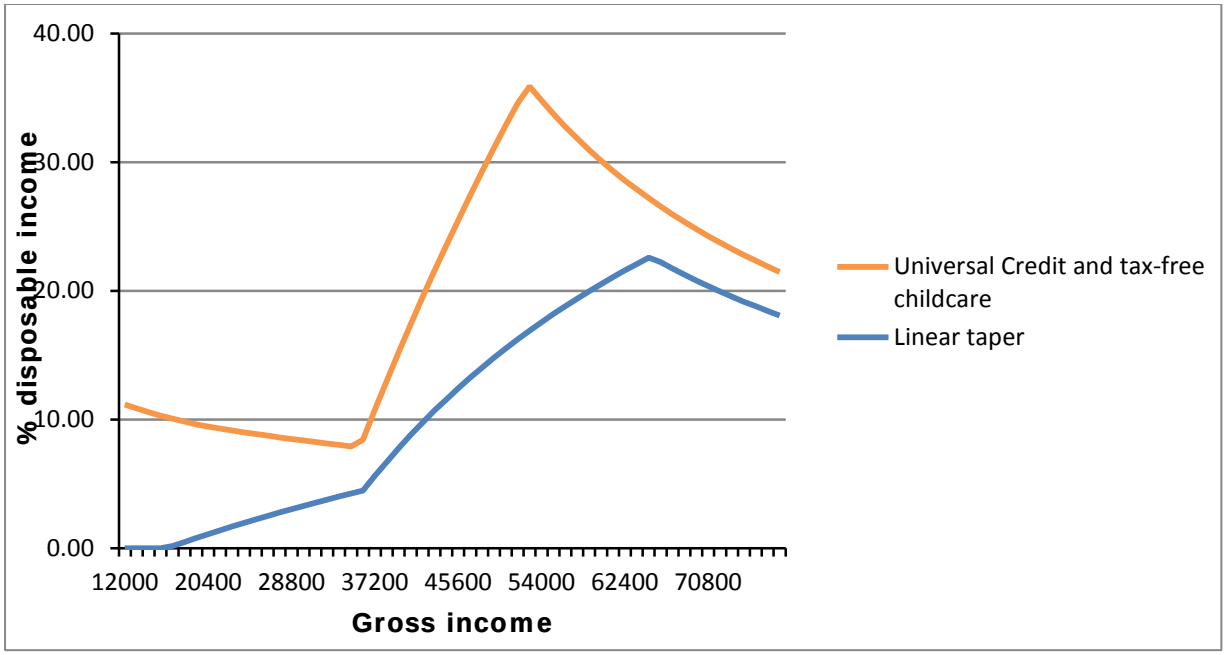


Figure 26: Percentage disposable income spent on childcare, couple with two pre-school children[15]



One way to dampen the abrupt shifts in the current subsidy structure is through a carefully designed linear taper: the percentage subsidy remains constant up to a certain income level and is then tapered at a linear rate to a second level. Figure 25 illustrates the structure of this subsidy. We have suggested a 100 per cent subsidy rate for families earning up to £16,200 (in line with the current eligibility threshold for the free two-year-old offer), a taper to a 90 per cent rate for families earning up to £36,000, and a further taper to a 20 per cent subsidy for families earning up to £65,000. These thresholds are for a couple – thresholds should be adjusted for single parents – and reflect this paper's recommendations for changes to Universal Credit.

Although a linear taper avoids the problem of cliff edges, it is unlikely to address the criticism that the current system is excessively complex and difficult for parents to understand. The approach that best reflects the goal of simplicity is a flat-rate fee per hour. To achieve the same level of support as parents receive under Universal Credit a basic per hour fee would begin at around 50 pence per hour. This fee could be increased in increments, for example by 50 pence or £1 as family income increases. This approach offers simplicity but is less well-targeted and would introduce significant cliff edges that could undermine work incentives. For example, at £1/hr a parent purchasing 40 hours of childcare each week would find their childcare payment increasing by over £160 each month once their income crosses a certain threshold.

Figure 27: Illustrative simple fee structure

Family income	Up to £16,000	Up to £36,000	Up to £46,000	Up to £56,000	Up to £66,000	Over £66,000
Maximum fee per hour (first child)	Free	£0.50	£1.00	£2.00	£3.00	£4.00
Maximum fee (second child)	Free	£0.30	£0.50	£1.00	£1.50	£2.00
Maximum fee (third child)	Free	£0.10	£0.30	£0.50	£0.80	£1.00

We suggest that the best approach is to combine a linear taper with a relatively simple fee model. The cliff edges introduced by an extremely simply fee structure are too significant to overlook, whilst a linear taper is well targeted but excessively complex. In a hybrid system, the parental contribution could rise in 10 pence increments to ensure a sufficiently smooth taper whilst maintaining the benefits of simplicity. Figure 27 illustrates how this fee structure can be set out clearly for parents (these amounts broadly reflect how this fee structure could be mapped onto current subsidies; future increases in average wages and subsidies would require higher fees). Unlike under current arrangements, it would be relatively simple to develop an online calculator that allows parents to see precisely what they can expect to pay for childcare. Figure 28 illustrates how this approach might affect family income and work incentives.

Figure 28: Net family income after childcare by second earner hours per week[16]

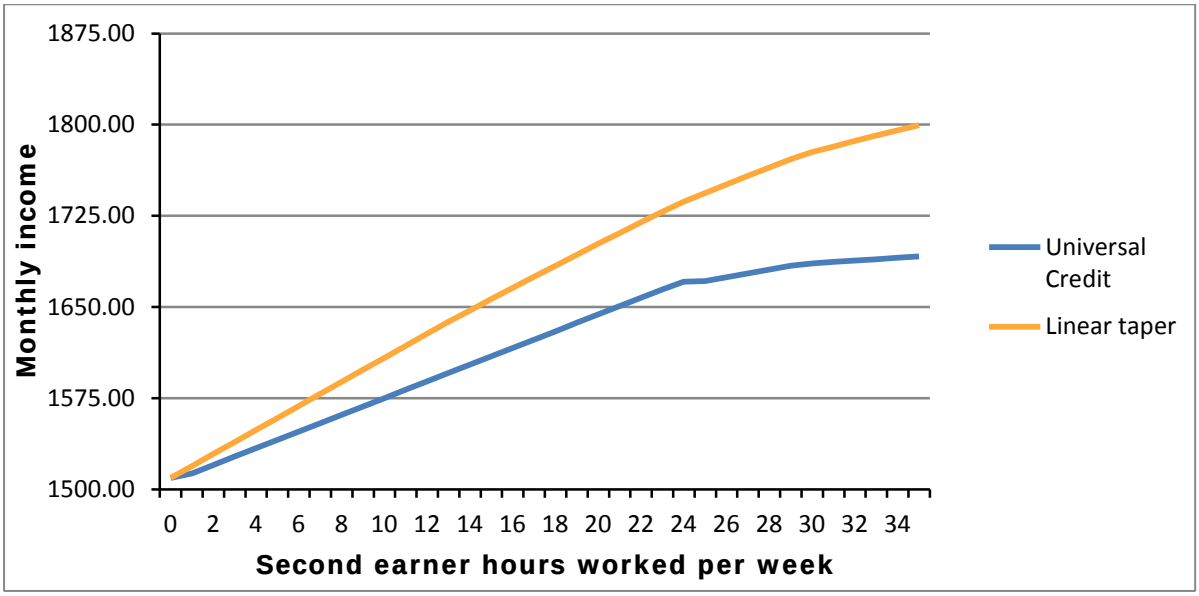
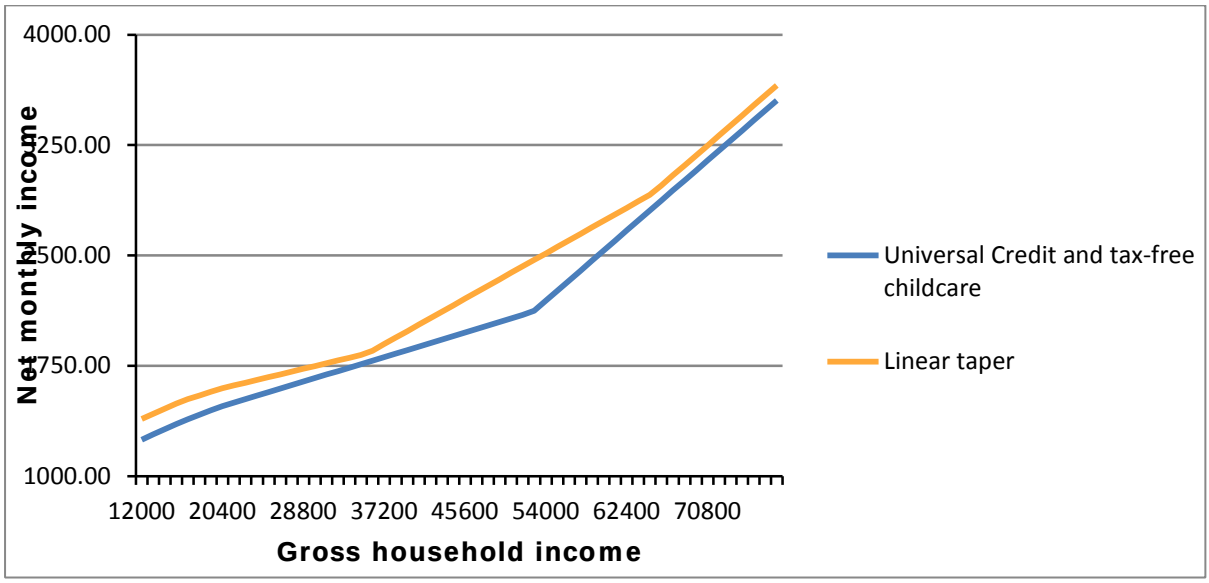


