

## 6. ECEC affordability

### Key points

- ✳ **Out-of-pocket expenses are a key determinant of whether families can afford early childhood education and care (ECEC). The Child Care Subsidy (CCS, including the Higher CCS (HCCS)) and the Additional Child Care Subsidy (ACCS) reduce out-of-pocket expenses for families, but those on lower incomes spend a higher proportion of their income on ECEC compared with those who are better off.**
  - The families whose incomes are in the bottom 10% of the income distribution pay out-of-pocket expenses equal to about 9% of their income on average. In contrast, families whose incomes are in the top 10% of the income distribution pay about 5% on average.
- ✳ **Aspects of CCS design can discourage ECEC participation by families.**
  - The activity test creates a barrier to participation for some children and it is unclear if the requirement that parents or guardians engage in activities like work or training to access subsidised ECEC has had any effect on labour force participation.
  - The 6% of families who were eligible for 24 or 36 hours of subsidised ECEC a fortnight in 2021-22 tended to have lower incomes and about two-thirds were charged for at least some unsubsidised hours of care.
  - The effectiveness of the CCS hourly rate caps in reducing out-of-pocket expenses is muted if families face fees above the cap. Between 2018 and 2022, the share of centre-based day care and family day care services with average fees above the CCS hourly rate cap nearly doubled from 13% to 22% and 24% to 45%, respectively. The combined effect of automatic indexation of the cap and increased subsidies (which occurred from July 2023) on affordability are not yet clear.
  - Information available to families when they are working out their CCS entitlement can be confusing and create substantial uncertainty as to their entitlements. Navigating this complexity can be much more difficult for those with low levels of English and / or computer literacy. For some families, this level of complexity creates a substantial barrier to ECEC access, and in some cases, means they choose not to access ECEC.
- ✳ **Relaxing the activity test for all families and lifting subsidies for low-income families would target support to children and families who would benefit the most. Alongside improving availability, inclusion and flexibility, these changes to the CCS would enable universal access to ECEC.**
  - Implementing these changes is estimated to increase: hours of ECEC used by 12%; hours of work by 3.4% (or the equivalent of 20,700 full-time workers); and Australian Government outlays on the CCS by 20% or \$2.5 billion per year.
  - Over half of the resulting increase in CCS expenditure would benefit the 20% of families on the lowest incomes.

**\* Broad-based CCS changes would make ECEC more affordable for all families but come at a substantial cost to taxpayers.**

- If in addition to relaxing the activity test and increasing the CCS rate for lower-income families, the Australian Government were to extend a subsidy rate of 90% of the fee, up to the hourly rate cap, to all families for three days of ECEC a week, it is estimated that total hours of ECEC used would increase by 21%; hours of work by 5.7% (or the equivalent of 34,900 full-time workers); and Australian Government outlays on the CCS by 53% or \$6.8 billion per year.
- Policy options extending the 90% subsidy rate to all ECEC users or introducing a flat fee of \$10 a day have similar implications for labour force participation, demand for ECEC and net costs to government.
- A disproportionate share of the increased government support would go to high-income families – rather than to those experiencing disadvantage, who are most likely to benefit from greater access to ECEC.

**\* Low-income families would not benefit if the only change to the CCS were a 90% subsidy rate for all families because they are already eligible for a 90% subsidy. However, a universal 90% subsidy rate would bring ECEC closer to the funding principle that underpins some aspects of Medicare.**

- This policy change is estimated to increase: total hours of ECEC used by 7.4%; hours of work by 2.8% (or the equivalent of 17,000 full-time workers); and Australian Government outlays on the CCS by 33% or \$4.1 billion per year.
- Nearly 60% of the increase in government outlays would accrue to the 20% of families on the highest incomes (those earning \$200,000 per year and above) and nearly 30% to the second highest 20% (those earning between about \$150,000 and \$200,000 per year).

**\* The Australian Government should ensure that the complexity of ECEC subsidy arrangements is not a barrier to access for families.**

- Options to make information provided on government websites about CCS eligibility easy to find and easy to understand by families should be explored.
- Functionality of the CCS calculator on the Starting Blocks website should be improved.
- Single Touch Payroll information from the Australian Tax Office should be used to prompt families to update their activity and income level details with Services Australia.
- Clear and easy to find information should be provided to families about the CCS withholding rate during the CCS application process and when families update their details with Services Australia.

Early childhood education and care (ECEC) promotes social and economic benefits such as child development and parents' labour force participation (particularly for secondary earners who are usually women), and a key element of whether a child participates is whether their family can afford ECEC.

This paper examines the affordability of ECEC.

- Section 6.1 discusses characteristics of the main government programs that provide support to families in covering their ECEC expenses.
- Section 6.2 considers the effectiveness of these programs at improving affordability for families and the extent to which families may still face financial barriers to ECEC participation.
- Section 6.3 focuses on changes to subsidy arrangements that would improve affordability as well as the effectiveness of subsidies to improve affordability.

## 6.1 How do governments provide support for families in covering ECEC expenses?

### Out-of-pocket expenses are the key determinant of affordability

For families with children attending formal ECEC (except preschool), out-of-pocket expenses depend on the fees they are charged and the amount of subsidy they receive. Fees are set by ECEC services. Subsidies depend on a family's characteristics, in tandem with the subsidy rates and eligibility criteria set by the Australian government. Two key Australian government programs deliver subsidies to families – the Child Care Subsidy (CCS) (which includes the Higher CCS (HCCS) for families with multiple children) and the Additional Child Care Subsidy (ACCS).

For families with children in the year before school, out-of-pocket expenses may be reduced further compared to other below school age groups because these children are eligible to attend a preschool program for which further funding is provided by both the Australian and state and territory governments. Preschool affordability is discussed below.

### A brief overview of the CCS and ACCS

In 2023-24, the subsidy amount that families are eligible for is a function of:

- an activity test – the level and type of recognised activity undertaken by parents or guardians determines the number of care hours that a family is eligible for to be subsidised by the CCS (in general, higher activity levels lead to higher eligible subsidised care hours)
- a family's income – for incomes up to \$80,000 per year, families are eligible for a 90% CCS rate, with the rate tapering down by 1% for every \$5,000 of income above \$80,000, reaching 0% at \$530,000
- whether the hourly fee for ECEC is above or below the CCS hourly rate cap – if the hourly fee is above the cap, the CCS rate is applied to the cap amount and the remaining fee must be paid for by the family. If the hourly fee is equal to or below the cap, the CCS rate is applied to the full fee.

Under the HCCS, families earning up to \$138,118 per year are eligible for a 95% CCS rate for second and subsequent children with the rate tapering down as a family's income increases.

The ACCS provides extra assistance to families who face additional barriers to accessing ECEC, through higher subsidy rates (generally 100% of fees if below or equal to the rate cap or up to 120% of the hourly rate cap if fees are above the rate cap) and a higher number of subsidised ECEC hours (generally 100 hours per fortnight).<sup>1</sup> There are four categories of ACCS.

- ACCS (Child Wellbeing) – for families caring for a child at risk of serious harm, abuse or neglect (Services Australia 2021).
- ACCS (Grandparent) – for grandparents on income support who are the principal carers of their grandchild(ren) (Services Australia 2022e).
- ACCS (Temporary Financial Hardship) – for families experiencing temporary financial hardship due to an event that happened in the preceding six months (Services Australia 2023a).
- ACCS (Transition to Work) – for families transitioning to work from income support (Services Australia 2023b).

Detailed information on the CCS, HCCS and ACCS is in appendix D.

<sup>1</sup> The exception to these conditions is ACCS (Transition to Work), where 95% of fees are subsidised if fees are below or equal to the rate cap or up to 95% of the hourly rate cap if the fee is above the rate cap, and the eligible subsidised hours depend on a family's activity level.

## CCS has a marked effect on out-of-pocket expenses

Many families have ECEC subsidised through CCS. In the December 2022 quarter, 1.4 million children attended a CCS-approved service<sup>2</sup> and of these children, 93% received subsidised ECEC (Productivity Commission estimates based on DoE administrative data (unpublished)).

Out-of-pocket expenses are typically significantly lower than the fees charged by services (table 6.1). Across a financial year, families pay out-of-pocket expenses with some CCS withheld.<sup>3</sup> Out-of-pocket expenses are slightly lower when calculated simply as the charged fee less subsidy, assuming that families will receive their CCS withholding amount at the end of the financial year. In this paper, out-of-pocket expenses are typically calculated this way.

One reason for the divergence in fees and out-of-pocket expenses between service types is differences in the number of hours typically charged to families. For example, fees and out-of-pocket expenses are lower for outside school hours care (OSHC) because primary school aged children spend less time in formal ECEC. In addition, OSHC fees are charged per session, and a child may attend two sessions per day – before and after school.

**Table 6.1 – Subsidies reduce out-of-pocket expenses<sup>a,b,c</sup>**

**Average fees and out-of-pocket expenses (with and without CCS withholding), by service type, December quarter 2022**

	Per hour			Per day (CBDC and FDC) or per session (OSHC)			
	Mean fee	Mean OOP	Mean OOP (CCS withheld)	Mean fee	Mean OOP	Mean OOP (CCS withheld)	Mean daily charged hours
<b>CBDC</b>	\$11.80	\$4.40	\$4.77	\$123.72	\$46.02	\$49.90	10.5
<b>FDC</b>	\$11.93	\$3.79	\$4.20	\$92.68	\$29.32	\$32.50	7.8
<b>OSHC</b>	\$8.81	\$4.08	\$4.31	\$30.68	\$14.00	\$14.84	3.7

**a.** Mean calculations are based off week summaries ending Sunday. **b.** This analysis excludes cases where out-of-pocket expenses were zero. **c.** CCS: Child Care Subsidy; CBDC: centre-based day care; FDC: family day care; OSHC: outside school hours care; OOP: out-of-pocket expense.

Source: Productivity Commission estimates based on DoE administrative data (unpublished).

