World Class

What does international evidence tell us about improving quality, access and affordability in the English childcare market?

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Section 1: Introduction

Early childhood education and care services (ECEC) have a significant role to play in promoting more equal life chances for children. At their best, they can facilitate maternal employment, boost family income and improve women’s life-time earnings, while giving children exposure to new developmental experiences at a time when they are most receptive and curious. If provision is sufficiently high quality, there is evidence that it can have a lasting impact on children’s cognitive and social-behavioural development (Sylva et al. 2008; Sylva et al. 2011; Ruhm and Waldfogel 2012).

To achieve these dual goals of promoting maternal employment and improving children’s life chances, governments need to resolve the tensions inherent in the ‘childcare triangle’ of access, quality and affordability. They need to expand the number of places to allow more children access, ensure those places are affordable to parents, especially those on low incomes, and improve the quality of childcare to have a positive impact on child development. Addressing each side of this triangle was central to the 2004 childcare strategy and a decade on, resolving these same tensions remains the central policy challenge for childcare going forward. As political parties line up to invest additional resources in childcare, it is imperative to look at what reforms would simultaneously address each of the three sides of the triangle.

In England, making improvements to access, affordability and quality is made more complex by the wide variety of ECEC services on offer, with the range of settings available varying by the child’s age, by area, and by parents’ working hours. The way in which this diversity of provision has evolved in England presents four specific challenges:

- The stark variation in quality between sectors, driven by differences in staff qualifications (this variation currently works in favour of more disadvantaged children, but this may change with welfare reforms);
- The current divide between settings specialising in part-time and full-time provision, which has implications both for social segregation and for ensuring that early education works as a stepping stone rather than a barrier to employment;
- The risk with a large for-profit sector that additional state funding will simply boost profits unless there are sufficient strings attached;
- The issue of the sustainability of settings in poorer areas with fewer full-time working parents.

This complex picture is probably not where one would start if designing a system from scratch, and it certainly makes it more difficult to attack the three sides of the triangle than if the state provided all ECEC services directly. However, we are unlikely to rebuild the system completely and, therefore, need to look to improve it from where we are, working with the current diversity.

In relation to ECEC, as for many other services, government has three policy levers at its disposal. It can provide services directly; fund services provided by other sectors; and regulate the quality and conditions of provision. Here we look at how each of these levers can play a role individually, and together, to significantly improve childcare.

We take inspiration from the design of systems in other countries that also operate a mixed economy, including voluntary and private providers alongside state provision and therefore negotiating a similar level of complexity in how the levers of government operate. We specifically
look at Australia, France, Germany, the Netherlands, New Zealand, Norway and the USA. The paper draws on recent work with our colleague Jane Waldfogel and a team of international experts, in which we explore how effectively these countries have approached the childcare triangle, and particularly how well they do at providing access to quality provision for children from disadvantaged backgrounds (Gambaro et al 2014).\(^1\) None of the countries has found a magic solution to the three-sided dilemma but looking at the nuts and bolts of other systems reveals the strengths and weaknesses of the English system, offers new ideas and points to potential dangers.

By aligning the two levers – funding and regulation – government can address both quality and access against a backdrop of diversity, while maintaining the strengths of the English system in direct provision.

Our aim is not to call for simple policy transfers; policies are embedded in national contexts and reflect particular historical developments. Nevertheless, the experience of other countries highlights how we could improve (and damage) the childcare system we have without rebuilding it entirely. By aligning the two levers – funding and regulation – government can address both quality and access against a backdrop of diversity, while maintaining the strengths of the English system in direct provision.

This paper starts with a description of the childcare market in England, highlighting the differences in provision across the state, private and voluntary sectors. It then goes on to look in turn at each of the levers available to government: provision, funding and regulation, drawing on international experience to identify the strengths and weaknesses of how each lever is used in England. Finally, the paper puts forward a set of possible reforms to funding and regulation that together would improve quality and affordability, while protecting the access to childcare that has been achieved over the last decade.

\(^1\) Where assertions about different national systems are not referenced, they come from the relevant country chapter of our edited book, *An Equal Start?* (Gambaro et al, 2014). We gratefully acknowledge the work of Anne Lise Ellingsæter, Jeanne Fagnani, Yusuf Emre Akgündüz, Janneke Plantenga, Pamela Oberhuemer, Helen May, Deborah Brennan, Marianne Fenech, Katharine Magnuson, Jill Rutter and our co-editor Jane Waldfogel.
Section 2

The childcare market in England

Early education and childcare in England is provided by a variety of organisations: state maintained schools, private and voluntary settings and childminders. Encouraging a range of providers has been a deliberate strategy intended to foster choice for parents (DfE 2004) although in practice some settings only cater for particular age groups and not all are available in all areas. In particular, there is a distinction between the state’s key role in providing services directly for three and four year olds, and its far more limited role in direct provision for under-threes.

Schools in England cater for all children for a full school day from the September after they turn four (i.e. up to one year before compulsory school entry). In the year before that, around a third of children attend a maintained state nursery class or nursery school, usually part-time (three hours a day) (Gambaro et al 2013). These places are concentrated in inner city areas because of the historical legacy of local authority investment in nursery education in the 1960s and 1970s (Owen and Moss 1989).

In the rest of the country, and for all younger children, services are predominantly provided by the private and voluntary sectors, with a very small role for local authority run Children's Centres. When the entitlement to free early education for three- and four-year olds was introduced by the last Labour government, the expansion of places took place entirely in private and voluntary sector settings (Stewart 2013). In 2011 39 per cent of three-year-olds accessing free part-time hours were doing so in a private setting and 17 per cent in the voluntary sector, with 38 per cent in schools and fewer than 2 per cent in a local authority setting other than a school, such as a Children’s Centre (Gambaro et al 2013 Table A2). Beyond the free entitlement, explicit limits were placed on the state’s role in childcare provision by the 2006 Childcare Act, which made English local authorities childcare providers of last resort. They have a duty to ensure sufficient places for all children whose parents want them, but they should not provide the places directly unless no private or voluntary sector organisation is willing to do so. (This duty has had limited effect in practice. Six years after the Act was passed only 20 per cent of local authorities in England reported sufficient places for children under two (FCT 2013)).