Figure 29: Net family income after childcare by gross income[17]



The kink in the Universal Credit/tax-free childcare line in Figure 29 reflects the problematic interaction between Universal Credit and tax-free childcare, where the tax credit taper leads to a relatively sharp drop in support as earnings rise (Figure 15 similarly highlights the rising proportion of disposable income spent on childcare by families moving from Universal Credit to tax-free childcare). A linear taper subsidy creates a smoother income trajectory as income rises above the Universal Credit eligibility thresholds.

The middle-income families that are hit hardest by fees arguably have more disposable income from which to contribute to childcare costs, but this gap in support is a problem any politically viable approach to reform seemingly must address. Addressing this gap does, however, imply new spending that is not targeted narrowly at families at risk of poverty. We

estimate that the parameters we propose could increase spending on subsidies by up to 25 per cent (at current levels of take-up and parental income), excluding improvements in funding to support quality improvement. The amount of this increase would depend heavily in practice on the responsiveness of parents to the policy. Much of this additional spending would benefit families with low to middle incomes, but some would also support families higher up the income spectrum. A key characteristic of inclusive Nordic systems is that all parents pay low fees. We suggest a midway approach between extremely low fees for all parents, which does not appear to be affordable in the near future, and asking some parents to pay a 100 per cent fee, which is likely to encourage fragmentation of childcare provision as better-off parents seek private services.

This paper sets out the case for a new per child cap on the childcare element in Universal Credit, replacing the current de facto two-child cap in support. A new subsidy scheme should go further than this. Families with more than two children are at greater risk of poverty. It makes little sense to build a childcare system that penalises parents for having greater childcare needs. Subsidies should actively support and encourage parents to work by providing proportionately *more* support rather than less for each additional child in order to sustain work incentives and prevent the parental contribution to childcare fees from rising towards an unrealistic proportion of family income. This is an important feature of Nordic systems that are most successful in removing barriers to work and encouraging take-up of childcare support.

Administering a new system

The basis of any reformed subsidy must be simplicity and user-friendliness. The online account system established to support the tax-free childcare scheme offers a potentially powerful tool to create an administratively simple subsidy scheme. Tax-free childcare accounts will operate much like an online current account: parents transfer money to the account, a top up is added and, when a parent chooses, payment is made to a provider. In contrast to tax credits, parents can build up and bank support to use when needed (and can withdraw money from an account if needed, without the top up). Parents confirm their employment status and income each quarter. This system is less bureaucratic than tax credits, where parents are rarely sure exactly how much support they will receive, with childcare costs and changes of more than £10 to monthly childcare costs must be reported.

The tax-free childcare scheme is likely to work well for providers in comparison to the childcare element of tax credits because it is a ‘closed loop’ system in which funding is transferred directly to providers simplifying payment for parents and reducing administrative costs for providers. This approach is also likely to reduce error and fraud costs. Using tax-free childcare accounts would also help to mitigate against stigma, as providers will have no knowledge of the parental contribution to fees. A sensible approach to reform would be to deliver childcare support for all parents through an account system by developing the infrastructure put in place for tax-free childcare.

Figure 30: Comparison of Universal Credit and proposed subsidy parameters

	Universal Credit (from April 2016)	Proposed subsidy model
Fees	85% subsidy tapered at 65 pence for each pound earned over £6,432 for couples and £8,808 for single parents (this amount is lower if a family receives support with housing costs).	Parents pay a simple fee per hour of care, tapered in 10p increments according to family income
Payment mechanism	Parents receive subsidy one month in arrears. Parents report monthly on any changes in childcare costs over £10.	Parents make payments through an online childcare account and can save and 'bank' support to use as needed.
Means testing	Universal Credit payment is adjusted each month if a family's circumstances change.	Eligibility is reconfirmed each quarter and percentage subsidy is set for three months based on income at beginning of quarter – parents whose income falls may report a change of circumstances.
Reimbursement for providers	Parents pay fees directly to providers 'up front'	Provider costs are met through a local authority grant
Support for more than one child	Support capped for one child at £646 and for two or more children at £1,108 each month.	Fee reduced by 50 per cent for each additional child. Care for any further children is free.

The implications of fee capping

The current market-based approach has the benefit of flexibility: if provider costs increase, but state subsidies do not, providers may increase parental fees. Equally, however, fees at the provider break-even point may exceed affordability for some parents (and providers may, and sometimes do, close because demand falls and too few parents are able to afford fees). Our preferred approach is explicitly designed to control fees as a proportion of income and implies a *de facto* price cap. It is important to situate this approach in the context of a deliberate shift from treating childcare as a marketised commodity to treating it as a vital public good. The latter requires a new approach to funding that is less capricious than the current system.

A price cap creates new risks, such as inadequate funding to sustain sufficient high quality provision or, equally, poor value for money for the state in a for-profit market. These risks demand an effective means of ensuring funding continues to meet policy goals. Current arrangements for funding the early education offer, where local Schools Forums recommend funding rates (within an allocation set by the local authority) could be made more robust. So long as children and parents benefit from clear legal entitlements and quality standards, both central government and in turn local authorities would need to set rates at a level that ensures there is sufficient provision to meet these entitlements. This approach seems to be most consistent with the existing policy and legislative framework and provides more flexibility to accommodate variations in local provider costs and fees.