Analysis of Department of Education administrative data showed that out-of-pocket ECEC expenses make up a higher proportion of disposable income for families in the first income decile (figure 6.1). The families whose incomes are in the bottom 10% of the income distribution pay out-of-pocket expenses equal to about 9% of their income on average. In contrast, families whose incomes are in the top 10% of the income distribution pay about 5% on average. The Australian Competition and Consumer Commission (ACCC) found a similar pattern in their Childcare inquiry June 2023 interim report (ACCC 2023a, p. 15). Families

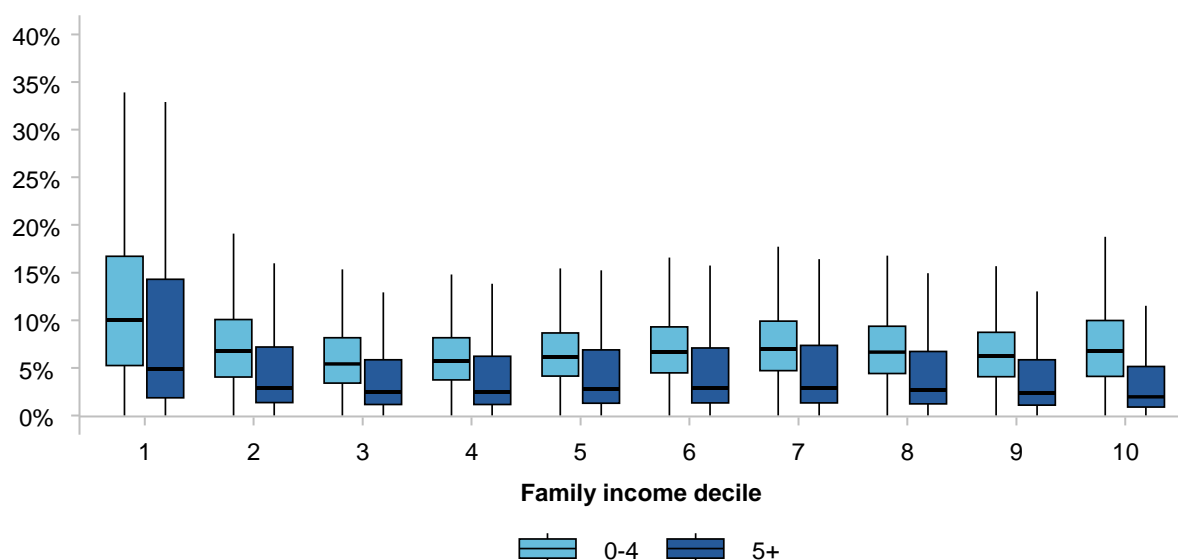
<sup>2</sup> For a provider to run a service that offers CCS, it must have two types of approval. One is by the relevant state or territory government which deems the service suitable to ensure the health, safety, wellbeing and educational outcomes of children. It is granted by the relevant state or territory regulatory authority and is known as National Law approval or state regulatory approval. The second type of approval is by the Australian Government which deems the service suitable to administer CCS. This is known as CCS approval or Family Assistance Law approval and it cannot be granted until state or territory government approval has been granted. Both approvals can be applied for at the same time (DoE 2023a). For the following discussion on CCS, 'services' refers to CCS-approved services unless otherwise stated.

<sup>3</sup> By default, 5% of a family's CCS entitlement for each week is withheld until the end of the financial year to reduce the potential for CCS debt. Discussion of CCS withholding is in appendix D.

where the youngest child is of before school age spend a higher proportion of their disposable income on ECEC compared to families where the youngest child is of school age (figure 6.1).

**Figure 6.1 – Families with before school-aged children spend a larger share of their disposable income on ECEC<sup>a,b</sup>**

**Out-of-pocket expenses as a share of family after-tax income, by age of youngest child in ECEC and family income decile, fortnight to 27 Nov 2022**



**a.** Subsidies for the out-of-pocket expense calculation are calculated as the CCS plus the ACCS. The out-of-pocket expense accounts for fees that might be paid above the hourly rate cap. After tax household income calculated by applying tax rates to customer and partner reported incomes. Excludes In Home Care services. **b.** These box and whisker plots show the median (black horizontal line), two hinges at the 25<sup>th</sup> and 75<sup>th</sup> percentiles (top and bottom box edges), and two whiskers extending to the values no further than 1.5 times the interquartile range from the hinges. Outliers are omitted.

Source: Productivity Commission estimates based on DoE administrative data (unpublished).



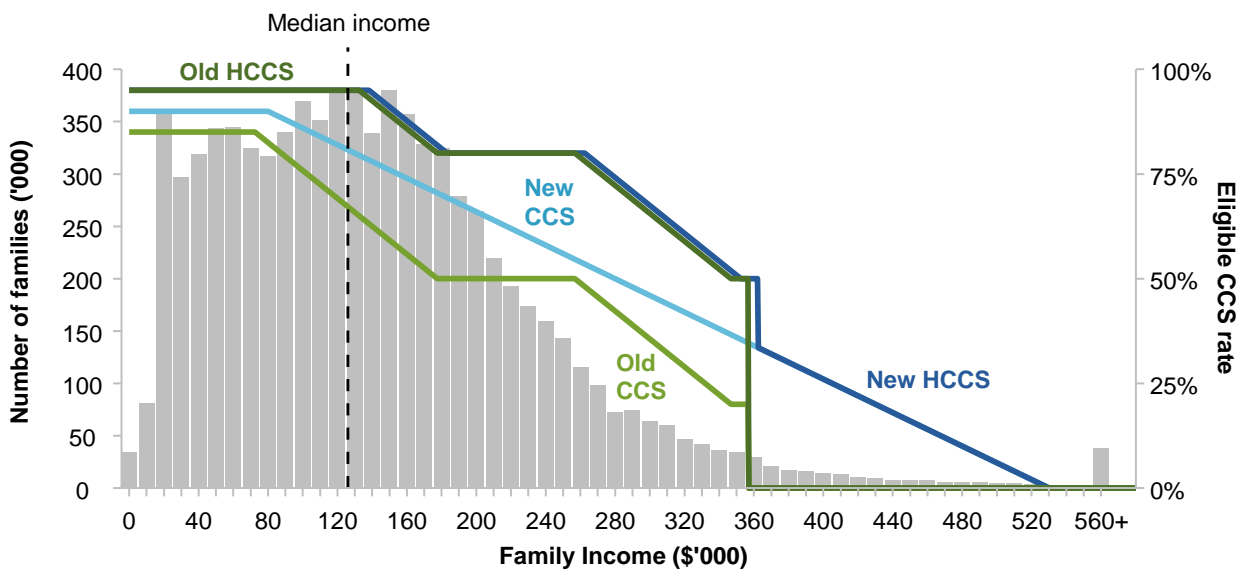
**Draft finding 6.1**  
**ECEC is less affordable for lower-income families**

The Child Care Subsidy lowers out-of-pocket expenses for families, but those on lower incomes spend a higher proportion of their income on ECEC compared with those who are better off. The families whose incomes are in the lowest 10% of the income distribution pay out-of-pocket expenses equal to about 9% of their income on average. In contrast, families whose incomes are in the highest 10% of the income distribution pay about 5% on average.

**Recent CCS reforms are expected to reduce out-of-pocket expenses for families ...**

Reforms to CCS that began on 10 July 2023 increased subsidy rates, and it was anticipated that the proportion of families receiving a CCS rate of at least 70% would increase from about half to about 70% (figure 6.2). Box 6.1 provides an example of how recent CCS reforms have affected out-of-pocket expenses.

**Figure 6.2 – About 70% of families have a CCS rate of at least 70% from 10 July 2023<sup>a</sup> 2023-24 and 2022-23 subsidy rates and number of families receiving CCS for the week to 26 June 2022, by family income**



a. The black dotted line represents median family income.

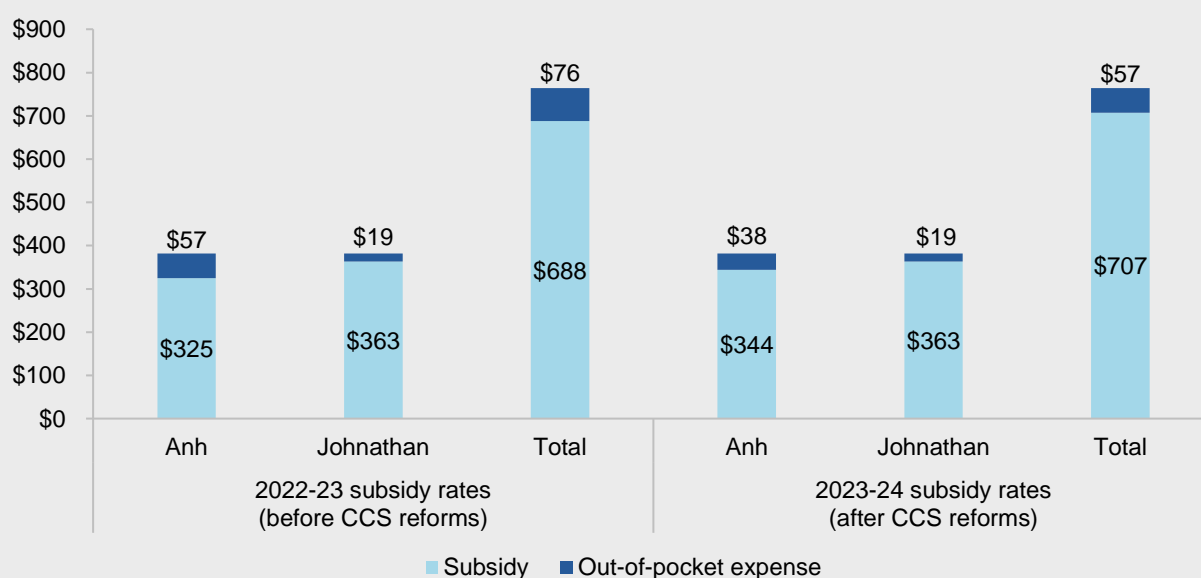
Source: Productivity Commission estimates based on DoE administrative data (unpublished).

### Box 6.1 – Illustration of the effects of recent Child Care Subsidy reforms on out-of-pocket expenses

Recent Child Care Subsidy (CCS) reforms reduce out-of-pocket expenses for families. Consider a family with a taxable income of \$60,000 and two children, Anh (aged three) and Johnathan (aged two). Both children attend a centre-based day care (CBDC) for three days a week. The parents meet the activity test and thus all hours attended at the CBDC are subsidised. CCS rates would apply for Anh and the Higher Child Care Subsidy (HCCS) rates would apply for Johnathan. The CCS reform would reduce this family's out-of-pocket expenses from \$76 to \$57 per week (figure below) if fees remained unchanged.

#### Families receive higher amounts of CCS from 10 July 2023<sup>a</sup>

#### Family with \$60,000 annual income and two children in CBDC, 2022-23 and 2023-24 subsidy rates, weekly expenses



a. These hypothetical scenarios assumes an annual family income of \$60,000 and that the two children attend CBDC for three 10-hour days each week. Johnathan is assumed to be the second child that received the HCCS. The hourly fee is assumed to be at the 2022-23 CCS hourly cap rate of \$12.74.

Source: Productivity Commission estimates.