Childminders have fallen slightly in number over the last fifteen years but continue to play an important role in providing wraparound care and care for younger children (Stewart 2013). A very small number of children (1 per cent) take up the free entitlement with a childminder (Gambaro et al 2013).

In theory, the advantage of having a mixed economy of provision with choice for parents is that competition will bid up quality. But it is difficult to find any evidence from either the UK or elsewhere that suggests this happens in practice. Most of the studies that specifically investigate this issue are from North America and find that quality is often worse in the for-profit sector (Blau and Currie 2006; Sosinsky et al 2007; Cleveland and Krashinsky 2009). Evidence from other countries, including Australia and the UK, is hampered by the fact that publicly available data do not distinguish between for-profit and non-profit settings, though a small study by Rush (2006) for Australia points to the importance of distinguishing within the for-profit sector, finding little difference in quality between community and independent centres, but markedly lower quality in corporate chains.

There are several reasons why the childcare market is rather different to the market for many other goods and even services. For one thing, not all families will have access to a choice of
setting, depending on their location. For another, it is difficult for parents to observe and judge the quality of a setting from the outside; an Ofsted rating is a crude measure that can quickly become outdated. On top of this, continuity of care is rightly valued, so parents are unlikely to move a child from a setting where they have settled unless there are serious concerns. Plantenga (2012) points to the high “status quo bias” in the Dutch childcare market, which she attributes in part to informational barriers and in part to parental loyalty to the relationships their children have established with adults and peers. For some combination of these reasons, quality improvements in for-profit settings appear to be driven by state regulation and requirements, rather than by the operation of market forces.

Without choice acting as a driver of quality, different types of childcare setting in England vary considerably when it comes to the quality of provision they offer. The most crucial difference relates to staff qualifications. Schools are staffed with qualified teachers and nursery nurses, while in private, voluntary and independent (PVI) settings qualification requirements are low: just 50 per cent of staff must hold a GCSE equivalent (level 2) qualification, with supervisory and management staff needing an A Level equivalent qualification (level 3). The presence of graduate workers is not required and graduates are scant, at around 4 per cent of the workforce, although there is considerable variation (Phillips et al 2010; Brind et al 2011; Gambaro 2012). Graduates are twice as common in local authority-run settings as in settings in either the private or voluntary sector (Gambaro et al 2013). Childminders must simply have completed an introductory course in home-based childcare, though those offering the entitlement must also be at least working towards a level 3 qualification.

Variations in qualifications between sectors translate into differences in staff-child ratios and funding levels. Nursery schools and nursery classes in primary schools have lower numbers of staff to children in recognition of their higher qualifications, with a ratio of 1:13 for three and four year olds, compared to 1:8 in PVI settings. They also receive greater per child funding which is significant in their ability to sustain better qualified staff. The NAO (2012) found that on average in 2010-11 nursery schools received £6.83 per child per hour and nursery classes (which benefit from overheads within primary schools) £3.97, compared to £3.77 in PVI settings. (These are averages; considerable variation exists between local authorities, as the NAO report discusses.)

Crucially, observational studies of quality, as measured by Environment Ratings Scales (ECERS and ITERS ratings), have found that schools offer higher quality provision than PVI settings for children aged three to five, although voluntary settings have made the largest improvements in the most recent years (Sylva et al 2004; Sylva et al 1999; Mathers et al 2007). This is very likely to be driven by differences in staff qualifications across settings. Recent studies indicate that having a graduate in the setting improves both the ECERS rating and the likelihood of achieving an ‘outstanding’ Ofsted grade (Mathers and Smees 2014; Gambaro et al 2013). A graduate presence seems to make a particularly important difference to the quality of provision for three and four year olds in settings with higher concentrations of children from disadvantaged backgrounds (Mathers and Smees 2014).

A final pertinent difference between settings relates to opening hours. Schools offer largely half day provision during the school year. Around 10 per cent of children in school nurseries attend for a full school day (Gambaro et al 2013) but this is something parents have little control over: it is not possible to request a longer day when needed. In contrast, many PVI settings are able to extend hours to cover a fuller working day, but not all of them offer the option of a part-time place. Despite the original policy intention, in many cases in PVI settings, the free entitlement comes only as part of a package of longer paid hours, so operates in effect as a reduction on fees.

Having described the childcare market and the significant differences between types of setting, we go on to look at the impact the state can have on access, affordability and quality through each of the levers at its disposal: provision, funding and regulation. We start with provision.
Section 3

Provision

While England has much less direct provision than other countries, for example France, state provision is one of the important strengths of the system in comparative perspective. Direct provision takes the form of primary and nursery schools as well as children’s centres.

Direct provision through primary and nursery schools carries several powerful advantages. First, the fact that all children are in school for a full day from the September after they turn four in England is remarkably egalitarian compared to the situation in several other countries, where school starts later and pre-school or kindergarten provision is less universal, such as Australia and the US. There is continuing controversy about whether such an early school starting age is optimal for all children (Sharp 2002; House 2011), despite the play-based and child-centred nature of the Foundation Stage curriculum. But from the perspective of narrowing inequality, having all children together in classes headed by a qualified teacher is a significant strength. The system also reduces the number of years for which parents face high childcare costs. Costs may be difficult to manage and high compared to other countries between the end of maternity leave and the start of reception, but they drop dramatically at that point.

Second, the fact that school provision for three-year-olds is concentrated in inner city areas means that these settings cater disproportionately for disadvantaged children, so the higher quality of school-based provision currently works (by historical accident) in favour of poorer children, as illustrated in Figure 1. No other country we looked at is successfully ensuring that a social gradient operates in the interests of more disadvantaged children. It should be pointed out, however, that recent welfare reforms in the UK are likely to change the geographical distribution of poverty, with lower-income families pushed out of city centres, and there is a risk that this advantage will be eroded.

The role of schools in the delivery of childcare also raises challenges and questions. The main issue is that the part-time, almost sessional, nature of provision for three- and younger four-year-olds can become a stumbling block to employment rather than a stepping stone. Relatedly, it can contribute to segregation between children of different backgrounds, as it is less attractive to parents who work than to those who do not. In contrast, all children in France attend state écoles maternelles from the age of three but the places are for the full school day so suit working and non-working parents alike. On the other hand, in the Netherlands, extreme segregation is observed between two to four year olds of non-working parents who attend voluntary sector part-time playgroups and the children of working parents in day nurseries offering longer hours.