Another, or complementary, solution would be to establish an advisory body to make a credible evidence-based assessment of reasonable provider costs and recommend funding rates to government and local authorities. The body would be responsible for gathering evidence on provider costs and monitoring the impact of the subsidy scheme on sustainability. The body would then make a recommendation to government on funding rates for different provider types and could make decisions about the appropriate geographic level of funding. This approach would have the benefit of helping to depoliticise an issue than has become increasingly contentious for childcare providers. Ministers would provide a remit for the body and retain ultimate control over funding, but would be held accountable for inadequate funding.

Fee capping naturally leads to the question as to whether early education and care should continue as a for-profit sector. The pragmatic response is that the UK may have, for the time being, little choice on this point. The majority of daycare provision is in the private sector, including in many cases, ownership or leases on premises. To replace this provision government would have to either buy out providers or invest to replicate this provision, which implies significant cost and disruption.

Over a longer period, we do believe that UK governments should re-examine the question of for-profit childcare provision. The government has ruled out for-profit provision in publicly funded primary and secondary education (although schools can charge for out of school care, they cannot make a profit by doing so). It is not clear what justifies making an exception for the early years. The main case for moving to not-for-profit model is that doing so would help ensure as much funding as possible, whether contributed by the government or parents, is invested within the childcare system. On the other hand, it would be difficult to argue on the current evidence that many for-profit models cannot meet higher standards of inclusiveness and quality if they are challenged to do so.

Regardless of an explicit decision to end for-profit provision, capped fees imply capped profits and are likely to lead to a shift over time in childcare provision away from for-profit models: our proposals explicitly seek to increase the role of, and encourage more vibrant competition from, social enterprises. A supply-funded system with capped parental fees would create challenges and potentially uncomfortable change for providers, but these challenges are, demonstrably, not insurmountable. Ultimately, policy-makers must be able to satisfy themselves that for-profit childcare providers are able to operate in a manner consistent with principles of inclusivity and high quality. Proposals we have set out, such as a statutory admissions framework, would test this question.

Recommendation: The government should move quickly to initiate reform of early years childcare funding, moving to a supply-funded model and a simple fee structure

4. A new childcare strategy

Figure 31: Estimated costs of anti-poverty childcare reforms (England)

Policy	Description	Estimated additional cost (£million)
Free early education	Graduate salary supplement Extension of free early education for two-year-olds Quality improvement within the early education offer Double the EYPP to £600 and extend to two-year-olds receiving free early education	£200 (rising over ten years to £500) £304 (60 per cent of children); £912 (all children) £248 (present offer) rising to £425 (free offer extended to all two-year-olds) £128
Sure Start children's centres	Restore revenue spending on children's centres to 2009/10 level	£560 (assuming current spend of £760)
Childminder networks	Graduate-led childminder networks available to all childminders delivering free early education	£26
Inclusion programme	Support for mainstream pre-school settings to offer places to children with special educational needs and disabilities	£251
Childcare entitlement	Capital spending to develop places for one and two-year-olds and extend provider hours; sustainability grants for sessional and nursery class providers in disadvantaged areas extending to daycare hours	£438 in the first year, rising to £578 in the second year and falling each year to £250 in the sixth and subsequent years

Social enterprise programme	Investment readiness funding and match funding to support a growth in early years social enterprises	£58
Supply-funded subsidy scheme	Supply-funded delivery of early years childcare, including: - high quality, graduate-led free offer - subsidised additional hours - equalisation of wages in private/voluntary and maintained settings	£10,675 (approximately £2,541 of which is accounted for by wage improvements)* *These figure reflects an assumption of significant increased take-up (see policy costings in Appendix B); they are not therefore an estimate of delivering existing provision, or improving wages at current staffing levels, through a supply-funded system.
Estimated spending 2017/18 Estimated cost after ten years		£7,466 £12,708

Figure 32: Implied devolved spending (£million)

Nation	Graduate-led high quality free early education	Children's centres and early years services	Pre-school childcare subsidies	Total	Estimated childcare spending in 2017/18[18]
Scotland	£434	£130	£708	£1,272	£736
Wales	£248	£74	£405	£727	£415
Northern Ireland	£150	£45	£244	£439	£250

Figure 31 sets out the estimated costs of our proposals in England (our methodology is set out in Appendix B). Figure 32 sets out the implied additional spending for the devolved nations in broad policy categories. Whilst these costs are significant, they should be understood in the context of a long-term strategy to create a universal childcare system with strong anti-poverty characteristics. There are potential long-term fiscal benefits to this investment that, if policy is sufficiently well-designed, would offset and in the long-term exceed these costs (see Box 3).

The UK spends approximately 0.5 per cent of GDP on early childhood services compared to 0.7 to 1.1 per cent in the Nordic nations with higher maternal employment levels and lower levels of child poverty (OECD, 2014). Our estimated costings suggest that reaching 0.85 per cent of GDP, or around £12.7 billion, would allow for investment in a range of anti-poverty priorities within a system that is sufficiently inclusive of families with middle-incomes to be politically viable over the long term. This figure would rise further should parental employment rise in future, as hoped. A more responsive childcare system will be a more expensive one, but these costs must be offset against the substantial direct and indirect long-term fiscal benefits of improved outcomes for families.

The government should not wait to invest in anti-poverty childcare priorities. We have divided our recommendations into those that can be achieved in the short- to medium-term and those that require funding reform and long-term investment (see Figure 1). We have prioritised steps that are most likely to have an impact on families in, or at risk of, poverty. These fall broadly into two categories:

- realising the potential of early education to act as a protective factor against poverty by improving quality by investing in staff and the quality improvement infrastructure of childcare; and

- improving parents' responsiveness to childcare subsidies where there is unmet demand by improving access to flexible daycare and investing in targeted affordability measures that benefit parents in poverty or at the greatest distance from the labour market.

Policy-makers pursuing an anti-poverty strategy can best pursue a dual-track approach; redirecting resources in the short term to address the most pressing investment priorities whilst re-organising funding in the medium term to create a more effective childcare system and create the structures for long-term investment.

Figure 1 sets out the proposed phases of reform. The first steps are designed to lay the groundwork for supply-led funding reform by developing and expanding services. We prioritise quality improvement in early education and investment in child and family support services to address the most pressing challenge in fulfilling the potential of free childcare to improve outcomes for children. This is followed by significant new investment to develop flexible childcare services in the least affluent areas and create a clear parental expectation of access to affordable pre-school childcare. Finally, reform of early years funding structures to a supply-led model will put flexible, high quality services on a stable and sustainable basis and provide government with the means to increase early years wages.

We have set out these proposals in 'modular' form as many could be usefully pursued individually. However, the government should not defer initiating comprehensive childcare funding reform. The government has rightly identified that childcare provision is inadequate to meet the needs of parents in a changing society, but is pursuing solutions that will not address the root causes of dissatisfaction with the current system. This paper has aimed to highlight that the nature, purpose and ethos of the childcare system is important. Policy aims such as guaranteeing access to high quality care and improving staff wages and working conditions are difficult, if not impossible, to achieve within current funding structures. Piecemeal measures are unlikely to substantively address anti-poverty priorities.

The momentum behind childcare reform is currently stronger in the devolved administrations than in England (see Box 5). Whilst our proposals broadly apply across the UK, good solutions will look different in each devolved nation — for example, each nation has a different approach to children's centres and early intervention services. Devolved policy-makers are hampered by current childcare funding arrangements as they have no control

over demand-side childcare funding within tax credits, the employer-supported childcare scheme or the tax-free childcare scheme. Funding reform must begin in Westminster, freeing up the devolved administrations to pursue appropriate local policies.

Box 5: Childcare reform in the devolved administrations

A number of recent initiatives show that each devolved government is well-prepared to pursue tailored devolved solutions to childcare reform.

