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Productivity Commission's Child Care Report: An Alternative Perspective

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The Productivity Commission's recent report, *A Path to Universal Early Childhood Education and Care*, presents a wealth of information and references many relevant studies. But its recommendations are questionable due to weaknesses in its analytical framework. An alternative approach could lead to different conclusions, particularly regarding the need for further childcare subsidies.

Issues with the Commission's approach

Some limitations in the Commission's approach stem from the Government's terms of reference. But we should expect more from the Commission given its important role in providing expert economic analysis.

1. Dual objectives of Early Childhood Education and Care (ECEC)

The Commission does not fully address the two objectives implied by the terms of reference: that ECEC is both 'an essential part of Australia's education system' and 'a powerful lever for increasing workforce participation'. A robust analysis would treat these as separate goals, likely requiring distinct policy tools (following the 'Tinbergen rule').

2. Overemphasis on Workforce Participation

The Commission seems to assume that increasing workforce participation is an inherently good economic goal. But participation is often a personal choice: some individuals choose early retirement, voluntary work, or reduced paid work to spend more time with their children. Economists and feminists alike have long recognised that GDP does not account for unpaid work, much of which is done by women - such as childcare, household responsibilities, and community volunteering.

A better approach would focus on creating opportunities for parents of young children to engage in paid work if they choose to, supporting parental choice in care arrangements, and addressing career penalties for those who take extended time away from full-time work. These issues are only briefly discussed in the report (for example in Box 1 on page 10), and even the more detailed labour force participation analysis in Volume 2's supporting paper 4 ('ECEC and labour force participation') appears to overstate the benefits of further increasing workforce participation among parents (mainly mothers) of young children.

3. Limited Exploration of Existing Policy Tools

The report does not adequately consider other government policies related to workforce participation, such as paid parental leave, parenting payments, and Family Tax Benefit Part B. Although these are mentioned in the supporting paper in Volume 2, the report does not explore ways to modify these existing programs.

4. Underestimating Costs

Finally, the report appears surprisingly sanguine about the costs of its recommendations.

Early Childhood Education

The report and related papers highlight substantial evidence of the long-term benefits of pre-school education delivered by education professionals, particularly for four-year-olds and to some extent for children as young as two. However, it remains unclear whether children under two benefit similarly or what the optimal hours of education are for older preschoolers. Generally, the states provide around 15 hours of preschool education for four-year olds, while fewer hours might be appropriate for younger children. Yet, the report only emphasises the need for 'high-quality' services without exploring these specific considerations.

Defining and measuring 'quality' in early childhood education is recognised as complex, though research consistently shows that quality is crucial, especially for disadvantaged children, and largely depends on the nature of children's interactions with educators and teachers.

The most efficient way to deliver early childhood education likely involves both preschools attached to primary schools and qualified educators within formal daycare services. However, the report does not clearly distinguish between educational services in daycare and general care. Instead, it simply underscores the need for educators and early childhood teachers in daycare settings.

This lack of clarity mirrors the current National Quality Framework and National Quality Standards (NQS), which already blend educational and general care standards. In Volume 2's first supporting paper, the Commission briefly references this framework but could have done more to differentiate standards specifically for education and for general care. Two of the NQS fields - focused on educational programs and staffing arrangements, including child-to-educator ratios and qualifications - relate primarily to education, while the other five address general care, especially safety and governance.

A clearer breakdown of these standards could have helped the Commission identify the most effective and efficient ways to deliver necessary education and determine where additional funding is warranted. This analysis might have further supported the recommendation for increased funding for education of disadvantaged children between the ages two and five.

There is a strong case for making early childhood education universally accessible and free. The case for universal, free childcare is less clear. Rather than distinguishing between these components, however, the Commission simply proposes higher childcare subsidies, with a more generous means test.