An additional issue arises in relation to the suitability of schools to cater for younger age groups. There is currently some pressure on schools to expand to include two-year-olds eligible for free
Section 3: Provision

places, but there is also controversy about whether schools are the right place for this age group; certainly specific investment and refurbishment would be needed. In any case, given a rising birth rate, schools may struggle even to meet demand from three- and four-year-olds. France experimented with nursery school for two-year-olds and then faced capacity problems: in 2000 37 per cent of children aged between two and three were in écoles maternelles, but this figure dropped to 12 per cent by 2011 following a marked increase in fertility rates from 1999. In England, 96 per cent of two-year-olds taking up their free places in January 2014 were doing so in PVI settings with just 1 per cent in maintained nursery classes (DfE 2014).

Figure 1:
Percentage of children accessing the free entitlement in a setting with a specialised graduate by the area deprivation level of the child

10=most disadvantaged


Notes: Includes children born between September 2006 and December 2007 who were receiving the free entitlement in all types of provision in January 2011. Child’s area deprivation level is measured using IDACI scores, which give the percentage of children in poverty in the small area where the child lives.

One drawback of the fact that schools cater for so many three- and four-year-olds is the knock-on implication for the sustainability and cost of provision for younger children in PVI settings. PVI providers are restricted in the extent to which they can cross-subsidise places for children two and under (where more staff are required for a given number of children) with revenue from three- and four-year-olds. This is an issue that our comparison countries also face to some extent – only in Norway do kindergartens cater for all children from one to six without losing older children to other types of setting. But the comparatively early and universal school (or nursery school)
Emerging evidence indicates that funding cuts are affecting the quality of provision in children’s centres in England.

Starting age in England and France makes it particularly challenging, although France has the advantage of higher state subsidies and, therefore, costs to parents are lower.

The state’s other direct form of provision – children’s centres - play a small but important role in ECEC in England: small in number, but important because of the high quality of provision (House of Commons 2010; House of Commons 2013). In addition to childcare, children’s centres offer a variety of wider services that are valued by parents and play a key role in supporting and sustaining other providers such as voluntary settings and childminders. The children’s centre model is admired and emulated in other countries, including Germany and France. Interestingly, France is attempting to design childcare in their centres with enough spare capacity to enable parents to change their childcare arrangement without changing setting in order to improve flexibility and reduce the risk of segregation between settings.

However, emerging evidence indicates that funding cuts are affecting the quality of provision in children’s centres in England. Ofsted (2012) reports that childcare workers and qualified teachers are the centre staff most likely to have faced redundancy since cuts set in, while Goff et al (2013) point to effects on wider family services. In addition, the purpose of the centres is changing, with the Coalition Government placing an increased focus on targeting services on the most disadvantaged (DfE 2012; Goff et al 2013). While traditionally centres have not selected children for ECEC on the basis of family income, targeting may change this, potentially making provision more similar to the US Head Start model. Head Start only serves children from low-income families and has been criticised for the lack of a social mix as well as for uneven quality, including low staff qualifications (Barnett et al 2004).

Non-state provision of childcare

The size of the for-profit sector swamps provision by Children Centres. The existence of for-profits raises a question of principle with regard to the acceptability of profit making in provision of early education, given that it is not legal in compulsory education. We consider this beyond the scope of our paper and set it aside (but see Lloyd and Penn 2012). But their strong presence also raises at least two practical issues: the sustainability of settings in poorer areas where fewer parents work or earn high wages; and the danger that state funding will simply lead to higher profits if there are insufficient strings attached. A third issue is that for-profit providers can operate as a powerful lobby to resist quality improvements. For example, in Australia the private sector appears historically to have acted as a brake on campaigns to tighten regulations in the sector, though more recently stringent requirements regarding qualifications have been introduced despite the opposition of private interests.

Voluntary settings have improved in quality more than any other sector in England in the last 15 years (Mathers et al 2007), but they need to be sustained and supported. Here too current policies may undermine the progress made, in particular the loss of the Graduate Leader Fund, which supported settings to employ a graduate between 2008 and 2011 (building on the Transformation Fund which operated between 2006 and 2008), and the removal of funding for local authorities to offer ongoing support and professional development. Examples from other countries illustrate the need for state support for the voluntary sector. In Australia community nurseries diminished significantly once government funding vanished during the 1980s. Cleveland and Krashinsky (2009) show that, in Canada, non-profit providers are able to provide quality childcare only if they
receive sufficient subsidies (or donations), and operate in a market with enough demand. This suggests that in highly deprived areas, even the most well-intentioned voluntary providers will struggle to offer high quality provision while remaining financially sustainable.

Finally, the role of childminders in offering wrap-around care is crucial in a fragmented system, as well as offering an alternative to centre-based provision that is valued by some parents for babies and very young children. Local authorities have worked to increase the quality of childminding with childminding networks and professional development schemes that were usually based in children’s centres. These schemes are now being replaced by childminding agencies delivered by a range of providers, which could include schools and childcare centres.

The government consultation on childminding agencies presents them as a ‘one-stop shop’ where parents will be able to go to find a childminder, and childminders to seek business support, training and advice (DfE 2014b). But professionals in the sector have raised concerns that they could lower rather than improve standards of care (Gaunt 2014; Gordon-Smith 2014). The role of the local authority in accrediting childminders is being removed, and it is not clear how much contact and training childminders will be able to expect from their agency, or what will be available to childminders who do not join one. Meanwhile, evidence from the ongoing evaluation of children’s centres points to a fall in the number offering childminder drop-ins, which played a key role in connecting and supporting childminders (Goff et al 2013).

A promising alternative model of support for childminders comes from New Zealand. There, ‘home-based educators’ have to follow the curriculum – as they do in England – but are also supported by an early years teacher known as a coordinator. Coordinators visit home educators at least once a month and also organise group sessions for carers and children. Childminding networks in England worked in a similar fashion, with coordinators based in Children’s Centres. But the New Zealand model is more stringent in having qualified teachers as coordinators, and because participation is a condition of receiving any public funding. In contrast, joining a childminding network was only ever compulsory in England for childminders delivering the free entitlement, and this requirement has now been removed (DfE 2014b).