The Scottish government recently commissioned an independent review of the Scottish childcare workforce by Professor Iram Siraj, which was published in June 2015 and proposes steps to improve workforce training, development and support (Siraj and Kingston, 2015). The independent Scottish Commission for Childcare Reform also recently set out a range of recommendations to ensure that parents have access to affordable, flexible childcare throughout the week (Children in Scotland, 2015). Notably, the Commission recommended a fundamental review of the UK childcare funding system involving all UK governments. The Scottish National Party itself set out its aspiration in the independence White Paper, *Future Scotland*, to move to a supply-funded system and increase free care for all children from age one to four in an independent Scotland.

These developments reflect the desire among Scottish leaders and policy-makers to improve the funding and delivery of childcare. This momentum may, however, stall if the Scottish government does not gain greater control over funding for childcare. Our proposals would allow the Scottish government to deliver the independent Childcare Commission's recommendation of a flexible childcare place for every child, using a supply-funded system consistent with the Commission's recommendation of a tapered fee model keeping fees below 10 per cent of a family's disposable income.

The Welsh Assembly Government has worked proactively to improve childcare provision, publishing *Building A Brighter Future*, a ten-year plan for childcare in 2013 and a draft ten-year workforce strategy in 2015 (Welsh Government, 2013; 2015). The Welsh Assembly Government has also recently acted to support local authorities in implementing the Childcare Act 2006 sufficiency duty, revising and updating statutory guidance and tools, and is expanding the early years Flying Start programme. But families in Wales are also affected by particularly poor access to affordable, flexible childcare, in great part due to the practical challenges of delivering childcare in Wales, with a dispersed population and pockets of severe deprivation.

The Welsh Assembly Government is not currently empowered to develop policies that respond effectively to the magnitude of Welsh childcare challenges. Additional funding would allow Welsh policy-makers to address persistent sufficiency problems and promote the supply of places to halt rapid rises in costs. The Welsh government would also be able to gradually expand Flying Start, addressing a key criticism that the current model reaches too few children.

Centre-based childcare provision is less developed in Northern Ireland than elsewhere in the UK – the main form of early years provision is maintained nursery classes in schools, which often lack flexibility. The Northern Ireland Executive published a new ten-year childcare strategy, *Delivering Social Change Through Childcare*, in 2015 (Northern Ireland Executive, 2015). The strategy contains many positive proposals and commitments, notably investing to develop new places to address the most pressing gaps in provision. However, the strategy is almost modest in many of its aspirations, for example, having limited commitments to quality improvement and committing to fund just 1,000 new flexible pre-school places.

The scope of Northern Ireland's childcare strategy reflects the funding constraints within which the Northern Ireland Executive must work. In the past, Northern Ireland has invested less in free early education than each UK nation and therefore must prioritise extending free care to two- and three-year-olds in order to develop sustainable early years services beyond nursery classes. Whilst in some respects childcare provision in Northern Ireland significantly lags that elsewhere in the UK, this counter-intuitively means that, with the benefit of investment, policy-makers would have the opportunity to guide the development of services more strategically than has been possible elsewhere in the UK to date.

The government can free up funding for immediate investment by re-prioritising some poor value childcare spending. HMRC figures indicate that around £200 million is spent each year on tax relief for workplace nurseries and directly contracted childcare (HMRC, 2014). A small proportion of parents benefit from this subsidy, which was established in 1990 when childcare subsidies were far less extensive than is currently the case. Moreover, this tax relief is principally received by nurseries that are 'linked' with employers through direct contracting rather than on-site nurseries. Whilst some of this funding is well spent, it is difficult to argue that the total amount is being invested strategically. Where there is a case for direct investment in settings, this should be based on need and we set out proposals for a properly funded pre-school childcare entitlement to achieve this.

Lowering the maximum eligibility threshold for the tax-free childcare scheme from the current level of £150,000 (or £300,000 for a couple) would also yield savings that could be re-invested elsewhere. The Resolution Foundation has estimated that £150 million could be saved by lowering the eligibility cap for the scheme to £65,000 per parent or £130,000 for a couple (Finch, 2015). As the tax-free childcare scheme is rolled out, the government plans to phase out the employer supported childcare voucher scheme by allowing parents to continue to use that scheme until their children are no longer eligible or they move to the tax-free childcare scheme. Winding down the employer supported childcare scheme at a faster pace could also save up to an additional £200 million each year (this amount would decline each year and reduce to zero).

The introduction of an early years admissions framework could also generate savings, as a proportion of independent providers may opt out of public subsidies in order to continue to operate independent admissions arrangements. According to Department for Education data, two per cent of providers delivering the early education offer are registered as independent schools. However, many independent nursery providers that operate selective admissions procedures are registered as early years providers with Ofsted and would not appear in these statistics as an independent school (neither early years registration with Ofsted nor access to early education funding carries a requirement not to operate a selective admissions process). Around seven per cent of children attend independent schools and the 'true' figure of independent nurseries and nursery classes may be higher than two per cent. A proportion of these providers might choose to participate in a statutory admissions framework, but the remainder would no longer receive public subsidies.

These options would create losers and no doubt are politically unpalatable. However, there is the potential for the government to quickly generate a substantial pool of funding – potentially over £550 million – by ending some poor value spending that could be better used elsewhere. Whilst the government is investing in childcare, it is not investing adequately in policies that will realise the potential of childcare to improve outcomes for the most disadvantaged children and families. Choices such as these must be considered if new funding cannot be found to meet anti-poverty priorities.

Despite stalling during the 2010-15 Parliament, investment in childcare is set to rise significantly across the UK in the next five years through the roll-out of the tax-free childcare

scheme and Universal Credit, and extensions to free early education. Given the constraints imposed by government on public spending since 2009, the striking fact has not been the reluctance of recent governments to invest in childcare, but their willingness to do so. A question mark remains, however, over how this funding is being used. Government is right to recognise that childcare is a strategic priority in a changing society. By recognising the need to make better use of investment, the government can continue to invest at a sustainable rate and develop the childcare system a modern UK society needs.

5. Conclusion

This paper has set out where the current pre-school childcare system falls short of fulfilling its anti-poverty potential, what the evidence suggests an anti-poverty childcare system should look like and how this system can be realised. The root of the flaws of the current system lies in the failure of UK governments to set out and pursue a coherent vision for childcare. Separate funding streams have been set up at different times and for different purposes with little thought to the overall picture of childcare provision. The fragmentation of funding has led to ambiguity about the policy aims of investment in childcare and insufficiently strong steps to integrate diverse policy aims. All childcare funding, whether it flows through tax credits, a voucher scheme or free early education, influences the same early years provision for families. Yet the UK has drifted into a funding structure that does not give government the tools needed to improve quality, access and affordability.

To address these problems, we propose the government should set out clearly its aims for childcare and build a funding system to meet those aims. In the most successful pre-school childcare systems, embodied by the 'Nordic model', the majority of funding goes directly to providers (supply-side funding). This allows the state to offer clear entitlements for parents, promote service models that meet both the development needs of children and the childcare needs of parents, and exert strong control over quality and affordability. In order to meet key policy aims, UK governments should rebalance childcare funding to the supply side.

Childcare provision is a product of the way childcare is funded. A fragmented funding system contributes to fragmented and uneven provision that delivers uneven outcomes and poor value for money. A supply-funded system can fundamentally shift childcare from being perceived as a commodity to a public good and significantly raise the standard of provision. There is a role for competition and choice in a supply-funded system, moderated by the constraints necessary to guarantee access to high quality, flexible and affordable care.