Alternative approaches that could achieve universal and free high-quality early education include:

- **Direct employment by State and Territory governments:** State and Territory governments could directly employ educators in both preschools and childcare centres to deliver age-appropriate education based on evidence.
- **Targeted subsidies for qualified staff:** A universal subsidy model could support centres in employing qualified staff, with funding adjusted based on the ages of children and the necessary hours of education.

Childcare Policy: Rethinking Support for Young Children's Care Needs

A more fundamental review of childcare policy would begin by clarifying the level of care children of different ages require. Although I am no expert, I suggest the following is likely agreed upon by most:

- **Babies** typically need full-time, individual care from an adult (sometimes even more support).
- **Toddlers (up to age two)** generally still require one-on-one full-time care.
- **Preschoolers (ages two to five)** can often be cared for in small groups for part of the day.
- **Primary school-aged children** receive care at school during school hours, with after-school care often needing fewer adults per child than care for younger children.

Currently, the policies and programs supporting childcare are complex. Here is a simplified breakdown of the support provided by the Commonwealth for two-parent families with one child, in line with these age-based care needs:

1. Babies

- Paid parental leave subsidises one parent to stay home full-time for about five months (six starting next year) at minimum wage (currently about $900 weekly).

2. Children under two

- There is no unique support specifically for this age and the various forms and levels of support provided for preschoolers set out below apply.
- For those utilising childcare, the subsidies for toddlers often understate the total support because of cross-subsidies from families with preschoolers which cover the higher staff-to-child ratios toddlers require.

3. Preschoolers

- Some low-income families with a child under six may qualify for a parenting payment of up to $350 per week, though it is tightly income-tested for both parents so mostly only paid to families with one parent not in the paid workforce.
- Families with a child under five and only one working parent may receive FTB Part B, with a less restrictive income test. This support is up to around $190 every fortnight.
- The childcare subsidy provides fee relief of up to 90% for families utilising centre-based or family daycare, capped at $600 per week for young children receiving 50 hours of care. Most families receive around 70% of the standard fee and most use less than 50 hours of care (for 25 hours of care, the maximum subsidy is around $300 a week). The subsidy is means-tested, and actual charges are often higher than the capped amount. Families choosing informal care, such as grandparents, generally receive no subsidy.

4. Primary school-aged children

- FTB Part B reduces to a maximum of around $130 per fortnight for single-income families, and only sole parents may receive a parenting payment.
- After-school childcare may attract fee relief, but fewer hours of support are provided (e.g. the subsidy is up to $175 per week for 15 hours of care). Again, no subsidy is available for informal care by family members.

The report does not examine these varied supports in detail, focusing mainly on the childcare subsidy. It recommends increasing fee relief (up to 100%), slightly relaxing the means test, and removing the activity test, which ties subsidy hours to hours worked or similar activities.

Simplifying the childcare subsidy would be helpful, especially by removing the activity test as suggested. However, even greater benefits would come from streamlining all support for the care of young children and their multiple complex rules. Such a simplification would acknowledge that families face real costs, whether they pay for childcare directly or forgo income to care for their children themselves.

To truly support employment access and allow choice in care arrangements, an ideal approach might involve payments based primarily on the age of the youngest child, starting at the current paid parental leave level for babies, then gradually decreasing as the child ages:

- **Babies:** Support at parental leave rates.
- **Under two:** Slightly reduced support.
- **Ages two to five:** More substantial drop in support.
- **Ages five to thirteen:** Additional reduction.

This structure would however, create large gains and losses compared to current programs, suggesting a need for political compromise. Families with children under two who provide most of the care themselves would benefit most, while families of older children relying heavily on childcare might receive less. This shift could impact work incentives, as discussed below, and might warrant adjustment.

Such an arrangement might not achieve the political appeal of 'cheaper childcare' but would still involve extensive support for most families with young children. Childcare fees would also be offset by the separate educational support provided. Overall, it would present a fairer, more consistent approach, recognising the real costs of raising young children and sharing them across society. This approach would leave parents with more balanced options for childcare arrangements and workforce participation.