Another interesting example comes from France where assistant(e)s maternel(le)s (childminders) are the most common form of childcare for children under three. In France, too, childminders have been encouraged to participate in childminder centres, where they can meet other childminders and receive advice from a qualified child nurse while children play together. The French system is also noteworthy for being heavily subsidised with some control on pay: minimum pay for childminders is set at the national level, with the goal of making this a more attractive employment option.

There are some advantages but also clear challenges from the mix of provision we have in the UK. Drawing on the experience of other countries with similar levels of diversity and complexity has started to highlight ways in which we could improve (and damage) the system we have without rebuilding it entirely. Having looked at provision, we go on to consider the other two levers government has at its disposal to improve quality, affordability and access – funding and regulation.
Section 4

Funding

The system of funding for ECEC in England combines elements of demand-side and supply-side funding, making things inherently complicated for parents and providers (and indeed for analysts and policymakers). We focus here on each type of funding in turn, drawing on policy in other countries for comparison and inspiration.

It is important to note at the outset, though, that the distinction between the two types of funding is not always clear cut. Traditionally, the terms have captured a split between countries that directly fund public providers and countries that encourage a mixed economy of providers, channelling state subsidies via parents in the interests of choice and competition. Countries in the former group have tended to pay most attention to issues of quality and access, leading the OECD to conclude that supply side funding is most effective at achieving these goals (OECD 2006).

However, ECEC systems have become more hybrid over time, and many countries have forms of funding that blur the supply-side/demand-side boundary. For instance, in both Germany and Australia parents receive a voucher but nurseries cash it in, so the money follows the child, preserving parental choice, but goes directly to the provider (and can be adjusted for different child characteristics). Funding for the free entitlement in England operates in a very similar way though no voucher changes hands. The money goes directly to settings, so it is generally considered a supply side form of funding, but it is demand-led, linked to patterns of enrolment. In our view, the formal distinction between supply-side and demand-side sources is less important than the precise design of the funding mechanisms.

Demand-side funding

There are currently two elements of demand-side funding in the UK. Each element has problematic features, and each is being reformed but not necessarily in ways that will improve these features.

The childcare element of Working Tax Credit reimburses up to 70 per cent of costs for families on low incomes and working a qualifying number of hours. It is to be replaced shortly by the childcare element of Universal Credit (UC). For the least well off eligible families, this part of the system is generous: in 2012 a single parent on half the average wage paid only 1 per cent of net family income for two children in full time care, and a single parent on the average wage just 6 per cent (Alakeson and Hurrell 2012). However, parents must pay costs up-front and then claim reimbursement through procedures that can be cumbersome. In addition, the subsidy is conditional on working a certain number of hours (16 hours per week for all non-disabled parents living in the household), so if hours drop or a parent has a period between jobs, childcare is disrupted.

Under Universal Credit, the hours requirement will be removed and 85 per cent rather than 70 per cent support will be available from 2016. However, both parents (or a single parent) must still be in paid employment, and the subsidy will be removed one month after a period of work ends, so concerns remain for those in insecure or sporadic employment. Recent research by the Citizens Advice Bureau (2014) found most providers required at least a month’s notice to change arrangements, with higher quality providers much more likely to do so. A final issue with both the existing tax credit system and the UC proposal arises from the highly targeted design of the subsidy. The combination of generosity at
Section 4: Funding

the bottom and steep withdrawal rates has a negative effect on work incentives, especially for second earners looking to increase their hours (Alakeson and Hurrell, 2012).

For higher earners, there is much less support available, and costs faced by parents are high. Alakeson and Hurrell (2012) calculate that a couple in the UK on twice the average wage would have paid 30 per cent of their net income to have two children in full-time provision in 2012. The only demand-side support currently available to better off parents is employer-supported childcare vouchers (which can also be made available to parents receiving tax credits if employers choose). Under the childcare voucher scheme, parents working for participating employers can reduce their tax and National Insurance payments by up to £930 a year per parent.

From September 2015, employer vouchers are being replaced by a ‘tax-free childcare’ scheme under which the government will pay 20 per cent of childcare costs up to a maximum of £10,000 per child for parents not eligible for UC. The new scheme will spread state assistance with childcare costs to more parents, including those not currently benefiting from vouchers. But it breaks the last link between employers and childcare that allow some continental countries such as the Netherlands to draw additional funding into the ECEC system, and it is more regressive than the voucher system. The employer scheme is worth £930 a year to basic rate taxpayers spending at least £2,913 on childcare. To receive the same subsidy under the new scheme, a family would need to spend £4,650. A higher rate taxpayer could gain by £630 a year by spending £1,485 under the voucher scheme and will now need to spend £3,150 to gain by the same amount. The maximum subsidy will be higher than it is at present (up to £2,000 per child), but only for those who can afford to spend more (on more hours or higher quality).

A further concern is that there has been some suggestion – though no firm evidence – that demand-side subsidies to date have fuelled higher prices, such that the real value to parents has been lower than intended (Paull 2014; and see NATSEM 2014, who make this argument in relation to Australia). With few strings attached, the tax-free childcare scheme could have similar effects.

Getting more out of demand-side funding

Both the Netherlands and Australia operate demand-side subsidy systems that on the surface appear more effective than the English one, and we examine each in turn for potential lessons.

In the Netherlands, the demand-side subsidy is the main mechanism for childcare funding. Importantly, only working parents are eligible, as employers make a substantial contribution, covering one third of parents’ out of pocket expenses. Parents are left to pay either the remaining 66 per cent, if they are on a high income, or as little as 3.5 per cent on a low income; thus the maximum level of support is more generous and the rate of withdrawal less steep than in the British case. Prices are not directly regulated, but parents cannot be reimbursed above €6.36 per hour and providers appear to set fees taking this cap into account. Hence there is effectively a price cap in operation, and the subsidies have not simply led to price inflation. This is perhaps the key lesson from the Netherlands for the UK, where caps on the demand-side have been on total childcare spending rather than spending per hour. The per child, per hour funding for the free entitlement in England (see supply-side funding section) fails to perform the function of a price cap because the free hours are effectively subsidised by the additional hours parents use. A weakness, however, of the Dutch system is that there is no link between the level of the subsidy and the quality of provision, and no additional funding for quality. We return to this below.