Unfortunately, the government currently appears to be moving further away from fundamental childcare funding reform. With each new demand-side childcare measure, it becomes harder for the government to influence the supply of childcare or control the parental contribution to the cost of care. This lack of control is increasingly striking given the government's rising share of spending as a proportion of revenue in formal childcare.

Evidence suggests that a strong degree of universalism is central to effective early intervention: it is only by reaching all children that those with additional needs can be identified and supported in a non-stigmatised, socially mixed context. The free early education offer provides a valuable platform for early intervention in the UK but is not utilised as effectively as it could be. The links between universal childcare provision and services that drive early intervention, such as children's centres, are therefore critical. Given the UK's complex mixed market of provision, in which many providers have weak links with early intervention services, this is a difficult challenge that requires childcare providers to work in new ways.

Lloyd and Potter (2014) highlight the conflicting evidence regarding the role of formal childcare in supporting maternal employment. It makes sense that where formal childcare provision is already good, or informal care is readily available, expanding childcare subsidies is unlikely to affect parental employment except so far as financial incentives to work are improved. Our proposals are intended to avoid inefficient investment as far as possible. Spending should be directed where investment can improve work incentives for families with low incomes and remove access barriers for those who experience barriers to employment, whilst avoiding poor value for money associated with large extensions to the free childcare offer or generous subsidies for parents with high incomes. The UK can create an anti-

poverty childcare system that is good value for money: this means placing an emphasis on quality and a simple but responsive system of entitlements and subsidies.

A significant caveat for anti-poverty policies predicated on increased parental employment is that there is a prerequisite of suitable family-friendly work opportunities. The current labour market context of underemployment and scarcity of high quality part-time work suggests anti-poverty strategies must look beyond improved childcare provision and conditionality in Universal Credit to the factors that shape the work opportunities available to parents, such as access to education and financial work incentives. Policy measures that rest on conditionality in welfare and childcare support alone seem likely to lead to disappointing results.

The government can achieve a great deal to transform childcare within modest spending constraints but, in the long term, the UK cannot achieve a world-class childcare system without fundamental funding reform and new investment. Childcare has become a high profile political priority but this has not led to sufficient attention to measures to support the most disadvantaged children and families. Investment in childcare measures specifically designed to help reduce poverty is a strategic imperative that should be prioritised by policy-makers, not ignored because it is fiscally or politically difficult.

The UK already has a mature childcare system, although one that is flawed, and policy recommendations must set out a practical route to build on this system. Yet an incremental 'building on' approach has manifestly failed to address many of the key policy challenges childcare presents. Escaping this status quo requires the willingness to challenge entrenched norms and practices and set higher aspirations for the childcare system. Our aim has been not only to set out an ambitious vision for childcare but to show how this vision can be achieved through reforms to key policy and funding structures and a viable plan of investment.

Despite the progress that has been made in the last two decades, the UK childcare system continues to represent an unfulfilled opportunity. The UK is in a strong position: the basis of a world-class childcare system is already in place. Policy-makers should grasp the opportunity to translate the potential of this system into reality.

List of recommendations

High quality early education and effective early intervention

UK governments should commit to a fully graduate-led early years workforce, supported by funding to meet training and wage costs

Funding for free early education should be increased in order to deliver quality care

The Early Years Pupil Premium should be increased to £600 per child and extended to the two-year-old offer (and introduced in the devolved administrations)

Duties in the Early Years Foundation Stage framework and devolved equivalents to support home learning should be clarified and strengthened

UK governments should clarify the status and aims of children's centres (and devolved equivalents) and ensure sufficient funding to provide universal early intervention and family support services

UK governments should work with professionals and children to design an age-appropriate statutory assessment, which ensures all children receive a developmental check on entry and exit from early education

Ofsted and devolved regulators should align early years inspection frameworks with appropriate process quality measures

UK governments should implement an early years workforce strategy and pay transformation programme to improve staff pay among private and voluntary sector childcare providers

Supporting parents through accessible, flexible childcare

UK governments should develop a statutory admissions code of practice for children accessing early years provision in centre-based providers

Each UK government should establish a well-funded social enterprise programme to promote inclusive pre-school nursery provision

UK governments should introduce an entitlement to pre-school childcare across a full day throughout the year, supported by a stream of sufficiency funding for local authorities

Each UK government should roll out a funded statutory early years inclusion framework that ensures children with special educational needs and disabilities are able to access a wide range of high quality childcare settings at no additional cost

Government should fund graduate-led childminder networks for all childminders delivering free early education

UK governments should provide 15 hours of free early education for all children aged two to four

Childcare and Universal Credit

The government should increase the childcare element of Universal Credit to 100% for families with an income below the relative poverty threshold

The Department for Work and Pensions should establish a facility to pay any up-front childcare fees for parents eligible for the childcare element of Universal Credit

The government should uprate the Universal Credit childcare element cap in line with childcare costs and remove the two-child cap

The childcare element of Universal Credit should be extended to jobseekers and parents participating in work preparation activities, including education and training

The government should introduce a second earner allowance in Universal Credit, which creates realistic work incentives for second earners moving into work

Childcare subsidy reform and supply-funded childcare

The government should move quickly to initiate reform of early years childcare funding, moving to a supply-funded model and a simple, progressive fee structure

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Appendix A

Early childhood education and care and poverty evidence review summary

Lloyd and Potter (2014) set out evidence that good quality, affordable and accessible childcare creates two potential pathways for impact on child poverty prevention and elimination by promoting children's development, leading to better educational outcomes and life chances, facilitating parental employment, and strengthening families' economic wellbeing. These impacts have the potential to eliminate inequalities in achievement between children with different backgrounds.

Only good quality early childhood education and care (ECEC) has long-term beneficial effects for disadvantaged children and the impact of poor quality care is proportionately greater for these children. In addition to the background of parents, such as previous education and skills, affordable and high quality childcare interacts with the local job market and the benefits system to determine the opportunities for families to maintain a sufficient income.

All four nations in the UK have a mixed childcare market of public, private and not-for-profit provision. Provision is commonly divided between maintained settings (i.e. settings that are principally publicly funded) and the private voluntary and independent (PVI) sector. All four countries also rely on a funding system that divides support for parents between a free early education offer, which varies in scope across the UK, and demand-side funding shaped in Westminster through the childcare element of working tax credit (in future Universal Credit), employer-supported childcare vouchers and, from September 2015, a tax-free childcare scheme.

Children from families with low incomes, minority communities, and those who have additional needs, are less likely to use ECEC services than their peers. Some, but not all, of these differences can be explained by the work status of parents. Disadvantaged children are more likely to receive care in a maintained setting, with the notable exception that most children taking up the offer of free childcare for the most disadvantaged two-year-olds in England are accessing the offer in PVI settings.

Quality and the ECEC system

Lloyd and Potter (2014) summarise evidence on the impact of free early education on development gaps and children's social mobility drawing on the EPPE study (Sylva et al., 2004). High quality early education provides benefits in relation to improvements in children's school readiness and cognitive outcomes at five to seven years. The effects of pre-school experiences were still felt at the point when children transitioned to secondary education, and also when child and family factors were controlled for and service quality was again key to positive outcomes. The impact of high quality early education is greater for boys, children with special educational needs, and those from disadvantaged backgrounds. Poor quality early education has little or no positive impact on children's outcomes. The home learning environment has a much stronger impact in children's outcomes than does early education, or parents' social grade or income.

Evidence from the EPPE study suggested that the amount, in months, of early education is important: an earlier start (under age three) is related to better intellectual development, provided children attend in high quality settings. The number of hours per week of free early education does not have a significant effect on children's outcomes at age five once a minimum threshold of hours per week has been reached. However, the duration in months

and years of early education and regularity of attendance are more important. Current UK evidence relates primarily to children who are three and over. The evidence base of the impact of early education for children from birth to school in the UK is limited. Policy-makers must often draw conclusions from targeted studies and international evidence.