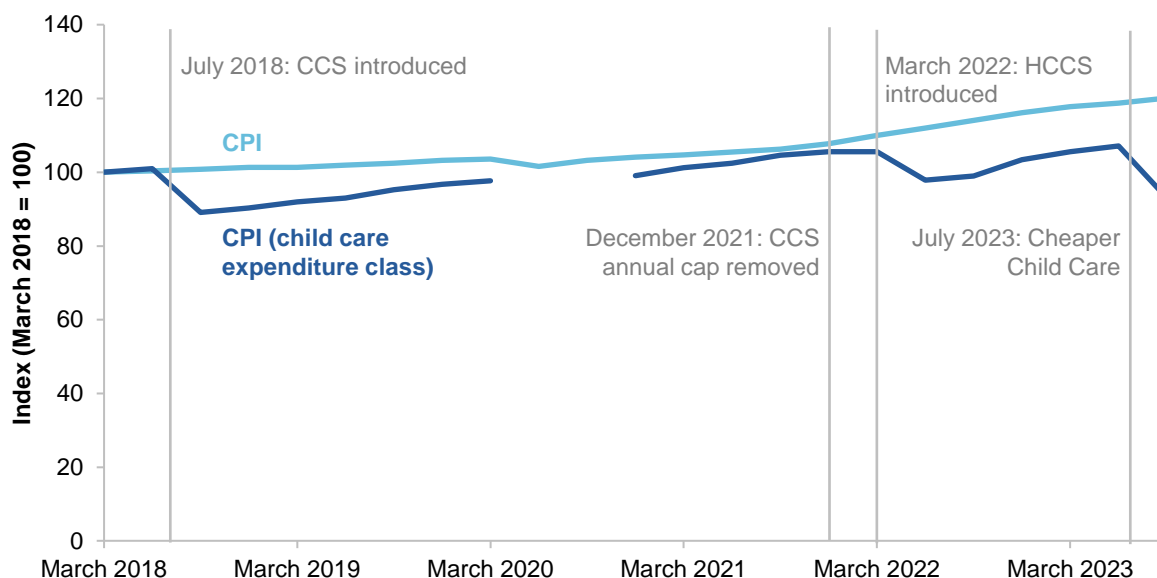
### ... however, the effectiveness of subsidy increases may be muted by fee growth

Fee rises can reduce the effectiveness of subsidy increases in reducing out-of-pocket expenses for families.

Since 2018, unlike overall inflation, out-of-pocket ECEC expenses have fallen (figure 6.3). The main reasons for this are the increased subsidies provided to families through the introduction of the CCS on 2 July 2018 (Parliamentary Library 2019), removal of the CCS annual cap on 10 December 2021, introduction of the HCCS on 7 March 2022 (Hume 2021) and the July 2023 Cheaper Child Care policy changes. Without the increase in subsidies, it is likely out-of-pocket expenses would have increased faster than CPI because of fee growth.

**Figure 6.3 – Since 2018, out-of-pocket ECEC expenses have fallen whereas the overall level of consumer prices has increased<sup>a</sup>**

**Quarterly index of child care CPI and CPI, March 2018 to September 2023**



a. Data for June and September quarter 2020 is excluded due to the impact of COVID-19 on out-of-pocket expenses.

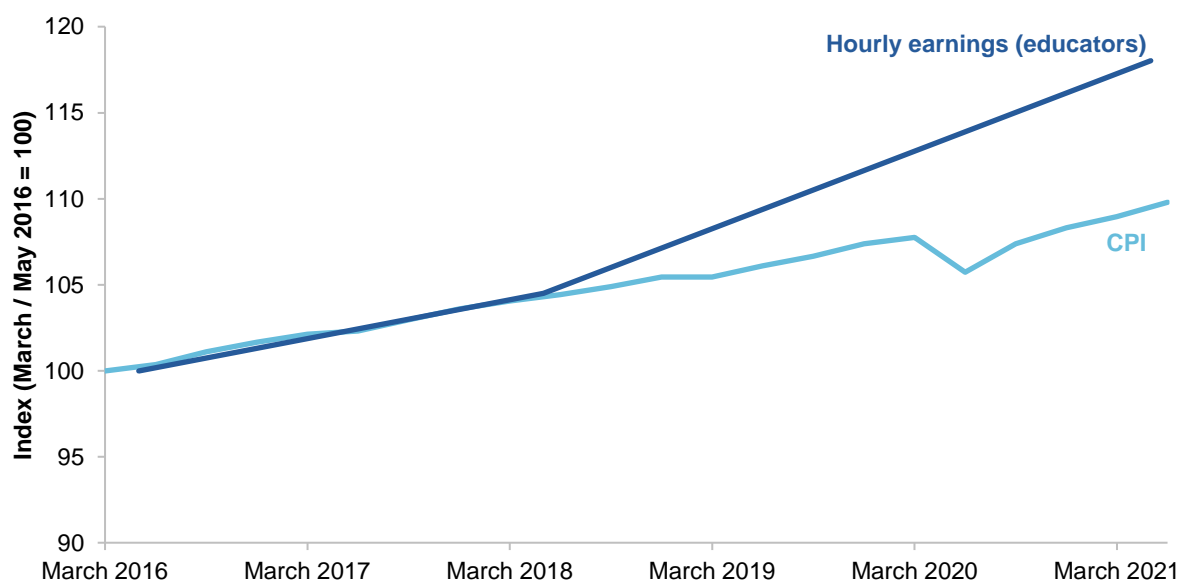
Source: Productivity Commission estimates based on ABS (September 2023) 'Table 7: CPI: group, sub-group and expenditure class, weighted average of eight capital cities' [time series spreadsheet], *Consumer Price Index, Australia*, accessed 30 October 2023.

The growth in fees is unsurprising given that increases in the hourly earnings of full-time educators have outstripped CPI growth in recent years (figure 6.4) and that labour is the largest cost for ECEC services. Labour costs account for 69% of costs for centre-based day care (CBDC) services and 77% of costs for OSHCs (ACCC 2023b, p. 43). The average costs for large CBDC providers grew 27% between 2018 and 2022 with average labour costs growing by 28% for that same period (ACCC 2023b, p. 50). For large providers of OSHC, average cost increases were in line with inflation between 2018 and 2022 with average labour costs growing by 7% (ACCC 2023b, p. 51). For large CBDC providers, finance and administration costs represent 9% of total costs and have increased in real terms between 2018 and 2022, reflecting greater 'investment, acquisition and debt' in the sector since 2020 (ACCC 2023b, p. 53).



### Figure 6.4 – Between 2018 and 2021, hourly earnings of full-time educators grew more quickly than CPI<sup>a,b,c</sup>

CPI and index of average hourly total cash earnings for full-time non-managerial child carers (ANZSCO minor group 421), March 2016 to June 2021



**a.** CPI data is released quarterly in March, June, September and December. **b.** Hours and earnings data is released biannually in May, with a three year gap between 2018 and 2021 due to COVID-19. Hourly earnings data is only available from 2016. **c.** Hourly earnings data only covers full-time employees. Part-time and casual employees may be expected to have higher hourly earnings on average, for example, due to casual loadings. This means that this data may underestimate hourly earnings for the entire population of educators.

Source: Productivity Commission estimates based on ABS (September 2023) 'Table 7: CPI: group, sub-group and expenditure class, weighted average of eight capital cities' [time series spreadsheet], *Consumer Price Index, Australia*, accessed 30 October 2023 and ABS (May 2021) 'Data cube 13. Full-time non-managerial employees paid at the adult rate' [data set], *Employee Earnings and Hours*, accessed 31 October 2023 (and previous releases).

### Any difference between hours charged and hours attended may also affect affordability

Total fees, subsidies and out-of-pocket expenses are based on the hours charged by a service. For many families, there is a difference between the hours for which they are charged and the hours that their child attends a service. For example, a service may only offer 10-hour sessions between 8am and 6pm, but a family may drop their child off at 8am and pick them up at 2pm. In this situation, the family will be charged for, and CCS will be applied to, all ten hours despite the child only attending 60% of the session. Families can also be charged for days where their child is absent.

Across a year, families only attend about 60% of the hours for which they are charged, and attendance rates are relatively similar across eligible subsidised hours thresholds<sup>4</sup> and income deciles. Attendance rates tend to be higher when a family pays for some unsubsidised hours<sup>5</sup> (figures 6.5 and 6.6).

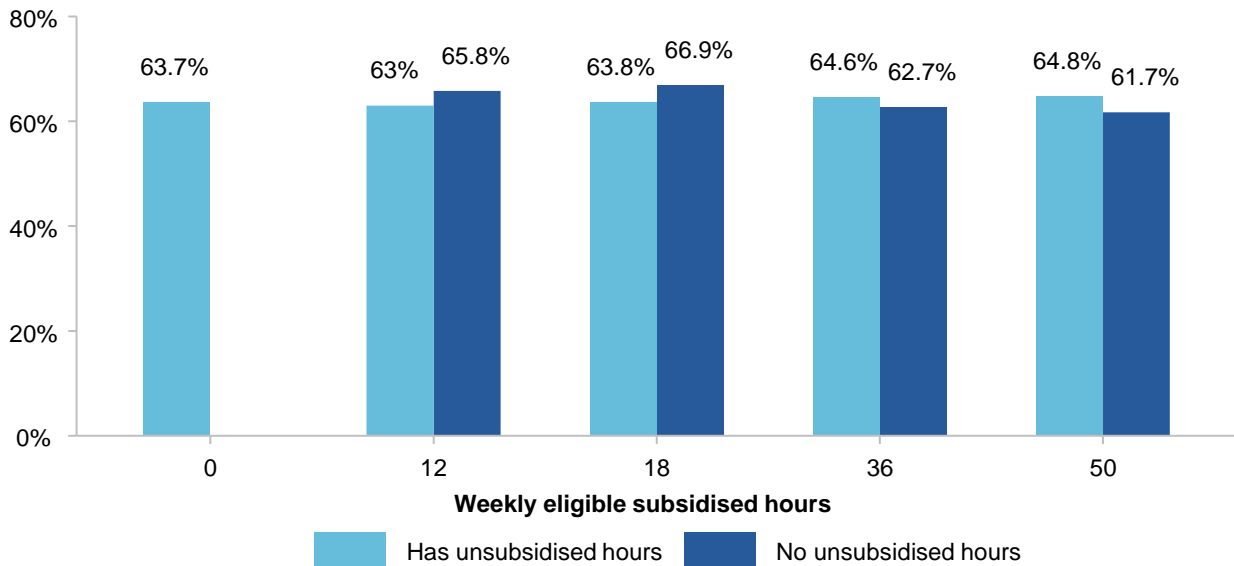
Paper 7 discusses enrolled versus attended hours further.

<sup>4</sup> Under the activity test, families are eligible for a number of subsidised hours depending on the parents' or guardians' activity levels. The activity test is discussed in more detail below.

<sup>5</sup> Unsubsidised hours are those that are not subsidised by the CCS. Families' eligibility for care to be subsidised by the CCS depends on whether they meet the activity test or have an exemption to the activity test and their level of income.