In Australia, the federal government directly subsidises parents who use approved childcare services, including long day care centres, family day care and outside school hours care, while state governments channel supply-side funding to providers of pre-school services (which are generally part-time). There are two federal subsidies available to parents: Child Care Benefit (CCB) and Child Care Rebate (CCR). CCB is means-tested and available to parents irrespective of working status, although non-working parents can only have 24 hours a week reimbursed
Childcare funding in Australia

There are two federal subsidies available to parents: Child Care Benefit and Child Care Rebate.

Child Care Benefit is based on family income, with the maximum rate payable to those on income under $41,902 (£23,300), tapering to zero when family income reaches $145,642 (£81,000) a year (one child) or $150,914 (£84,000) (two children) (with a higher payment for additional children). At the time of writing, payment is capped at AUD$3.99 per hour (£2.22), or AUD$199.50 per week, which leaves parents to pay what is referred to as a “gap fee” – the difference between the actual fee and the benefit. However, parents on Income Support (for example) receive further assistance, contributing just AUD$1 an hour. CCB payment rates are adjusted every year in line with the Consumer Price Index, but its value has eroded because fees have increased at a higher rate than the CPI (ECA 2014).

The Child Care Rebate is available only to working families, but is not income tested, so families who may not be eligible for CCB may receive CCR, while most families are entitled to both. Like CCB, CCR can be paid directly to providers either fortnightly or weekly as soon as the provider sends the child’s attendance information through an online portal, so parents do not need to pay and then reclaim.

Aside from shifting the administrative burden from parents to providers, the main advantage of this system over the tax-free childcare scheme being introduced in the UK is that it is more generous, covering 50 per cent rather than 20 per cent of costs. It is also less regressive because it covers a higher share of costs up to a lower cap, so is less favourable to high-income families using high-cost, long-hours childcare. As Figure 2 shows, demand-side funding in Australia succeeds in keeping childcare spending down below 10 per cent of family income right across the distribution. However, like the UK system the scheme creates an incentive for providers to increase fees, and they appear to have done so (see NATSEM 2014).

### Table: Childcare funding in Australia

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Interestingly, there have been recent calls for reforms to the Australian funding system, with proposals by Deborah Brennan and Elizabeth Adamson endorsed by Early Childhood Australia (Hurst 2014). Brennan and Adamson suggest merging the two subsidies into a single payment, the Early Learning Subsidy (ELS). This would cover a proportion of service fees up to a capped hourly rate. Rather than using an arbitrary figure uprated annually, as for CCB, the maximum ELS hourly rate would reflect reasonable costs of delivering a high quality service. ELS would be designed to cover essential cost elements such as salaries, to meet national quality guidelines, and legitimate variable costs such as rent, administrative costs, and “fair” surplus or profit (Brennan and Adamson 2014, p. 44). The base rate for ELS would be between 35% and 50% of reasonably priced ECEC, but it would increase to cover 90% of reasonable fees for low-income families. Families on welfare would have the entire costs of childcare covered. These changes would be aimed at simplifying the system while ensuring (through the hourly cap fee) that subsidies do not simply fuel growth in fees.

Neither Australia nor the Netherlands represent good role models on quality. Demand-side subsidies are generally not well-designed to encourage or enable investment in quality improvements, so they need to be coupled with separate sources of funding for this which neither the Netherlands nor Australia have introduced. The best example here may be the defunct English
Graduate Leader Fund. The North Carolina ‘Child Care WAGE$®’ project, which provides funding for salary supplements to workers who have progressed towards higher qualifications, aimed at increasing training, retention and compensation, is another interesting example.

Figure 2:
Out of pocket costs for one child in long day care before and after Australian Government subsidies, March Q 2012

Supply-side funding

There are two types of supply-side funding in England. First, a number of small but significant funding streams existed under the previous administration that we might call ‘pure’ supply-side funding: funding that was channelled to local authorities and on to providers without direct ties to the pattern of service use. Most of these sources have now been withdrawn, though some such support for local authority children’s centres continues. This type of supply-side funding is tiny within the overall landscape but vital in ensuring sustainability of provision in disadvantaged areas.

The second type of funding, that for the free entitlement for two-, three- and four-year-olds, we might call supply-side but demand-led: the money follows the child but bypasses parents and is channelled directly to providers. Funding for the free entitlement operates essentially as a flat per child rate, with a higher rate for two-year-olds. There are two possibilities to consider that would develop the design of this funding in a progressive way – a version of one of which is currently on the table in England. We draw on examples from Germany, New Zealand and the
US for comparison. We go on to consider possibilities for extending supply-side funding to the non-free parts of the system (younger children and additional hours beyond the entitlement, for whom state support in England is currently channelled via parents, as discussed). For ideas we examine how things work in Germany, Norway and France.

**Getting more out of supply-side funding**

One weakness of the flat rate funding system to date is that it does not vary with the level of disadvantage of the intake, though the costs of providing a quality service to disadvantaged children appear to be higher, and the added value of quality is greater (Gambaro et al. 2013; Mathers and Smee 2014). Local authorities in England can include a supplement for disadvantage in their allocation for the free entitlement, but few do so (or if they do the extra is just a few pence) as they receive no compensating funding from central government.

Under a new proposal put forward by the Coalition Government in 2014, an Early Years Pupil Premium will provide additional funding for disadvantaged children accessing the entitlement. Children from families eligible for free school meals, looked after children and adopted children will each qualify for an additional £300 per year, or 53 pence per hour, on top of an average hourly total projected by the Institute for Fiscal Studies for 2015-16 to be £4.52 for 3 year olds and £5.57 for 2 year olds (DfE 2014a, Brewer et al. 2014). This extends the principle of the current Pupil Premium funding for compulsory schooling, though the premium is considerably higher for primary school children at an extra £1,300 per child from 2014-15.

German Länder currently use supply-side funding formulae that differentiate across children from different backgrounds and with different needs. In some cases these are similar in principle to the pupil premium idea, with flat rate reimbursement rates supplemented for specific groups of children. In Bavaria, for example, there is a base rate that applies to children from three up to school entry (1.0), with additional funding for children under three (2.0), school-age children (1.2), children with disabilities (4.5), and children whose parents are both of non-German speaking origin (1.3). It is interesting to note that the difference in funding for children under and over three is much greater in Bavaria than in England (double in Bavaria; one quarter higher in England), and the boost for disadvantage is also proportionately greater (30% higher for a non-German speaker, compared to 10-12% higher for children qualifying for the Early Years Pupil Premium in England).