High quality ECEC must be part of wider anti-poverty strategies to have an optimal impact in promoting social mobility. Research evidence suggests that supporting parents - bringing up children in difficult circumstances to create a positive home learning environment - must be an absolute priority. Equally important is the need to promote high quality ECEC if disadvantaged children are to benefit.

Targeting provision exclusively at disadvantaged children is not a strategy that follows from research evidence, which suggests the social mix of children in ECEC settings is a crucial aspect of quality and outcomes. Several major European research reviews conclude that universal services in which special attention is given to disadvantaged children should be preferred over separate provision focused exclusively on targeted populations. In addition to encouraging segregated services, targeted approaches are less effective at identifying needs.

Resources are being withdrawn from children's centres, which puts targeted support for the most disadvantaged children and early intervention at risk. The ability of local authorities to integrate services may be more limited where they are not able to co-locate services.

Good quality provision is harder to find in the most disadvantaged areas, according to UK studies of provision using the internationally recognised Early Childhood Environment Ratings Scale, quality measures and Ofsted grades. The Ofsted framework, however, is not designed as a fine-grained quality measure and should not be relied upon as such by policy-makers. One of the key respects in which poor quality provision differs from good quality settings is in the employment conditions and the spectrum of qualifications held by staff, over and above, minimum requirements.

Whilst the roll-out of the Early Years Foundation Stage framework should have helped to improve the quality of care in formal settings, outcomes as measured by the Early Years Foundation Stage profile assessment have subsequently improved relatively modestly. Ofsted has highlighted that the gap between outcomes for the most and least disadvantaged children in school readiness is failing to close significantly.

The quality of individual ECEC services is inextricably linked to the quality of the ECEC system in which services are embedded. The dynamics of competition and choice may drive provision into economically more prosperous areas and put pressure on staff pay, conditions and training. Many small for-profit providers struggle to exceed minimum quality standards set by Ofsted. A market model and reliance on demand-side parental subsidies limits the government's ability to intervene in the market to promote quality. There are limitations and tensions inherent in an ECEC market model. Unencumbered for-profit provision maybe inappropriate even from an economic perspective.

According to the comparative studies of ECEC undertaken by international organisations, the extent to which a system is 'coherent and extensive' is a critical determinant of quality. Substantial investment in both ECEC and its infrastructure is needed to achieve these goals. From an economic perspective, ECEC should be thought of as a 'public good' rather than a service provided within a market, with benefits for children, families, governments and national economies. The manner in which policy frames ECEC produces different outcomes for ECEC systems. In the UK, ECEC is marketised and the richest parents benefit disproportionately from ECEC provision.

An OECD thematic survey and recent analysis of OECD data concludes that the most successful forms of government intervention appear to promote supply-led systems and limit parental fees. In making recommendations on how to achieve access to quality and affordable ECEC provision for poor children, ECEC delivery mechanisms and the wider UK childcare market context ought to be considered. Debate should not be centred on the perfection of an ECEC system based on a market, competition and choice, but should involve a wider examination of the values and principles underpinning the ECEC system.

Economic wellbeing

There is conflicting evidence of the impact of reduced childcare costs on parental labour market participation both internationally and in the UK. Access to affordable childcare is one of a number of factors, including job opportunities, incentives in the tax and benefit system, women's educational levels and parental preferences that determine maternal employment. In the UK, parental preferences do not appear to be closely matched with eventual employment decisions and opportunities.

Lloyd and Potter (2014) highlight the importance of decoupling childcare subsidies from employment status if the children of parents with low incomes, who may be in intermittent employment, are to benefit from stable ECEC provision. The early education offer helps to achieve this goal, but parents may be forced to prematurely alter formal childcare arrangements, such as changing a nursery, if they can no longer top up free hours (or their child is aged below two and does not have access to free hours). Extending the early education offer could simplify access and flexibility and have a positive effect on provider sustainability. Successful integrated systems like the Nordic systems do, however, charge parents fees and are not free at the point of delivery. These fees are low in comparison to the UK and must also be seen in the context of generous direct subsidies to providers.

The early education offer in the UK consumes a significant proportion of ECEC funding by comparison with similar developed nations. UK policy-makers are faced with the problem of improving quality and access without realistically being able to introduce charging for free early education.

Recommendations

Lloyd and Potter conclude that the evidence suggests that children in poverty in the UK are not yet benefitting fully from ECEC. The evidence base for the two-year-old offer in its current form, with the majority of children receiving care in settings of insufficient quality and which lack a 'whole family' approach, is slight and there are continuing problems with the quality of wider ECEC, including in maintained settings.

The way in which state support is allocated between parents and ECEC providers may lead to different impacts on social groups, with the most disadvantaged children at risk of losing out. The UK has one of the most privatised and marketised ECEC systems in Europe. The market structure of ECEC provision creates practical problems for parents around access and affordability and sustainability challenges for providers. International examples suggest that the operation of the ECEC market could be improved by means of more stringent requirements for providers to qualify for public subsidies. In Norway, where a mixed ECEC market is carefully regulated, research evidence indicates positive and equitable outcomes for children's social mobility and families' economic wellbeing.

The authors set out five recommendations for policy-makers, highlighting that these are interdependent and in need of further refinement:

1. Review the current structure of government intervention in ECEC

The UK early childhood education and care system is overly complex. It needs to be simplified and made more transparent to deliver both social mobility and economic wellbeing. Aspects that need to be reviewed include the promotion of socially mixed provision, the role of local government, the qualifications, pay and employment conditions of the ECEC workforce and levels of direct support for providers, in order to ensure a high quality, flexible, accessible, affordable and sustainable ECEC service.

2. Government support for parental childcare costs should be simplified

The level of up-front parental contributions to childcare costs needs to be reviewed as well as the current multiple support strategies through the tax and benefit systems. The availability of sufficient and affordable early childhood provision interacts with local job opportunities and the tax and benefits system, in determining whether, dual or single earner families with young children, can escape or avoid family poverty through paid work.

3. There should be no trade-off in quality between the publicly supported ECEC, driven primarily by social mobility, and that driven primarily by economic wellbeing.

Maintaining and improving quality in ECEC is especially vital if its dual purpose is to be realised and harm avoided to the life chances of poor children, who suffer more as a result of poor quality provision.

4. Support for children's centres should be increased

Children's centres should be hubs of whole-family support, including more of them offering ECEC alongside other services. In parallel, local government should play a more prominent role in supporting service quality and access to ECEC, especially for poor children.

5. Support for parents to maintain a good home learning environment should be strengthened

A good home learning environment is more important for young children's development than parental education or socio-economic status. Reducing the burden of family poverty helps parents create or maintain a good home learning environment. This is another area in which children's centres could provide practical support to parents within their communities.

In summary, these recommendations are broad and in need of further refinement. Improving quality, affordability and access to provision for poor children all pose major challenges. A refocusing of policy on the rationales for public support for ECEC is urgently needed, as the reality does not seem to match the government's stated intention of promoting social mobility, economic wellbeing and social justice through public support for ECEC. Perhaps most of all, the workings of the UK's ECEC market need reconsidering from a principled, as well as from a pragmatic perspective, if ECEC is to make a serious contribution to lifting poor children out of poverty and improving their life chances.