**Figure 6.5 – Attendance rates are reasonably similar across eligible subsidised hours thresholds ...<sup>a,b</sup>**

**Average proportion of charged hours attended, by eligible subsidised hours**

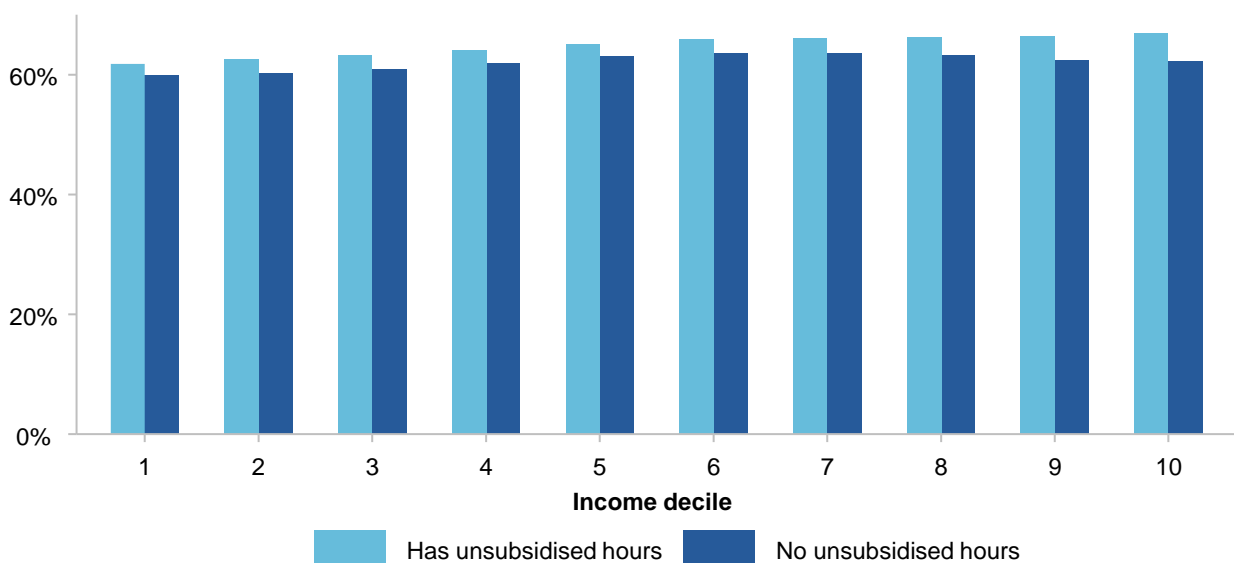


**a.** Based on families who accessed CCS-approved services in 2021-22. A family’s maximum subsidised hours can change through the year. Weekly eligible subsidised hours for a family is based on half of the family’s median fortnightly eligible subsidised hours, as reported in weekly-level data for the financial year. Weekly hours are used, rather than fortnightly hours as defined in CCS policy, to allow a simpler comparison with data provided at the weekly level, but could overstate unsubsidised hours if families use substantially different hours of ECEC across each week of a fortnight. **b.** Families with a median of no eligible subsidised hours and no unsubsidised hours represent less than 0.01% of families and are excluded from this figure.

Source: Productivity Commission estimates based on DoE administrative data (unpublished).

**Figure 6.6 – ... and income deciles<sup>a</sup>**

**Average proportion of charged hours attended, by income decile**



**a.** See figure 6.5 note a.

Source: Productivity Commission estimates based on DoE administrative data (unpublished).

## Preschool funding assists in improving affordability for children in the year before school

Preschool is attended by many children in the year before full-time school<sup>6</sup> and is delivered through dedicated preschools and CBDCs.<sup>7</sup> Most children participate in a preschool program in one of these settings, but some attend both.

There are no or low affordability barriers for children to attend a program in dedicated preschools in the year before school. All states and territories offer free or subsidised preschool through government-run services (table 6.2) during the school term. For example, the Australian Capital Territory, the Northern Territory, Western Australia and Tasmania offer free preschool in these settings. For 55% of children enrolled in a dedicated preschool in 2022, families paid no fees and for 31% of children, families paid between \$1 and \$4 per hour (ABS 2023c). There may, however, be other barriers (such as inconvenient session times or lack of access) that stop a family from sending their child to preschool in a dedicated setting.

There may be affordability barriers for children in the year before school who attend a preschool program in a CBDC. Compared to other age cohorts attending CBDCs, out-of-pocket expenses may be reduced further in some states and territories for children in the year before school (such as New South Wales, Victoria and Queensland) due to state or territory government preschool funding passed on to families as fee relief (Victoria and New South Wales provide \$2,000 and \$2,110 respectively in fee relief for children in the year before school attending a preschool program in a CBDC, for example). Families would also still be eligible to receive the same level of CCS even when accounting for this state and territory government funding.<sup>8</sup> And children in the year before school who attend preschool in a CBDC are eligible for 36 subsidised hours of care per fortnight without the need for parents or guardians to meet the activity test. Families whose eligibility for subsidised hours was below this previously would receive a higher allowance of subsidised hours. Nevertheless, some families may still face affordability barriers to access preschool through a CBDC which would be heightened for some as not all states and territory governments provide funding for out-of-pocket expense relief for children attending a preschool program in a CBDC.

As well as direct fee relief, some states provide preschool services with program funding. For example, the NSW Government offers a program payment through its Start Strong program to eligible services, on a per-child basis, which can be used for costs associated with staffing or functional and educational resources to improve the quality and affordability of preschool in New South Wales (NSW DoE, pers. comm. 30 October 2023; 2023a). In South Australia, funding from the Preschool Reform Agreement can be used for additional subsidies to services for each enrolled child who is Aboriginal and/or Torres Strait Islander or holds a concession card, and/or has a disability (CFFR 2021, pp. 7–8). And in the Northern Territory, preschool programs in regulated long day care settings may be eligible for the Northern Territory's Early Childhood Services Subsidy, which aims to help offset the cost of service delivery – although may not directly reduce fees for families (NT DoE, pers. comm., 11 October 2023).

<sup>6</sup> Some services offer preschool programs for both three-year-old and four-year-old children. This section focuses on preschool in the year before school.

<sup>7</sup> In the case of preschool programs, funding arrangements differ across jurisdictions and by service type (appendix E). Median out-of-pocket expenses for children attending preschool range from \$0 to \$3.67 per hour across jurisdictions.

<sup>8</sup> State or territory government funding provided is considered a Third Party Payment (TPP). Typically, TPPs result in a lower CCS entitlement for families. However, a TPP can be 'prescribed' in the Minister's Rules, which enables the payment to directly reduce the gap fee after CCS entitlement has been calculated (*A New Tax System (Family Assistance) Act 1999 (Assistance Act)*, paragraph 2(2A)(c) of Schedule 2).

**Table 6.2 – Fee relief for preschool in the year before school, by jurisdiction 2023**

	Fee relief	Coverage
<b>New South Wales</b>	<p>Fee relief of up to \$4,220 per year for children attending an eligible community or mobile preschool.</p> <p>Fee relief of up to \$2,110 per year for children attending an eligible CBDC or MACS preschool (in addition to CCS).<sup>a</sup></p> <p>No fees are payable in 2023 for children attending a NSW Department of Education preschool.</p>	<p>Children enrolled in 600 hours or more of preschool in a year at an eligible service will receive the maximum fee amount.</p> <p>Fee relief in community and mobile preschools is proportionately adjusted if children are enrolled for less than 600 hours per year.</p> <p>Five days per fortnight for all children.</p>
<b>Victoria</b>	<p>Free in participating dedicated (sessional) kinder programs.<sup>b</sup></p> <p>Fee relief of up to \$2,000 per year for children enrolled in a kinder program through CBDC (in addition to CCS).</p>	<p>Children attending kinder for 15 hours per week (regardless of setting) are eligible for either free kinder (dedicated programs) or fee relief (programs within CBDCs).</p>
<b>Queensland<sup>c</sup></b>	<p>Free under the Kindy plus program for certain priority cohorts.<sup>d</sup></p> <p>Fee relief of up to \$3,544 per year for sessional kindergarten or \$500 per year for kindergarten in CBDC, under the Kindy Family Tax Benefit subsidy.</p>	<p>Priority cohorts (600 hours per year)</p> <p>Families that receive the Family Tax Benefit</p>
<b>South Australia</b>	<p>Families pay contributions for government preschools, with fees set by the preschool.<sup>e</sup></p> <p>Preschool in CBDC settings is not subsidised beyond CCS.</p>	<p>15 hours per week (600 hours per year).</p>
<b>Western Australia</b>	<p>Free in government and community kindergartens with the exception of voluntary contributions up to a maximum of \$60 per year and mandatory charges for extra cost optional components under the <i>School Education Regulations 2000</i>.</p> <p>Kindergarten in CBDC settings is not subsidised beyond CCS (though grant funding to some services may indirectly contribute to reduced costs for families).</p>	<p>15 hours per week (600 hours per year).</p>
<b>Northern Territory</b>	<p>Free in government preschools.</p> <p>Preschool in other settings is not directly subsidised to families beyond CCS.</p>	<p>15 hours per week (600 hours per year).</p>

	Fee relief	Coverage
<b>Tasmania</b>	Free in public school-based settings, and free in some non-government school settings. <sup>e</sup>  CBDC-based kindergarten can be subsidised by both the state and under the Preschool Reform Agreement in some circumstances. <sup>f</sup>	600 hours per year (15 hours per week).  Five hours per week funded by the Preschool Reform Agreement if the CBDC service operates a registered kindergarten program. An additional ten hours per week funded by the state if the service registers as a school, regardless of profit status.
<b>ACT</b>	Free in public school settings.  Preschool is not subsidised beyond CCS in other settings.	15 hours per week (600 hours per year).

**a.** MACS refers to Multifunctional Aboriginal Children's Services, which are a type of childcare service for Aboriginal and/or Torres Strait Islander children. **b.** Some dedicated kinders may choose to not participate in the Free Kinder program, and can charge fees (set by the provider). Services under the Free Kinder program may also charge for additional hours above the 15 hours per week. **c.** The Queensland Government announced it will introduce free kindergarten for all children attending a government-approved kindergarten program for 15 hours a week (600 hours a year), from 2024 (2023a). **d.** Cohorts eligible for fee-free kindy under the Kindy plus program include holders of an Australian Government Health Care Card or Pensioner Concession Card, formal foster or kinship arrangements, three or more children of the same age enrolled in the same year, children living in formal child protection out-of-home care arrangements, children who identify as Aboriginal and/or Torres Strait Islander, and children whose family holds a temporary visa or is seeking asylum or have entered Australia under the Refugee and Humanitarian Program. **e.** Preschool directors set fees in consultation with the preschool's management committee, based on the estimated cost of providing the program, and children cannot be excluded from a preschool program if their family cannot pay a fee. There is some flexibility to reduce or waive fees if needed (SA DfE 2022). **f.** Families may still incur school levies when using kindergarten in a government school in Tasmania. **g.** At September 2023, no CBDC kindergarten programs in Tasmania received funding to provide free kindergarten under the National Partnership Agreement or state-based funding, because none of these services delivered a registered kindergarten program nor were registered as a school.

Source: ACT Education Directorate (pers. comm., 14 September 2023); NSW DoE (pers. comm., 30 October 2023; 2023c, 2023b, 2023a); NT DoE (pers. comm., 11 October 2023); Queensland DoE (2023b); SA DfE (2022); Tasmanian DECYP (pers. comm., 14 September 2023); Victorian Government (2023); WA DoE (pers. comm., 8 November 2023).

The high proportion of four-year-olds enrolled in preschool suggests that lower fees are effective in encouraging preschool attendance. The ABS estimated that in 2022, 87% of all children aged four were enrolled in a preschool program<sup>9</sup> (ABS 2023c).