A different approach, operating in other German states such as Berlin, is to use a flat funding formula with additional funding for nurseries with a particularly disadvantaged intake. For example, a nursery with more than 40% of children from migrant families will get extra funding to reduce ratios or to provide language support. We return to this idea shortly.

The second main weakness with supply-side funding in England is that it is not well-structured to support investment in quality. The flat-rate system makes it difficult (even impossible) for settings to choose to take on more highly qualified staff. Local authorities can only increase resources to some settings by reducing them elsewhere, while most parents either cannot afford to pay more or do not see the value in doing so. The near absence of a socio-economic gradient in qualification levels in the PVI sector is an illustration of this (Gambaro et al. 2013), and it is also a pattern seen in the Netherlands where parental choice in a market-based system has not resulted in better-off parents paying more for higher quality.

The US and New Zealand offer alternative examples of how to adjust funding to support and incentivise quality. In the US, federal money is used to create a quality competition across states. For example, the Race to the Top—Early Learning Challenge (RTT-ELC) is a discretionary grant for which states can apply. They have to submit a plan to build state-wide systems that raise the quality of Early Learning and Development Programs and increase access to high-quality programs for children with high needs. If they win, they get a sizeable pot of money; around $50
million was awarded to each of six states in 2013, with $1 billion allocated in grants in total since 2011 (US Department of Education 2013). This may not be a model that translates easily to England because of the far more limited autonomy of local authorities compared to states in the US.

A further issue is that RTT-ELC is based on Tiered Quality Rating and Improving Systems (TQRIS) which consists of six performance metrics, with two relating to staff training. The closest equivalent in England to TQRIS would be Ofsted scores, but research suggests that Ofsted scores are higher, other things being equal, where there are fewer children from disadvantaged backgrounds in the classroom (Gambaro et al 2013), so using Ofsted to allocate funding could be a regressive move. There are also concerns about how effectively Ofsted scores capture all aspects of quality. Mathers et al (2012) point to a fairly weak correlation between Ofsted scores and the widely respected ECERS and ITERS ratings, especially for children under three. For both these reasons focusing extra quality payments on staff qualifications seems a more promising and enabling strategy.

It is also worth considering whether the role of supply side (demand led) funding could be expanded to subsidise additional hours, in place of the current demand-side system aged two and above, but the quality bands apply to both age groups, and there is widespread acceptance that it is valuable for provision for young children too to be staffed by trained teachers. A similar system would be straightforward to introduce in England. At its simplest, settings could simply be reimbursed for the extra cost of employing a graduate or qualified teacher, for example, and bands could also operate in relation to the proportion of staff with level 3 qualifications. This would require additional funding overall, not just a redistribution of existing resources.

There is also a case for combining premia for disadvantage and quality. For example, given evidence that graduates raise the quality of ECEC provision, with particularly large effects on disadvantaged children (Mathers and Smees 2014), it may make more sense to use pupil premium money to increase staff qualifications than to give it to providers to spend as they wish. Rather than giving a small amount of extra money for each child meeting particular criteria, pupil premium money could be concentrated (at least initially) on settings with high numbers of disadvantaged children (as in the Berlin model), but earmarked specifically for more qualified staff. For example, settings with 40 per cent of children meeting the criteria could be given the resources to hire a graduate.

The scope for longer term supply-side reform

So far we have discussed ways in which funding for the free entitlement could be improved to make it more sensitive to children’s disadvantage and provide more possibility and incentive to improve quality. It is also worth considering whether the role of supply side (demand led) funding could be expanded to subsidise additional hours, in place of the current demand-side system. Both Norway and France channel all state funding through supply side subsidies. In both countries a system of scaled fees is in operation, with families contributing according to income and settings compensated accordingly.

In France, the administration of income-related fees is relatively straightforward, as most of the crèches are currently public and run by the local network of CAF (Caisses des allocations
World Class: What does international evidence tell us about improving the English childcare market?

Section 4: Funding

In Norway, on the other hand, almost half of the kindergartens are run independently from local authorities, and a system of income-related fees still operates, although not perfectly. In 2011 only 53 per cent of all children enrolled were in kindergartens using income-related fees, but among the municipalities that had not established such arrangement, 60 per cent offered a social assistance scheme whereby fees are waived for families whose income is below a certain threshold. Fees are capped nationally, with an annual debate in parliament on the level of the cap, so there is no possibility for kindergartens to charge high-income parents a fee above this level. This cap combined with the fact that income-related bands are not universal means that low-income families tend to spend twice or three times more of their income on childcare than higher income families. This may not be a problem in a country such as Norway, with low income inequality and overall high income, but may result in a steeper gradient in accessing ECEC in countries with higher inequalities.

In Germany, a system of income-related co-payment operates for provision not covered by free hours. (The number of free hours varies substantially between Länder in both starting age – two or three – and in the number of hours, with Berlin offering 7 hours per day from age three, but most states fewer). Whatever the exact design, an important aspect of the German model is that local authorities are heavily involved in the administration of funding. Parents must submit a tax declaration form from the previous year to the local authority and this is used to determine the level of co-payment, which is then paid directly by the parent to the provider. The provider then receives the rest of the subsidy from the local authority.

This is not impossible to envisage in England, where central government funding of the entitlement is administered via local authorities and local authorities are responsible for checking eligibility for the two-year-old offer. Also, Children’s Centres generally charge income-based fees, which require some form of income assessment. The role of local authorities could be expanded to administer additional government funds and even to collect parents’ co-payments, as they do currently in social care. This way individual providers would not have to charge parents directly or to assess their income. But Germany has many voluntary sector providers and no for-profit ones. It is more difficult to see how it might work in the English context of a large for-profit sector, whose existence depends precisely on their charging strategy.
Section 5

Regulation

The final lever available to government to improve childcare is regulation. All countries regulate quality in similar ways: by setting requirements for staff qualifications and ratios, by having a curriculum, and by a system of monitoring. However, the design and overall balance in the use of these levers varies greatly. Furthermore, some countries regulate aspects of provision that are left untouched in England: wages and profits (Norway) and social mix (France).