Appendix B: Policy costings

Funding for early years graduates

We assume that the proportion of staff qualified to graduate level in private and voluntary sector provision must increase to the same level as nursery schools – 35 per cent – in order to ensure every child benefits from graduate-led care (Brind et al., 2014). This would require an additional 84,000 qualified graduates in private and voluntary settings. Recent research suggests the average difference between the annual salary of a non-graduate and graduate staff member is approximately £6,000 (Ceeda, 2014). The implied long-term cost of a fully graduate-led workforce is an additional £500 million annually. There is a limited number of newly qualified early years graduates each year, so the cost of a graduate subsidy would initially be lower than this amount and would rise in line with the increase in proportion of graduates in early years settings.

Free early education

Estimate for the cost of a universal two-year-old offer from Brewer et al., 2014b.

For funding increases to improve the quality of free early education, we assume a 21 per cent increase in subsidies for three- and four-year-old children, and an 18 per cent increase for two-year-old children. These adjustments affect only the proportion of early education delivered by non-maintained providers. These percentages are based on analysis of the gap in funding between present levels and the cost of high quality care set out in *Counting the cost: An analysis of delivery costs for funded early education and childcare* (Ceeda, 2014).

Early Years Pupil Premium

The current allocation for the EYPP is £300 each year per eligible child at a total cost of £50 million for approximately 40 per cent of three- and four-year olds. Eligibility criteria for the EYPP are nearly identical to those for the two-year-old offer (the two-year-old offer is available to children with a statement of special educational needs, an education, health and care plan, or who are eligible for Disability Living Allowance, but the EYPP is not). The cost of doubling the EYPP is therefore a further £50 million. The cost of extending the EYPP at £600 to 130,000 two-year-olds (the 40 per cent of children who are eligible for the two-year-old free early education offer) is a further £78 million.

Children's centres

We propose increasing funding for child and family support services from present levels of spending to the level in 2009/10, £1.3 billion, as a proxy for the level necessary to support an effective universal offer (Stewart and Obolenskaya, 2015).

Pre-school childcare entitlement

Current sessional and school-based services models cannot, all at once, be transformed into flexible provision. Rather, we estimate the cost of a rolling programme of capital and revenue support to transform services over a ten-year period. We suggest that the programme should combine targeted investment to extend flexible provision among providers serving the least affluent communities and a flexible discretionary grant of £250 million to support flexibility in wider services through capital and revenue spending.

We assume that in the first stage of the programme new daycare places will be required for 30 per cent of one-year-olds, and that 30 per cent of sessional and nursery class provision serving two- to four-year-olds will transition to full daycare. It is likely that increasing the flexibility of sessional and school-based provision would lead to some consolidation of settings; however, we do not assume savings from such consolidation.

We estimate capital spending of £650 per one-year-old place using ONS population estimates for 2015/16 and estimated capital investment per new place for the roll-out of the two-year-old offer. We also assume sustainability funding is required to support these places for five years, initially at 50 per cent of the cost of each full-time place, falling to 30 per cent in the second and third years, and finally to 10 per cent for the final two years. We estimate the cost of this grant based on average fees in Britain at 75 per cent occupancy of the mean number of places per setting by provider type (Brind et al., 2014).

We estimate the capital cost of supporting 30 per cent of sessional providers and nursery classes to move to daycare hours. We also assume a revenue subsidy of 30 per cent of the cost of additional hours (6 hours per day in sessional provision and 5 hours in nursery classes) for two years, falling subsequently to 10 per cent. We also assume, based on recent Department for Education survey data, that half of nursery classes already operate extended hours. Capital funding for adaptations or expansion to these settings is estimated to be less than that required to create a new place, at £400 per place.

<u>New one-year-old places:</u>

Capital: £118,000,000
Revenue (year one): £227,000,000
Revenue (years two and three): £136,000,000
Revenue (years four and five): £45,000,000

<u>Sessional provider transitional funding:</u>

Capital: £31,000,000
Revenue (years one and two): £109,000,000
Revenue (years three to five): £36,000,000

<u>Nursery class transitional funding:</u>

Capital: £14,000,000
Revenue (years one and two): £54,000,000
Revenue (years three to five): £18,000,000

Year	Capital	Revenue	Total (inc. £250million flexible grant)
One	£59,000,000; £16,000,000; £7,000,000	£114,000,000; £55,000,000; £27,000,000	£438,000,000
Two	£59,000,000; £16,000,000; £7,000,000	£114,000,000; £55,000,000; £27,000,000 / £68,000,000; £55,000,000; £27,000,000	£578,000,000

Three	£75,000,000	£68,000,000; £18,000,000; £9,000,000 / £114,000,000; £55,000,000; £27,000,000	£441,000,000
Four		£23,000,000; £18,000,000; £9,000,000 / £68,000,000; £18,000,000; £9,000,000	£395,000,000
Five		£23,000,000; £18,000,000; £9,000,000 / £23,000,000; £18,000,000; £9,000,000	£350,000,000
Six onwards			£250,000,000

Universal Credit

To estimate the cost of free childcare, we use the estimated cost of the childcare element under Universal Credit of £1.7 billion (House of Lords, 2015), assuming 50 per cent of families eligible for tax credits have an income below the relative poverty threshold after housing costs (HMRC, 2015).

Extending access to the childcare element of Universal Credit to parents in education or training: the government estimated in 2008 that providing support with childcare costs for 50,000 parents who are in education or training through 67 local authorities would cost £75 million each year (the Free Childcare for Training and Learning for Work scheme). We adjust for inflation and use this figure to estimate the national cost of a similar scheme.

Inclusion strategy

Early years area special educational needs coordinators (SENCOs) are graduate-level staff who complete a postgraduate qualification meeting standards set by central government. SENCOs receive a salary supplement of between £2,000 and £4,000. The fee for a suitable postgraduate qualification is typically around £6,000. Guidance published in 2005 suggested that the ideal ratio of early years area SENCOs to settings is one SENCO for every 20 non-maintained settings. Anecdotal evidence suggests the current ratio is as low as 1:50. This means around 2,100 additional area SENCOs are needed. We estimate the cost of an additional 2,500 early years area SENCOs at a total of £21 million in wage costs and £4.5 million in training costs.

We estimate that a training budget that allows for three days of specialist training each year for members of staff in every centre-based setting and one quarter of childminders – covering both skills development and *ad hoc* training for individual children – would cost £30 million each year.

Assuming all children aged one to four with an education, health and care plan require an additional staff member to be present (0.7 per cent of children age three and four have an EHC or SEN statement), an annual budget of around £195 million is needed to meet additional staff costs. This figure is likely to be an over-estimate as many children with an EHC plan do not require additional supervision. As staff gain confidence and benefit from additional training, it is also likely mainstream settings will gain confidence that they can care for children with disabilities, in many cases without additional staff members.

Childminder networks

We estimate that, on average, three graduate-led networks are needed for each local authority to ensure that all childminders delivering the early education offer have access to a network (currently around 17,000 childminders in England). If each network is led by an early years graduate at the average salary for a nursery school teacher, this implies an annual staff cost of £17.5 million (assuming staff are based in local authority premises). We further assume an annual materials and training budget of £500 per childminder (£8.5 million).

Supply-funded childcare

We estimate the total cost of supply-funded care in three scenarios. The first reflects the cost of an improved 'high quality' hourly rate for pre-school childcare based on research by Ceeda (2014), including both free and subsidised hours, and assumes that working parents use on average 25 hours of care each week for 48 weeks of the year. Take-up figures reflect data from the *Study of Early Education and Development: Baseline survey of families* (Speight et al., 2015): 46% of one-year-olds and 69% of two-year-olds are in formal childcare among higher income households, which we use as a proxy for families where both parents are in work.