### Families in remote areas experience unique affordability barriers when accessing preschool

Early learning programs can also be delivered by distance education for the year prior to a child starting compulsory schooling. For many geographically isolated families, this is the only avenue available to access early childhood education. Children that receive primary or secondary schooling by distance education are eligible to receive the Assistance for Isolated Children Distance Education Allowance which 'contributes towards incidental costs incurred by geographically isolated families' (DSS 2023b, p. 57).

However, children attending preschool via distance education are ineligible to receive the Distance Education allowance as it is not an approved course (DSS 2023b, p. 20).

[Children attending distance preschool] are deemed ineligible for the Assistance for Isolated Children (AIC) Distance Education Allowance as they are not recognised by the Australian Government as participating in compulsory schooling and no payment is available through the

<sup>9</sup> 22% of all children aged five were also enrolled in a preschool program.

Child Care Subsidy (CCS) either as these children are still in their parents' care while participating in distance education. (Isolated Children's Parents' Association of Australia, sub. 58, p. 5)

### **The intent of the CCS hourly rate cap is to constrain growth in fees and government spending**

The CCS hourly rate cap was introduced to provide some downward pressure on fees by sending a strong message about what a 'high fee' service is whilst allowing variability in fees and also restraining government expenditure over time (DET 2015, pp. 51, 54). It was designed to motivate families to shop around to lower their out-of-pocket expenses and that ECEC services would take this into account when setting fees (ACCC 2023b, p. 164).

### **It is unclear if the CCS hourly rate cap has constrained fees**

The Australian Institute of Family Studies (AIFS) Child Care Package evaluation<sup>10</sup> found little evidence that the CCS hourly rate cap was constraining fees (Bray et al. 2021, p. 341). The share of hours being charged over the CCS hourly rate cap has been increasing over time even with the annual indexation to CPI (ACCC 2023a, p. 129). Between 2018 and 2022, the share of CBDC and family day care (FDC) services with average fees above the CCS hourly rate cap nearly doubled from 13% to 22% and 24% to 45% respectively (ACCC 2023b, pp. 167–168). The share of OSHC services with average fees above the CCS hourly rate cap remained relatively stable at 13% (ACCC 2023b, p. 170).

The ACCC found that the complexity of the CCS along with unique characteristics of the childcare market may limit the effectiveness of the CCS hourly rate cap in constraining prices (ACCC 2023b, p. 164). For example, the ACCC noted the disconnect between the CCS calculated at an hourly level and fees generally charged at a daily level (ACCC 2023b, p. 165). It was also noted that prices are important in attracting families to services but not in retaining them (ACCC 2023b, p. 98). Non-price considerations also contribute to families' decisions to change ECEC services.

Characteristics of a service or its clientele may increase the likelihood of its fees being above the CCS hourly rate cap. The AIFS evaluation found that factors that increased the probability of being charged at least one hour with a fee in excess of the cap included: living in capital cities and remote areas; higher incomes; youngest child aged 0-2; low usage (up to ten hours per week); and living in the Australian Capital Territory, Western Australia, Victoria and New South Wales<sup>11</sup> (Bray et al. 2021, p. 70). Analysis of administrative data also shows that children from higher-income families and who live in major cities and remote Australia were more likely to have fees above the hourly rate cap (Productivity Commission estimates based on DoE data (unpublished)). Aboriginal and/or Torres Strait Islander families were less likely to be paying fees above the CCS hourly rate cap (Productivity Commission estimates based on DoE data (unpublished)).

Some of these factors, such as remoteness, would reflect higher costs in delivering ECEC that are out of families' control, but others, such as family income, likely reflect families' willingness to pay. Any potential increase in assistance aimed at increasing ECEC participation should ideally target families for whom costs are relatively high due to factors outside of their control.

Families are also more likely to face hourly fees in excess of the cap if they enrol their children in shorter sessions rather than full days in CBDC services (ACCC 2023a, p. 105). Analysis of administrative data in the AIFS evaluation indicated that services tailor session lengths and hourly fees to reflect families' number of eligible subsidised hours (which are determined by the activity test). AIFS found that families using nine hour

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<sup>10</sup> Hereafter referred to as the AIFS evaluation.

<sup>11</sup> This analysis was completed using a logit model.

sessions overwhelmingly had an entitlement to 36 or 72 subsidised ECEC hours a fortnight whereas families using ten hour sessions overwhelmingly had an entitlement to 100 subsidised hours, but these families' 'daily' rates were similar (Bray et al. 2021, pp. 168–169).

The ACCC also found that the activity test influenced session lengths with an increasing number of 10-hour session lengths charged by CBDCs. 10-hour session lengths grew the most between 2018 and 2022, increasing by 63% (ACCC 2023b, p. 177). 9-hour session lengths also increased by 36% during this same period, while 11- and 12-hour session lengths remained relatively stable (ACCC 2023b, p. 177). 10-hour session lengths were also the most common session lengths followed by 11- and 12-hour session lengths in 2022 (ACCC 2023b, p. 177). This increase in 10-hour session lengths coincides with a greater use of four and five days of care per week by families (an increase of 33% between 2019 and 2022) (ACCC 2023b, p. 176). This is likely due to the maximum entitlement of subsidised hours available under the activity test of 50 hours per week. When this 50 hours is divided amongst five days, it works out to be ten hours per day. Structuring session lengths this way means that families' entitlement is fully utilised.

Some families may face lower out-of-pocket expenses with shorter session lengths while others may be better off with longer session lengths, even if their children do not require care for the whole session (box 6.2).

### **Box 6.2 – Interactions between the Child Care Subsidy hourly rate cap and the activity test**

Divya's family and Sam's family are both looking for centre-based day care (CBDC) for their children. The CBDC they are considering offers two session length options – either ten or 12 hours. The daily fee is \$150 irrespective of session length, meaning the derived hourly cost for the ten-hour session is \$15 (above the hourly rate cap of \$13.73), while the hourly cost for the 12-hour session is \$12.50 (below the hourly rate cap). Both Divya and Sam have access to up to 72 hours of subsidised care each fortnight (or 36 hours per week), and both are eligible for an 80% subsidy rate.

Divya will be working three days a week, and considers that ten hours of care for her child per working day will be sufficient. The cost of three sessions per week is \$450. However, as illustrated in the figure below, the out-of-pocket expense for the 12-hour session is cheaper given her circumstances. The lower hourly fee means that the 80% subsidy can be applied to the whole fee amount instead of being capped.

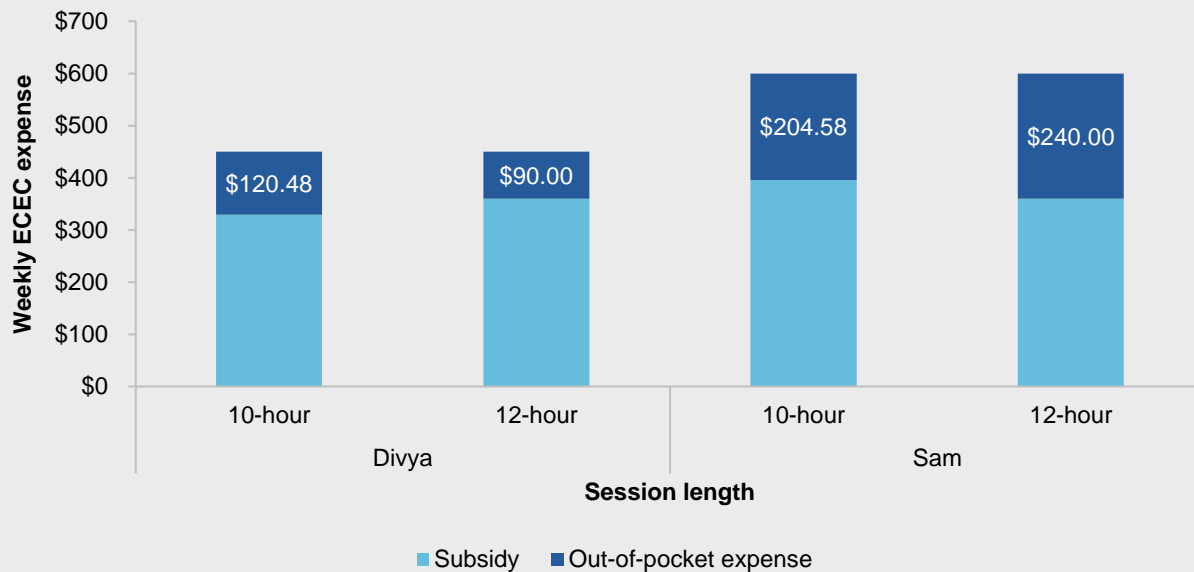
Sam will be working shorter hours for four days a week. The cost of four CBDC sessions is \$600. Sam's circumstances mean that choosing the ten-hour session length is more cost-effective, despite the higher hourly fee, because more hours of care will be subsidised under the activity test.



**Box 6.2 – Interactions between the Child Care Subsidy hourly rate cap and the activity test**

**The activity test affects out-of-pocket expenses**

**Weekly expenses, 2023-24 subsidy rates**



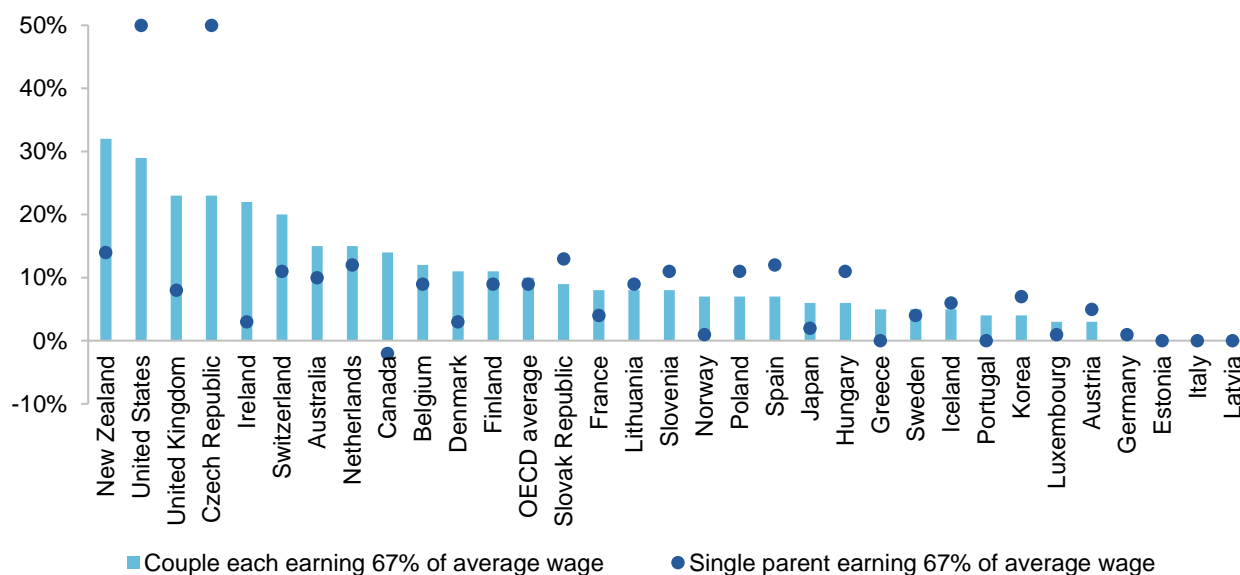
Source: Productivity Commission estimates.