Workforce Disincentives: Impact of Women's Labour Force Participation and Policy Considerations

Women's workforce participation has risen substantially over the last fifty years, reflecting individual preferences and broader social shifts[1]. While the traditional 'M-curve' in women's workforce participation by age has diminished, it still persists for most mothers. Typically, women's workforce participation climbs with age until childbirth, at which point participation declines sharply. Following this, participation increases in a staggered way, initially through part-time work in most cases and then more full-time work as children reach primary school age. Participation rates then gradually decrease in women's fifties and sixties, generally more rapidly than for men. Although higher education levels and evolving career aspirations may continue to erode this M-curve, such changes are likely to remain marginal, given the demands of parenting.

Volume 2 highlights that means tests on transfer payments, combined with the structure of personal income tax, are more significant drivers of high workforce disincentive rates, or effective marginal tax rates (EMTRs) than the childcare subsidy means test (though it still imposes a higher EMTR than the nominal sliding reduction of fee relief might indicate). Many families face EMTRs exceeding 50% over broad income ranges due to the interaction between FTB Part A income testing and personal income tax, impacting not only parents of young children but also those with older children. This situation suggests a stronger case for reinstating a more universal basic family allowance rather than further relaxing the already generous means testing of childcare. Additionally, adjusting FTB Part A payments in line with wages, as recommended by the Henry Review over a decade ago, would also address this challenge more effectively than indexing to prices.

A payment structure based solely on the child's age, as previously suggested, would reduce the financial returns from increased paid work. Parents choosing to work or expand their hours would bear the full childcare fees, alongside personal income tax and any reductions in FTB Part A. Removing cross-subsidies that benefit families with very young children (under two) by charging families with older children would reduce childcare costs for those with children aged two and above but would raise them for those with children under two.

While this setup might feel more transparent by showing the real costs of childcare, whether through lost income or paid fees, it could also necessitate some childcare fee relief to counteract disincentives to work, although probably not as much as is now provided let alone the increases the Commission recommends.

Instead of boosting childcare subsidies, an alternative approach would involve reducing the long-term career costs associated with taking time away from full-time work for parenting. This challenge, which is fundamentally about equal employment opportunities (EEO), could benefit from more in-depth analysis by

[1] Fifty years ago, I contributed to the groundbreaking Social Welfare Commission report on childcare, which influenced the Whitlam Government's decision to initiate Commonwealth support for childcare. This decision sparked an enormous expansion in the availability of both family daycare and formal childcare over the following decades.

the Productivity Commission, as such policies could address gender disparities in career advancement without imposing additional financial burdens on families.

Supply-side risks

A system focused more on cash subsidies and family choice would not need to assume fully competitive, market-driven childcare services. Instead, it would still need close regulation to ensure quality and safety. As Professor Deborah Brennan, Chair of the PC, points out in Volume 2 of the report, relying more on not-for-profit organisations (and government agencies) to manage childcare could reduce risks and increase benefits compared to a system dominated by for-profit providers. A first step toward this model could involve having State and Territory education departments oversee professional training in childcare centres.

Conclusion

A more in-depth analysis of the two main goals of the early childhood education and care (ECEC) sector might have led the Commission to consider a broader range of recommendations or at least different priorities.

Such an analysis could highlight specific steps to enhance preschool education based on clear evidence of the benefits, ensuring free and universal access with direct government provision. Separately, it might prompt rethinking the support for young children's care, enhancing family choice and opportunities for paid work. If moving to a simpler system of age-based payments is too challenging, then some smaller but impactful changes should be prioritised over increased childcare subsidies, such as:

- Greater support for families with a parent who chooses to reduce their paid work hours, particularly those with very young children;
- Making the basic family allowance (FTB Part A) more universally available and more generous;
- Exploring ways to minimise long-term career impacts for those who reduce workforce participation to care for young children.

Given these priorities, budget consideration would seem to rule against the Commission’s recommendations of completely free childcare.