The second scenario factors in a further increase in funding to align staff wages in private and voluntary providers with those of the maintained sector, using average funding rates for maintained nursery schools. It also assumes that parents use on average 30 hours of care each week as take-up patterns change due to improved access and lower costs. The third scenario estimates costs following a ten per cent increase in parental employment and an increase in use to 35 hours each week. In each scenario, we estimate the parental contribution to the total cost of care assuming that on average the state would meet 57 per cent of the total cost of care. This estimate is based on a calculation of the percentage of fees met by parents under the proposed supply-side subsidy scheme (see Figure 29).

<u>Scenario one: High quality subsidy, current staff wages</u>

Age	Subsidised hours per year	Children in age cohort[19]	% with all parents employed[20]	Estimated take up	Cost per hour	Direct cost (£million)	Cost after parental contribution (£million)
One	1,200	723,260	50% (361,630)	50% (180,815)	£6.57	£1,426	£813
Two	630	683,303	53% (362,151)	70% (253,506)	£6.57	£1,791 (free early education) £1,050	 £598
Three	630	699,862	56% (391,922)	90% (352,730)	£5.47	£2,182 (free early education)	

						£1,216	£693
Four[21]	630	687,760	58% (135,626)	90% (122,063)	£5.47	£1,072 (free early education) £421	 £240
Total						£9,158	£7,389

Scenario two: Increased take-up and staff wages

Age	Subsidised hours per year	Children in age cohort	% with all parents employed	Estimated take up	Cost per hour[22]	Direct cost (£million)	Cost after parental contribution (£million)
One	1,440	723,260	50% (361,630)	50% (180,815)	£8.62	£2,244	£1,279
Two	870	683,303	53% (362,151)	70% (253,506)	£8.62	£2,350 (free early education) £1,901	 £1,084
Three	870	699,862	56% (391,922)	90% (352,730)	£7.18	£2,864 (free early education) £2,203	 £1,256
Four	870	687,760	58% (135,626)	90% (122,063)	£7.18	£1,407 (free early education) £762	 £435
Total						£13,731	£10,675

Scenario three: High take-up, 10 per cent rise in parental employment

Age	Subsidised hours per year	Children in age cohort	% with all parents employed	Estimated take up	Cost per hour	Direct cost (£million)	Cost after parental contribution (£million)
One	1,680	723,260	60% (433,956)	50% (216,978)	£8.62	£3,142	£1,791

Two	1110	683,303	63% (430,481)	70% (301,336)	£8.62	£2,350 (free early education) £2,883	 £1,643
Three	1110	699,862	66% (461,908)	90% (415,717)	£7.18	£2,864 (free early education) £3,313	 £1,889
Four	1110	687,760	68% (159,009)	90% (143,108)	£7.18	£1,407 (free early education) £1,141	 £650
Total						£17,100	£12,594

Notes

1 Detailed childcare spending figures for devolved nations are not available. To estimate current spending, we have adjusted spending in England for the population of each devolved nation. These figures are therefore an estimate of the funding available to each devolved government.

2 No account is taken of potential increases to early education funding following the present funding review and introduction of the National Living Wage. Spending figures are given for England (we assume that spending in UK-wide schemes broadly reflects the relative population of each nation). Comparable spending data for the devolved administrations is not available.

3 Research by the Institute for Public Policy Research suggests that the cost of extending free childcare to 30 hours each week for three- and four-year-olds with working parents will be significantly more expensive – by up to £800 million – than the government's published estimate of £650 million (Cory, 2015).

4 All figures from Households Below Average Income statistics 2012-13. Relative poverty is defined by the Act as earning less than 60 per cent of median income; severe poverty as less than 50 per cent of median income; and material deprivation is the self-reported inability of households to afford 'particular goods and activities that are typical in society'.

5 Assumptions for Figures 9 to 15: National Minimum Wage and Personal Allowance set at 2016 rates (£6.70 and £11,000). First earner working full-time. First child age one, second child age three and third child age five; 30 hours free early education included for three-year-old child; 10 per cent sibling discount applied to second (least expensive) child; five-year-old child assumed to be in school and using after school childcare during term-time and full-time childcare during holidays. Childcare cost data from Family and Childcare Trust Childcare Costs Survey 2015, using average UK costs. Universal Credit rates set at 2015/16 level (parents are assumed to be under 25), excluding work allowance which is set at £192. Minimum income standard threshold is indicated where possible using the Minimum Income Calculator. Each family receives the average UK local housing allowance (based on the maximum number of rooms allowable for the number of people in the family) and we assume that the allowance covers 100 per cent of rent. Housing Allowance rates from Valuation Office Agency Housing Allowance data as of January 2015. Child Benefit is included in each calculation.

6 Child tax credit capped at two children.

7 Disposable income is net income after housing costs (which affects the relative amount of disposable income for a couple in London). Same assumptions as for Figure 9.

8 Assumes 40 hours daycare for first child aged one, 25 hours daycare with 10 per cent sibling discount for second child, aged three, and daily after-school care for third child; costs data from Family and Childcare Trust *Childcare Costs Survey 2015.*

9 Assumptions as those for Figure 9.

10 HMRC provides data on the number of families with eligible childcare costs of over £180 each week. However, it is not possible using this data to distinguish families accessing support for one child from those accessing support for more than one child.

11 House of Commons Written Answer: HC Deb, 11 July 2013, c345W

12 Assumptions as those for Figure 9.

13 HC Deb 11 July 2013, vol 345W.

14 Assumptions as those for Figure 9.

15 Assumptions as those in Figure 9. Disposable income means net income after tax, national insurance and social security payments are taken into account after housing costs.

16 Assumptions as those for Figure 9.

17 Assumptions as those for Figure 9.

18 Detailed spending figures for devolved nations are not available. To estimate spending in the devolved nations, we have adjusted spending in England for the population of each devolved nation. These figures are therefore an estimate of 'available' spending, though devolved government may choose to spend more or less than this figure on childcare.

19 ONS population estimates for 2015/16.

20 Labour Force Survey.

21 Take up among four-year-olds is reduced to take account of the transition of four-year-olds into reception class.

22 Hourly costs in scenarios two and three are based on average hourly allocations to nursery schools for free early education (data from the Early Years Benchmarking Tool).

Acknowledgements

This report was commissioned to support the Joseph Rowntree Foundation's *Anti-poverty strategies for the UK* project and builds on an evidence review, *Early childhood education and care and poverty*, by Eva Lloyd and Sylvia Potter of the Cass School of Education at the University of East London (Lloyd and Potter, 2014).

The authors would like to thank in particular Katie Schmuecker and Helen Barnard at the Joseph Rowntree Foundation, and Eva Lloyd at the Cass School of Education, for their comments and feedback on drafts of this report. We are also grateful to the Joseph Rowntree Foundation's anti-poverty strategy advisory group for their helpful feedback on our proposals. We would like to particularly thank Duncan Lugton, who conducted a number of interviews and provided invaluable support during the project.

We would also like to thank the many people who agreed to be interviewed as part of the project or participated in roundtable seminars to discuss childcare and poverty, including: Peter Brant, Chris Barnham, Mike Brewer, Jonathan Clifton, Karen Cornish, John Davies, David Finch, Alison Garnham, Kayley Hignell, Aaron Hunter, Kayte Lawton, Neil Leitch, Marcia McHugh, Sarah Mulley, June O'Sullivan, Gillian Paull, Katy Pell, Neeraj Sharma, Jodie Smith, Helen Stephenson and Maggie Tierney.

We are grateful for the thoughtful and challenging responses to the question of how childcare can help to reduce poverty and many comments and ideas that helped to shape our proposals. There were many different and sometimes competing perspectives and the final report, of course, reflects the views of the authors.