**International evidence suggests that ECEC is relatively expensive in Australia**

OECD analysis based on data from 2022 indicated that Australian families tend to pay more for ECEC than families in many other developed countries (figure 6.7). It is important to note, though, that this analysis does not incorporate HCCS or the July 2023 changes to CCS rates and income testing.<sup>12</sup> The effect of HCCS on fees is unclear, but data suggests out-of-pocket ECEC expenses have fallen under the new CCS arrangements. Using preliminary Department of Education data, between July 2022 and July 2023, hourly fees increased by 8% while out-of-pocket ECEC expenses decreased by 16.6% (DoE (unpublished)). Other OECD countries have also recently made changes to their ECEC funding arrangements – for example, Ireland’s Core Funding scheme was introduced in 2022 (appendix B). It remains to be seen how these new policy settings have affected relative affordability across OECD countries. These international comparisons also rely on hypothetical examples. They do not reflect actual families’ situations but rather illustrate an ‘invented’ family’s outcome. Overall, despite these limitations, the comparisons are useful in highlighting the relative differences in ECEC expenses across countries.

<sup>12</sup> HCCS was introduced in March 2022. As HCCS was not in place on 1 January 2022, it is not modelled in the OECD’s analysis of Australia’s net ECEC expenses in 2022 (OECD 2023a, p. 20).



**Figure 6.7 – ECEC expenses are higher in Australia than the OECD average<sup>a,b,c</sup>****Net childcare expenses for single parents and couples, % of net household income, 2022**

**a.** Expenses are for full-time use of CBDC, after any benefits designed to reduce gross fees have been applied. These benefits may take the form of allowances, tax concessions, fee rebates and increases in other entitlements. **b.** Data assumes that families have two children aged two and three and that parents are aged 40 and work full-time. **c.** Information on fees and benefits is based on national rules. Where fees are determined at the local level, in most cases the local authority of a country's capital is considered.

Source: OECD (2023).

## 6.2 Some families still face affordability barriers to ECEC participation

Despite the CCS, affordability can still be a barrier to ECEC participation for some families.

- The Smith Family's Small Steps, Big Futures report stated that 'cost is a significant barrier for families and plays out differently in different contexts' (2021, p. 19).
- In its voluntary parent and guardian survey, the ACCC found that 60% of respondents said fees were somewhat financially burdensome and a further 14% struggled with fees (2023a, p. 58)<sup>13</sup>. Further, households that considered their out-of-pocket expenses burdensome limited their use of childcare (ACCC 2023a, p. 15).
- The 2022 Australian Early Learning Monitor found that 87% of Australians believe that many families do not send their children to ECEC or limit participation in ECEC due to the cost (Thrive By Five 2022, p. 5).
- A NSW Productivity Commission survey and choice modelling analysis identified that when barriers to ECEC were considered in isolation, cost was rated the highest barrier by non users, low users and high users of ECEC. But when parents considered out-of-pocket expenses amongst other barriers (such as preferred provider type and suitable hours), decisions were less influenced by cost (NSW PC 2023,

<sup>13</sup> The ACCC report notes that these statistics may be understated as the number of respondents that reported their income between \$0 and \$73,000 was lower than would be expected from a sample representative of the whole population. The sample size in the other income brackets were similar to the broader population.

p. 36). Non users of ECEC were the least responsive to changes in cost and low users of ECEC were the most responsive (NSW PC 2023, p. 15).

- In Australia, 15% of mothers who wanted a job or more hours of work and nominated caring for children as their main barrier to work, said that the costs of ECEC were the main reason they were not in the labour force (ABS 2023a) (labour force participation of parents is discussed in paper 4).

## **Families experiencing disadvantage face relatively higher financial barriers to ECEC participation**

As illustrated in figure 6.1, out-of-pocket expenses represented a higher proportion of disposable income for families in the lowest two income deciles (ACCC 2023a, p. 15). This could be limiting ECEC participation for lower-income families. Financial resources are more constrained for lower-income families which makes them more sensitive to price.

Out-of-pocket expenses could be one reason families with lower incomes are less likely to be using formal ECEC. Children living in low socio-economic areas are less likely to participate in ECEC compared to children living in higher socio-economic areas (figure 4.6).<sup>14</sup> Low-income families can still face affordability issues even when taking into account the 90% CCS rate:

for families with little disposable income, the remaining 10 per cent of childcare fees remains unaffordable. For these families, ECEC is considered a luxury, with finding housing and keeping food on the table remaining the priority. (The Salvation Army, sub. 56, p. 9)

That said, there may be other reasons why lower-income families are not using ECEC, such as the activity test (discussed below), availability (paper 5), non-financial barriers (paper 7) and preferences to care for their own children (paper 4).

Efforts to improve affordability for low-income families have been found to have positive effects on ECEC attendance. For example, Goodstart Early Learning developed the Early Learning Fund to reduce fees for children from low-income families or facing other forms of hardship, but who are not eligible for other subsidies such as ACCS (Goodstart Early Learning, sub. 125, p. 32). This support provided families with at least two days of ECEC for about \$7 a day, in addition to engagement with families to set learning goals. Children supported by the Fund were found to have higher attendance rates and better retention in ECEC – with only 7% of children leaving compared with 52% among other low-income families in 2020 and 2021.

## **Additional support is available through the ACCS for families experiencing vulnerability and disadvantage**

The ACCS plays an important role in improving affordability for families whose personal circumstances mean that they face additional barriers to accessing ECEC. The higher subsidy rate reduces out-of-pocket ECEC for eligible families. The ACCS was found to be effective and targeted at children who may be vulnerable in the AIFS evaluation (Bray et al. 2021, p. 235).

Use of ACCS is low relative to total ECEC attendance. In the 2022 December quarter, there were about 40,000 children accessing ACCS (74% of whom were eligible through the Child Wellbeing category), among the 1.4 million children attending CCS-approved services (DoE 2023c). And across the three main service types (CBDC, FDC and OSHC), between 2% and 3.7% of all hours were subsidised through ACCS (ACCC 2023a, p. 35). Children receiving In Home Care had a higher proportion of hours subsidised through ACCS (32%), which reflects

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<sup>14</sup> Although living in a low socio-economic area does not necessarily mean that all families living in the area have low incomes, spatial socio-economic data does indicate the 'collective socio-economic characteristics' of people living in an area (ABS 2023d).

that families with complex or challenging needs are eligible for this form of care. The majority of these children (over 90%) were subsidised through ACCS (Child Wellbeing) (ACCC 2023a, p. 35).

While the low usage of ACCS partly reflects the nature of this targeted assistance, there is a question of whether usage could or should be higher. Some families who are eligible for ACCS may not apply, and hence not attend ECEC, for reasons such as stigma or distrust of government. These and other barriers to ECEC attendance that are associated with the design and application of CCS are discussed below.

It is difficult to know what the 'right' level of ACCS use should be in the community. Each ACCS category targets families that face certain circumstances, and families may or may not face these circumstances permanently. For example, the ACCS (Temporary Financial Hardship) category provides assistance for 13 weeks to families that are facing temporary financial hardship (Services Australia 2022d). The ACCS (Grandparent) category provides assistance with no time limit on eligibility, to families where a grandparent or great grandparent is the guardian and receives an income support payment (Services Australia 2022c). Whether families face circumstances that make them eligible for ACCS may depend on events that occur unpredictably or vary from year to year (for example natural disasters or increased unemployment and/or financial hardship due to broader economic conditions).

To provide an indication of whether the current level of ACCS access is 'right', ACCS (Child Wellbeing) was examined as an example as it is the most commonly used ACCS category and a data source with a comparable population cohort was readily available. ACCS (Child Wellbeing) is for families caring for a child at risk of serious harm, abuse or neglect and includes children in formal foster care or formal kinship placement or in the care of the state, territory or the Minister (Services Australia 2021). The number of children receiving subsidised ECEC through ACCS (Child Wellbeing) was compared to data on children receiving child protection services.

In the December 2022 quarter, about 1% of children aged 0–12 years old received subsidised ECEC through ACCS (Child Wellbeing). This contrasts to about 3% of children aged 0–14<sup>15</sup> years receiving child protection services in 2021-22 (Productivity Commission estimates based on ABS (2023b) and AIHW (2023, table S2.3)). A child may receive child protection services if they are subject to an investigation due to a notification of maltreatment, have been granted a protection order due to being the victims of abuse/neglect or are in need of protection, are in out-of-home care because they are unable to live at home or if their families have been referred to intensive support services (AIHW 2023).

Although the ACCS (Child Wellbeing) eligibility criteria does not fully align with children receiving child protection services, it is clear that there are overlaps within these two groups. The higher proportion of children receiving child protection services relative to those receiving ACCS (Child Wellbeing) may suggest that there is scope for more children to access ACCS (Child Wellbeing). The apparent underuse of ACCS could be due to a number of reasons such as administrative complexity or families not knowing that children may be eligible to receive subsidised ECEC through ACCS (Child Wellbeing). Administrative complexity is discussed further below.

### **Other groups also experience some affordability barriers**

There are other groups in the community who potentially face affordability barriers when accessing ECEC services. One is children with disabilities and/or additional needs. The ACCC's 2023 survey of parents and guardians found that 77% of parents and guardians of a child with disability and/or complex needs said that

<sup>15</sup> Child protection services data was grouped according to the ages unborn, <1, 1-4, 5-9, 10-14 and 15-17 which meant aligning ages exactly with CCS eligibility (0-12) was not possible. The age grouping of 0-14 was used instead to provide a comparable grouping to CCS eligibility.

they found childcare fees 'somewhat financially burdensome' or that they 'struggle to pay fees', compared to 74% of all respondents (2023a, pp. 103–104). Some submissions also noted that families of children with disabilities or additional needs may incur additional costs that make it harder to access ECEC services (Gowrie SA, sub. 25, p. 9; Royal Australasian College of Physicians, sub. 37, p. 8). There is not adequate data to determine whether families of children with additional needs face higher average out-of-pocket expenses for ECEC than other families (ACCC 2023a, p. 103). But children with disabilities are slightly more likely to live in low-income households compared to children who do not live with disabilities (AIHW 2020, p. 96). This increases the likelihood that families of children with disabilities face financial barriers to using ECEC services.

Inquiry participants suggested that out-of-pocket expenses can also be a barrier to some Aboriginal and/or Torres Strait Islander children participating in ECEC.<sup>16</sup> And a qualitative study in seven communities across Australia found that affordability was a common barrier to ECEC participation for Aboriginal and/or Torres Strait Islander families – especially for families that were not using ECEC (Kellard and Paddon 2016, p. 23).