Curriculum

Overall, the curriculum in England seems to be a success. Play-based and child-centred, the Early Years Foundation Stage curriculum has the additional strength of covering the whole age span from zero to five, including childminder provision; this is unusual, innovative and brings unity to the sector. However, the Tickell Review (2011) raised questions about whether the curriculum could be delivered effectively without a more highly qualified workforce. There is a parallel here with New Zealand, where the ambition of a workforce entirely composed of qualified teachers grew out of the child-centred nature of their own early years curriculum.

Staff qualifications

In England, requirements on staff qualifications are lower than in most countries discussed here, with the exception of school nursery settings. The emphasis for promoting quality lies more heavily on staff to child ratios, the curriculum, and the inspection system. The weakness in regard to staff qualifications is twofold: a scarcity of graduate professionals in the PVI sector, and the poor vocational qualification system. In comparison, while the Netherlands and Germany perform at least as badly in relation to graduates, vocational training appears to be stronger and more solid. Ideally, England should act to improve both (as indeed was recommended by the Nutbrown Review in 2012): to develop vocational training, while also providing routes into more academic graduate level degrees. This would in turn require much stronger coordination between training providers to establish a single qualifications framework and avoid the proliferation of weak qualifications which are the hallmark of the ECEC sector today.

A clearer training framework would also facilitate a closer link between qualifications, occupational titles and, consequently, pay. In Germany, for example, a more regulated labour market and a stronger vocational education system create a closer match between occupational titles and qualifications attained. There are three occupational groups, each corresponding to a specific training programme and qualification (Oberhuemer et al 2010; OECD 2006). In order to work as a Kindermiester, one has to successfully complete two years of vocational training at a Fachschule (similar to a further education college). The title of Erzieher, instead, requires the completion of a two- or three-year programme at a Fachhochschule (broadly equivalent to a higher education college or ex-polytechnic). Finally, one can become a Sozialpädagog upon completing a bachelors degree in Social Pedagogy. Pay is set accordingly, thus creating a clear financial incentive to obtain further training.

By contrast, in England, wages are fairly flat: workers with higher qualifications accrue very little financial advantage. Of course, adequate resources and appropriate funding mechanisms are
key part of the story here: as argued above, flat rate funding schemes leave very little incentive for settings (and therefore individuals) to invest in further training.

Ratios

England’s relatively favourable ratios have led to controversial proposals, now shelved, to relax requirements, with the Government putting forward examples from other countries in support of their case, including France which has recently increased ratios for childminders (DfE 2013). In fact, ratios in England are not as unusual as is sometimes suggested. In Norway, for example, the actual practice is one employee for 3.4 children, fairly similar to England, and the Norwegian government is proposing a change to 1:3 for children under three (as in England), but with one graduate to every six. In New Zealand there is also movement in favour of tightening ratios up. Where change is in the other direction, as in France, it is clear that the intent is to expand provision rather than improving quality. In the context of high turnover, poor pay and low qualifications, relaxing ratios is only likely to damage quality.

The role of Ofsted

To some extent Ofsted inspections can be considered a strength of the English system, providing transparent and accessible quality checks on all ECEC services that is absent in many other countries. On the other hand, there are risks in relying overwhelmingly on the professional judgements of one or two inspectors who visit a setting for one day and whose qualifications and experience are not always clear. Indeed the recruitment and training of inspectors is not managed directly by Ofsted, which has outsourced the early years inspectorate since 2010. While inspectorates for schools and children’s services will be brought back in house after 2015, in order to ensure greater coherence and quality of inspections (McCardle 2014), there is no plan for a similar move in relation to early years. In relation to nursery education in the maintained sector, there is also the problem that no separate judgement is currently provided for early years provision within schools, though this is currently out to consultation.

However, perhaps the biggest risk lies in the recent shift towards reliance on Ofsted as the sole arbiter of quality. There are two concerns here. First, the poor correlation between Ofsted scores and other measures of quality, especially for children under three, shows that a single judgement can be a blunt reflection of what is happening within a setting; a wider range of quality measures is valuable (Mathers et al 2012). Second, a three-yearly inspection visit is no substitute for continuing professional support and development. Local authorities were playing a key role in providing this on-going support, and the removal of their responsibility (and funding) in this regard represents a significant and worrying development. It puts England out of step with several other countries including Norway, France and Germany where municipalities or départements (in the case of France) play an important role in sustaining and improving provision.

New areas for regulation

Lastly, some countries regulate aspects of provision not considered above. In France, social mix is itself considered an aspect of quality, which is centrally regulated. This sort of regulation is important if children benefit from being in a mixed environment because of peer effects, or if a
Section 5: Regulation

concentration of children from disadvantaged backgrounds makes it more difficult for staff to provide high quality ECEC. There is growing evidence that both issues are relevant (e.g. Shager 2012; Ebert et al 2013; Mathers and Smees 2014), but there is little attempt in England currently to monitor the extent of concentration, and little thought about how different policies might influence it.

In Norway, regulation covers both wages and profits. Kindergartens can receive state subsidies only if they operate no more than ‘reasonable’ profits, and profits are not considered reasonable if the wage share is lower than in municipal-run kindergartens. Given Ofsted infrastructure, it would not be difficult to regulate these aspects of provision in England if we chose to do so. Interestingly, Birmingham Council has recently said that only settings that pay the Living Wage can offer the entitlement; funding has not increased and many cannot afford to pay that, so providers are appealing against the Council decision. This is an interesting example both of the importance of providing adequate funding for required quality improvements – and also of the tricky balance involved in regulating providers from for-profit settings.
Section 6

Next steps

The system of ECEC provision in England has a number of relative strengths, many of them stemming from direct state provision. A universal reception class, part-time nursery classes staffed by qualified teachers and covering many of the more disadvantaged children, and Children’s Centre provision (albeit small in scale and under threat) are among these strengths. The Early Years Foundation Stage curriculum and a strong inspection system through Ofsted are also valuable aspects of the system.

The major weaknesses are the quality of provision outside the state sector and the high price to parents of ECEC beyond the entitlement. The flat per child funding of the free entitlement does not offer scope to adequately support more disadvantaged children (though this is set to partially change) nor does it allow for investments in quality. Demand side subsidies are intended to increase affordability, currently focusing mostly on lower-income households. But the new tax-free scheme expands support for higher earners in a way that is regressive, with most funding going to those who spend more in total, and with no additional support for quality improvement.