Analysis by the ACCC found that the average hourly CBDC fee charged for Aboriginal and/or Torres Strait Islander children was slightly less than for non-Aboriginal and/or Torres Strait Islander children (before subsidies) (ACCC 2023a, p. 102). This may reflect that Aboriginal and/or Torres Strait Islander children are more likely than the average Australian child to live in a less advantaged socio-economic area, where ECEC fees tend to be lower on average (ACCC 2023a, p. 81; NIAA 2023b). And while some Aboriginal and/or Torres Strait Islander families do not face difficulties with ECEC affordability, Aboriginal and/or Torres Strait Islander families are proportionally over-represented in lower income bands (NIAA 2023a), which increases the likelihood that they will face challenges with ECEC affordability.

The Productivity Commission heard from inquiry participants that other cohorts may also face higher affordability barriers to accessing ECEC, compared to the average Australian family.

- Children and families who have restricted residency in Australia (such as temporary protection visa holders) may not be eligible for CCS, which can make ECEC services prohibitively expensive.<sup>17</sup>
- Some submissions suggested that out-of-pocket expenses can be a significant barrier for families from culturally and/or linguistically diverse backgrounds (Centre for Excellence in Child and Family Welfare, sub. 59, pp. 2-3). And a qualitative study of some newly-arrived families in Australia found that cost (and low awareness of available subsidies) of dedicated preschools was a significant barrier for many participants (Brotherhood of St Laurence 2020, p. 13).
- Single parent families and families with multiple births may also face greater affordability barriers. The financial burden of ECEC can be significant for single parent families due to their greater reliance on a single income (Council of Single Mothers and their Children, sub. 100, pp. 3-7). Families with multiple births can also face higher affordability barriers due to multiple children needing ECEC at the same time (Australian Multiple Birth Association, sub. 165, p. 4).
- Families that are known to child protection, in the out-of-home care system and/or experiencing family or domestic violence can also face elevated financial barriers to using ECEC. This can include difficulties paying fees, as well as financial constraints due to relocations (which may include financial consequences if the appropriate notice is not given to ECEC services, or if children are absent) (Centre for Excellence in

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<sup>16</sup> Binarri-binyja yarrowoo Aboriginal Corporation, sub. 85, p. 10; Centre for Excellence in Child and Family Welfare, sub. 59, pp. 2-3; National Aboriginal Community Controlled Health Organisation, sub. 151, p. 6; National Indigenous Australians Agency, sub. 152, p. 5; SNAICC, sub. 133, p. 18.

<sup>17</sup> 1<sup>st</sup> Impressions Early Learning Centre, sub. 91, p. 1; Early Years Intercultural Association, sub. 97, p. 1; Brotherhood of St. Laurence, sub. 96, p. 7; Paul Ramsay Foundation, sub. 148, p. 4; The Salvation Army, sub. 56, p. 14.

Child and Family Welfare, sub. 59, p. 2; Council for Single Mothers and their Children, sub. 100, p. 5; WA Government, sub. 162, p. 10).

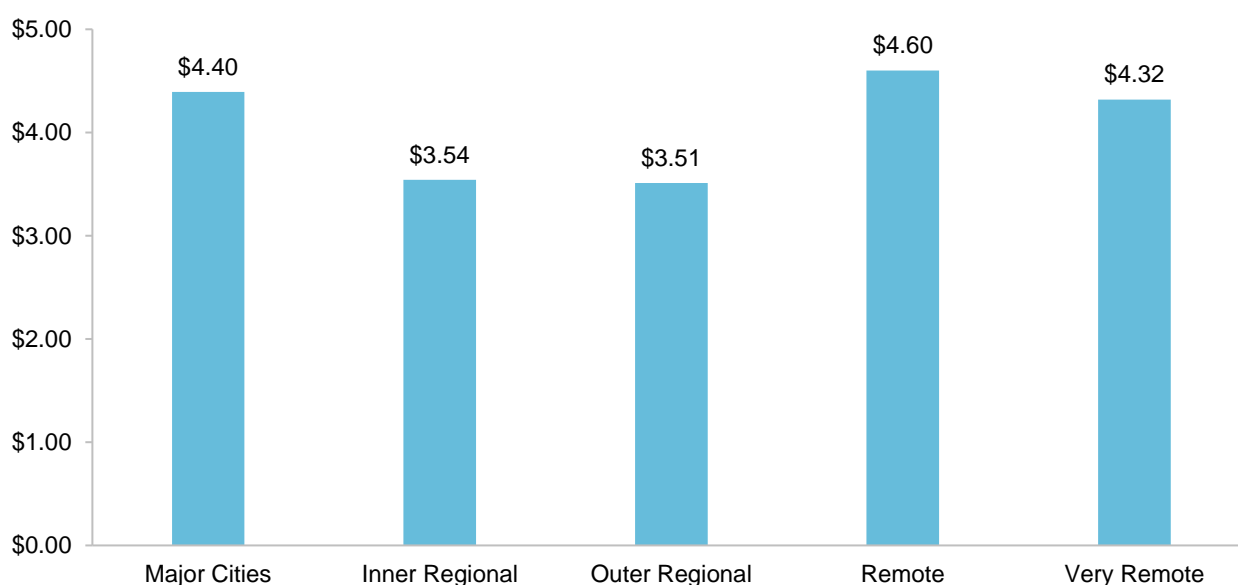
Some families also face barriers due to the indirect costs of ECEC. Families living outside of metropolitan areas can incur significant additional costs associated with travel and time to get to an ECEC service, which can increase the financial barriers to ECEC (SDA, sub. 72, p. 20) (paper 7 discusses this in more detail).

### The relationship between remoteness and affordability is complex

Although mean out-of-pocket expenses do not increase or decrease consistently with remoteness – expenses are highest on average in metropolitan and remote areas (figure 6.8) – there is some evidence that affordability may be of particular concern to families living in remote areas.<sup>18</sup> Additional expenses associated with ECEC participation (such as travel costs) can be higher for families living in regional and remote Australia (paper 7 discusses this further).

#### Figure 6.8 – Mean out-of-pocket expenses are highest in metropolitan and remote areas<sup>a</sup>

##### Mean hourly out-of-pocket expenses by remoteness, 2021-22



a. This analysis excludes cases where out-of-pocket expenses were zero.

Source: Productivity Commission estimates based on DoE administrative data (unpublished).

The ACCC's June interim report identified that families in remote and very remote Australia have lower effective subsidy rates on average than families in less remote areas. This means that compared to other families in Australia, families in remote and very remote Australia, on average, receive a lower proportion of subsidy relative to the fees they pay. And the difference cannot be explained by differences in household income or CCS rates. A possible reason for this difference is that families in remote and very remote Australia use more unsubsidised hours compared to other families. The ACCC intends to investigate

<sup>18</sup> One caveat of the following discussion is that while data on fees and out-of-pocket expenses represents the best available information on how affordability differs with remoteness, a more relevant measure of affordability may be out-of-pocket expenses as a proportion of household income.

whether this trend can be explained by families living in remote areas being more likely to use ECEC services beyond their maximum number of subsidised hours under the activity test (2023a, pp. 116–117).

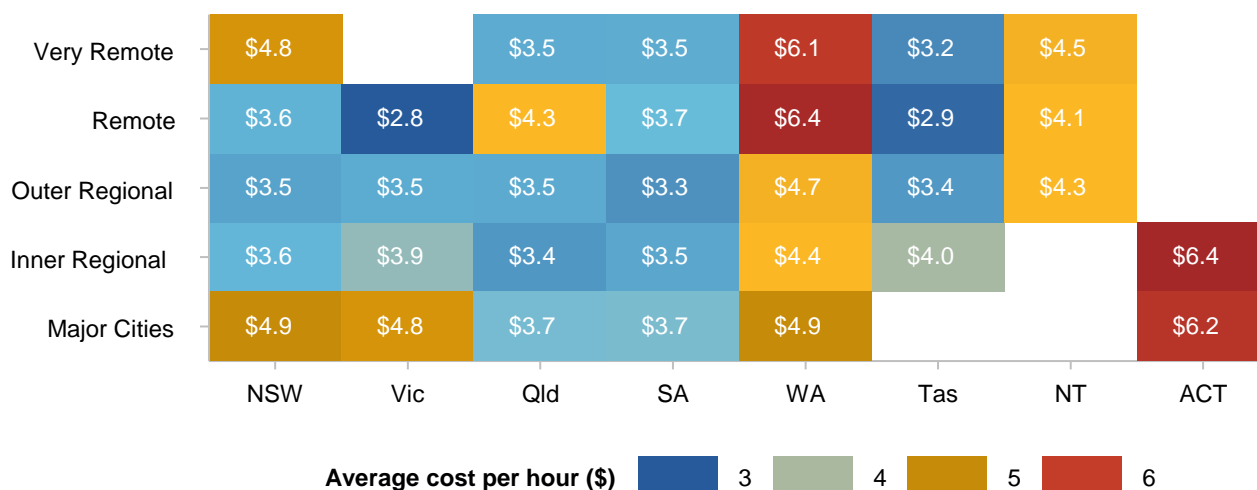
These aggregate figures, however, obscure more complicated associations between remoteness, fees and out-of-pocket expenses. For example, the relationship between remoteness and average fees differs by service type. Mean CBDC fees fall with remoteness, while mean FDC fees increase. OSHC fees do not display a clear pattern – mean fees are highest in remote Australia and similar across other levels of remoteness (ACCC 2023a, p. 80).

The link between remoteness, affordability and service type is further complicated by the fact that other factors affecting affordability, such as market structure, differ systematically with remoteness. For example, most CBDC services in remote areas are operated by not-for-profit providers and fees for not-for-profit services are lower on average than fees for for-profit services (ACCC 2023a, p. 94). Likewise, large CBDC providers (40 or more services) are less likely to operate in remote and very remote Australia, and mean fees for small providers (less than five services) are lower than mean fees for large providers (ACCC 2023a, p. 95).

Additionally, the association between remoteness and out-of-pocket expenses differs by jurisdiction (figure 6.9). While mean out-of-pocket expenses fall with remoteness in Victoria and Tasmania, in Western Australia, mean out-of-pocket expenses rise significantly with remoteness. This is at least partly explained by the fact that mean CBDC and OSHC fees are higher in Western Australia’s remote areas than in other states and territories. The ACCC will explore whether the large number of mining towns in Western Australia is contributing to this result (2023a, pp. 85–86).

**Figure 6.9 – The association between out-of-pocket expenses and remoteness varies by jurisdiction<sup>a,b,c</sup>**

**Average hourly out-of-pocket expenses, by jurisdiction and remoteness, 2021-22**



a. Out-of-pocket expenses are adjusted to June 2023 dollars. b. Blank tiles mean no cross-classifications between jurisdiction and remoteness level. c. This analysis excludes cases where out-of-pocket expenses were zero.

Source: Productivity Commission estimates based on DoE administrative data (unpublished).