As additional challenges we would highlight the current divide between settings specialising in part-time and full-time provision, which has implications both for social segregation and for ensuring that early education places can be effective stepping stones to employment; concern that state funding may in part be leaking out as higher profits in the private sector; and concern about the sustainability of ECEC settings in poorer areas.

Despite the strengths of direct state provision, a mixed economy is likely to be an ongoing feature of the ECEC landscape in England. The experience of other countries suggests ways in which the weaknesses and challenges identified in this paper can be addressed against a backdrop of diversity. There are several promising ideas thrown up by the experience of other countries that can inform how we reform the childcare market in England to enable higher quality and improve affordability, while not reducing access, especially for children from disadvantaged backgrounds.

By using funding and regulation more effectively, and in particular by improving the way they operate together, it should be possible to improve the system’s ability to address the three sides of the childcare triangle without tearing things up and starting again. We set out, then, some recommendations for improving both supply-side and demand-side subsidies, as well as additional recommendations for further promoting quality through regulation.

Supply side funding through the entitlement:

» Funding for the entitlement should be better designed both to reflect children’s disadvantage and to support investment in quality, drawing on examples from Germany and New Zealand. The Early Years Pupil Premium is a step in the right direction, but is small in scale, and the funding should come with tighter strings attached to ensure investment in quality. Rather than spreading the money thinly with a per child formula, it would be more effective to focus the premium, in the first instance, on enabling settings with a high number of disadvantaged children to invest in more highly qualified staff.

Demand-side subsidies to improve affordability:

» Demand-side subsidies operate more effectively where there is a cap on reimbursement per hour (as in the Netherlands and as proposed for Australia) rather than an overall
reimbursement cap. This appears to help prevent subsidies leading to fee inflation.

» Subsidies that cover a higher proportion of costs up to a lower cap (as in Australia) are more progressive than those covering a relatively low proportion up to a higher cap (as in the tax-free childcare scheme).

» Allowing parental subsidies to be paid directly to providers (also as in Australia), for example through a voucher, rather than requiring parents to claim a reimbursement, can reduce pressure on parents. This would be similar to the free entitlement except parents would be expected to pay the difference between the voucher and the price.

» Demand-side subsidies do not themselves enable investment in quality, so there need to be separate supply-side resources for this, such as the former Graduate Leader Fund, and/or the North Carolina ‘Child Care WAGES®’ model.

Continuing to provide ‘pure’ supply-side subsidies to support the wider childcare infrastructure:

» Children’s Centres and the voluntary sector play an important role in providing ECEC for working parents in poorer areas and a system of supply side funding outside the entitlement (not tied to patterns of usage) is essential to making this possible. This funding is under threat and needs to remain on a stable footing.

» Childminders are likely to remain an important part of the system for younger children and as wraparound care. They could be more firmly supported through compulsory inclusion in networks with a trained early years teacher as co-ordinator (as in New Zealand).

» The local authority role in providing on-going support and professional development is crucial, distinct from that of Ofsted three-yearly inspection visits, and should be restored.

Regulation:

» There is a very strong argument for tighter controls on settings that receive state funding (this also applies to supply side subsidies). These should certainly include tougher requirements on staff qualifications (following the requirements of the Nutbrown Review, and following a feasible timetable). In addition, it would be worth considering regulations on wages and profits (as in Norway); and perhaps on social mix, as in France.

In the longer term, a question remains about the relative merits of supply-side and demand-side subsidies. If we decided to shift to a stronger reliance on supply-side support, the most straightforward route would be to replace current demand-side subsidies with a more generous free entitlement, perhaps with extra hours restricted to those in work, as Labour has proposed with its expansion to 25 hours (with some generosity to protect continuity of care when there are breaks in employment). To some extent, this is an extreme version of the Australian idea of generous reimbursement (sent direct to providers) up to a lower limit (in this case, 100% of costs covered up to a certain number of hours). This is attractive in its simplicity to both parents and providers, and would reduce the issues of social segregation and employment barriers currently associated with the part-time places, as well as the work disincentives inherent to tightly means-tested support. These are persuasive arguments, and expanding the entitlement hours for three- and four-year-olds might be a neat and feasible policy.

But for an expanded entitlement to replace targeted assistance entirely it would also have to stretch down to babyhood, and providing sufficient hours for all children of working parents...
would surely come at unacceptable cost to government. An alternative would be to channel all funding on the supply side while operating a system of income-related fees for parental contributions. This works in France, Norway and Germany and is worthy of further consideration in England too, though it would be a new departure to make it work in the context of a large for-profit sector and it would need careful thought in relation to childminder provision too. It is possible that a more effectively designed demand-side subsidy could achieve the same ends.

The recommendations put forward here are suggestions for ways forward and not costed proposals. It is our view that substantial increased investment in the sector is essential for serious improvement in the qualifications of the ECEC workforce, alongside noticeable improvements in affordability for parents. At the same time, however, there are a number of ways in which existing money could be spent more wisely and effectively. Better design and integration of funding and regulation mechanisms should deliver some benefits at little additional cost.
Section 7

Conclusion

Considerable progress has been made in expanding access to early education and childcare over the last decade. One million new places have been created and the near universal take up of the free entitlement for three and four year olds is a remarkable achievement, ensuring that those families who were least likely to use ECEC services now have access. However, not enough progress has been made in improving the quality of provision, with the risk that the beneficial impacts of our investment on child development will not be realised.

In the run up to the next election, it is critical that further attention is paid to ensuring that the investment we are making in childcare delivers for children as well as for working parents. We need to focus on improving quality at the same time as affordability and access, and work with the mixed economy we have. It is tempting to argue for different choices to have been made a decade ago but in reality, we are unlikely to remake the system we have from scratch.

Looking at the way in which other countries with similarly mixed systems of ECEC negotiate the tensions inherent in the childcare triangle reveals the need to shift towards a system of funding and support that requires more in return for the receipt of public funding and simultaneously offers more support for providers to meet these new requirements. Public funding should come with ‘strings attached,’ notably around improvements in staff qualifications, but the state will have to invest to ensure that the sector can raise its game for the benefit of children and families.
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