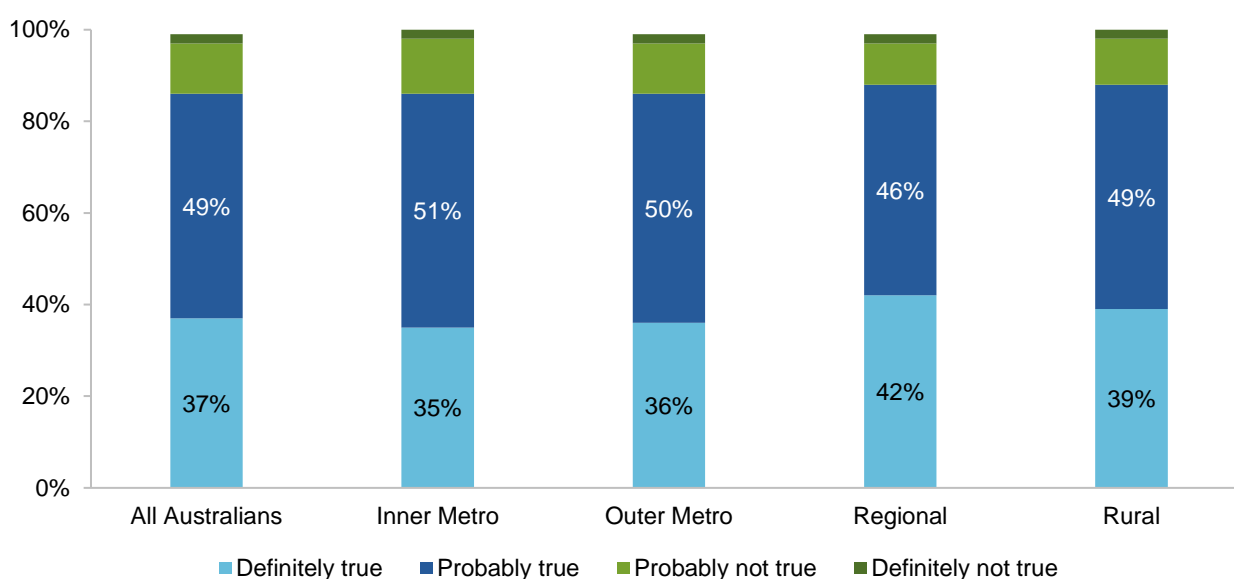
**Perceptions of ECEC affordability differ with remoteness**

As well as identifying whether actual fees and out-of-pocket expenses change with remoteness, it is also important to consider whether perceptions of affordability differ geographically as perceived affordability of ECEC – regardless of the actual expense – acts as a barrier to ECEC participation (The Smith Family 2021, p. 5). Figure 6.10 highlights that concerns about ECEC affordability are slightly more pronounced in regional

and rural areas relative to metropolitan areas. Additionally, parents using ECEC in regional Australia are relatively more likely than those in metropolitan areas to believe that ECEC costs have risen substantially over the past three years (Thrive By Five 2023).

**Figure 6.10 – People in regional and rural areas are slightly more likely to be concerned about ECEC affordability**

**Share of responses to the statement ‘Many families don’t send their children to early childhood education and care or limit how long they send them, because of the cost’**



Source: Thrive by Five (2022).

## The activity test aims to increase labour force participation

As noted above, the number of subsidised care hours a family is eligible for is determined by the level and type of ‘activity’ of the parent or guardian (table 6.3). Recognised activities include working, volunteering, looking for work, maternity and parental leave and education and training. When there are two parents or guardians, the lower activity level determines the number of eligible subsidised hours.

In 2021-22, a majority of families were eligible for the maximum number of subsidised care hours of 100 hours per fortnight (table 6.3) and very few were eligible for none (Productivity Commission estimates based on DoE administrative data (unpublished)).<sup>19</sup> The majority of families meet the activity test through undertaking paid work (paper 4, figure 4.1).

For some families, exemptions to the activity test apply. Eligible families can access between 24 and 100 hours of subsidised care each fortnight depending on their entitlement without meeting the activity test. Further details on the activity test and exemptions are in appendix D.

<sup>19</sup> As families’ maximum number of subsidised care hours can change through the year, this analysis used the median value for each family as reported in weekly level data.



**Table 6.3 – Higher activity levels increase a family’s eligible subsidised care hours<sup>a,b</sup> 2021-22**

Implied activity level each fortnight	Hours of subsidised care each fortnight	Number of families	Percentage of families
Less than eight hours	0 hours if income is above \$70,015	10,945	1.0
	24 hours if income is \$70,015 or below <sup>d</sup>	15,564	1.4
More than eight to 16 hours	36 hours	51,281	4.6
More than 16 to 48 hours	72 hours	304,590	27.1
More than 48 hours	100 hours	743,499	66.0

**a.** Based on number of families who accessed CCS-approved services in 2021-22. Some families were excluded due to missing data. Implied activity hours is based on median observed eligible subsidised hours for a family during the year, rather than actual activity hours (which could be lower at points during the year due to exemptions to the activity test, including for most ACCS recipients). **b.** Income thresholds based on 2021-22 CCS policy.

Source: Productivity Commission estimates based on DoE administrative data (unpublished).

### However it is unclear if the activity test has had its intended effect on labour force participation

The activity test was tightened in July 2018 with the introduction of the CCS to induce parents and guardians to increase their activity levels. Under the previous funding model, families that undertook at least 15 hours of activity a week were eligible for up to 50 hours of subsidised ECEC. Families that did not meet this test were eligible for up to 24 hours a week. With implementation of the 2018 Child Care Package, the number of subsidised hours that families could access without the need to meet an activity test was halved to 24 hours per fortnight (12 hours per week) (Bray et al. 2021, p. 8).<sup>20</sup>

The change to the activity test was recommended in the Productivity Commission’s 2014 ECEC inquiry.

The Commission is aware that this activity test may deter some parents from taking a job with very low hours per week, but it also provides an incentive to increase work hours above the minimum threshold for ECEC assistance. The recommended hours for the activity test reflects the need to balance these incentives, as do the recommendations on the exemptions from the activity test. (PC 2014, p. 25).

Whether the activity test has increased labour force participation is ambiguous. As noted in the AIFS evaluation:

taken as a whole, these results suggest that while employment and other activity of parents may have increased since the introduction, the impact is small, and cannot necessarily be attributed to the [2018 Child Care] Package, as opposed to ongoing trends towards greater participation. (Bray et al. 2021, p. 280).

### The activity test can make it harder for some families to participate in ECEC

The tightened activity test has increased barriers for some families to participate in ECEC, particularly for those living with disadvantage. The AIFS evaluation found that the 2018 reduction in subsidised hours ‘disproportionately impacted children in more disadvantaged circumstances’ (Bray et al. 2021, p. viii). In regards to the 24 hours of subsidised care per fortnight, the evaluation also noted that ‘these hours can be

<sup>20</sup> Families with more than four and less than 15 hours of activity per week in 2018 became eligible for either 18 or 36 hours of subsidised care a week under the new test.



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quickly absorbed by long session times and weekly booking routines, with the 24 or 36 hours typically translating to one day a week in a service that has 10, 11 or 12 hour daily sessions' (Bray et al. 2021, p. 185). Between 2018 and 2022 there was a 26% drop in the number of children accessing the non-activity tested 24 hours of subsidised care per fortnight (Productivity Commission estimates based on DoE administrative data (unpublished)). There could be a number of reasons for this including:

- affordability barriers (even with assistance through the subsidy)
- lack of access to ECEC
- families unwilling to put their children in for one day of ECEC per week
- families receiving assistance through ACCS (Child Wellbeing) which provides a higher subsidy rate and more subsidised hours (over this same period there was an increase in the number of families with a child accessing ACCS (Child Wellbeing) (Productivity Commission estimates based on DoE administrative data (unpublished) although correlation does not necessarily mean causation).

Any hours above eligible subsidised hours that are unsubsidised can limit ECEC participation for families living with disadvantage. Analysis of CCS administrative data for 2021-22 shows that families eligible for 12 and 18 hours of subsidised ECEC tended to have lower incomes (figure 6.11) and used less ECEC than those eligible for more subsidised hours (Productivity Commission estimates based on DoE administrative data (unpublished)). Furthermore, lower-income families were more likely to have a higher number of unsubsidised hours (figure 6.12). The ACCC had similar findings in its September interim report (ACCC 2023b, p. 181).

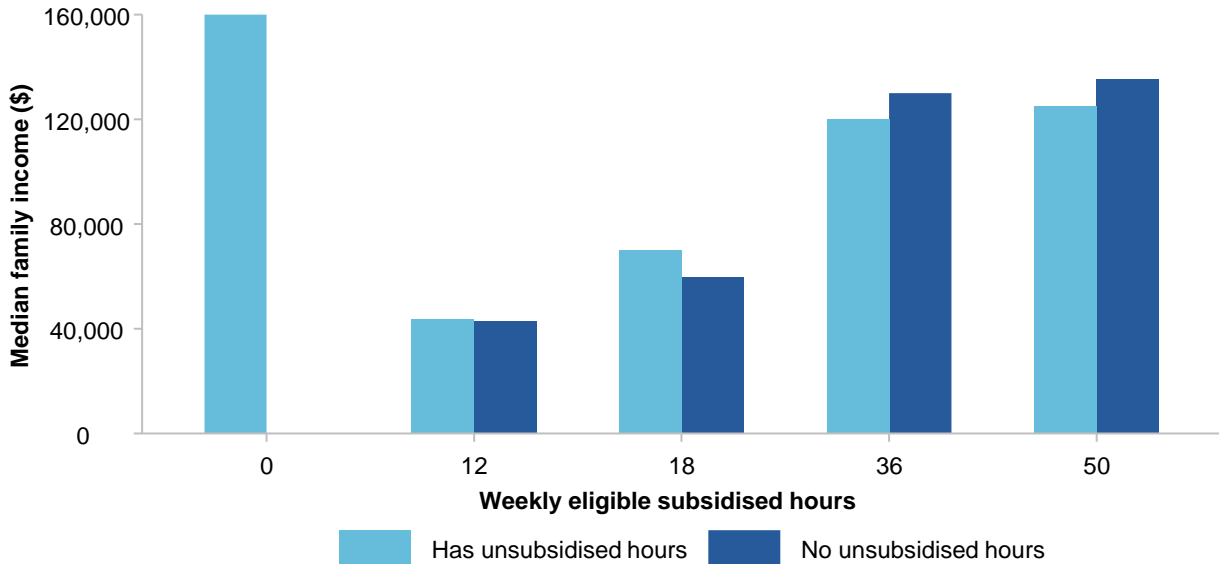
Furthermore, families eligible for relatively few subsidised hours are more likely to accrue unsubsidised hours (figure 6.13). In 2021-22, 6% of families were eligible for either 12 or 18 hours of subsidised ECEC a week. About two-thirds of each of these groups were charged for at least some unsubsidised hours of care during the year – with the mean shares of unsubsidised hours sitting at about 33% and 19% for each group respectively. These families also tended to have lower incomes (figure 6.11).<sup>21</sup> In contrast, only about 30% of families with a higher number of eligible subsidised hours accrued unsubsidised hours and these families also tended to have higher incomes (figure 6.11).

Recent changes to the activity test aim to support participation in ECEC for Aboriginal and/or Torres Strait Islander children. From 10 July 2023, the number of subsidised ECEC hours that these children can receive increased to 36 hours per fortnight, regardless of activity level.

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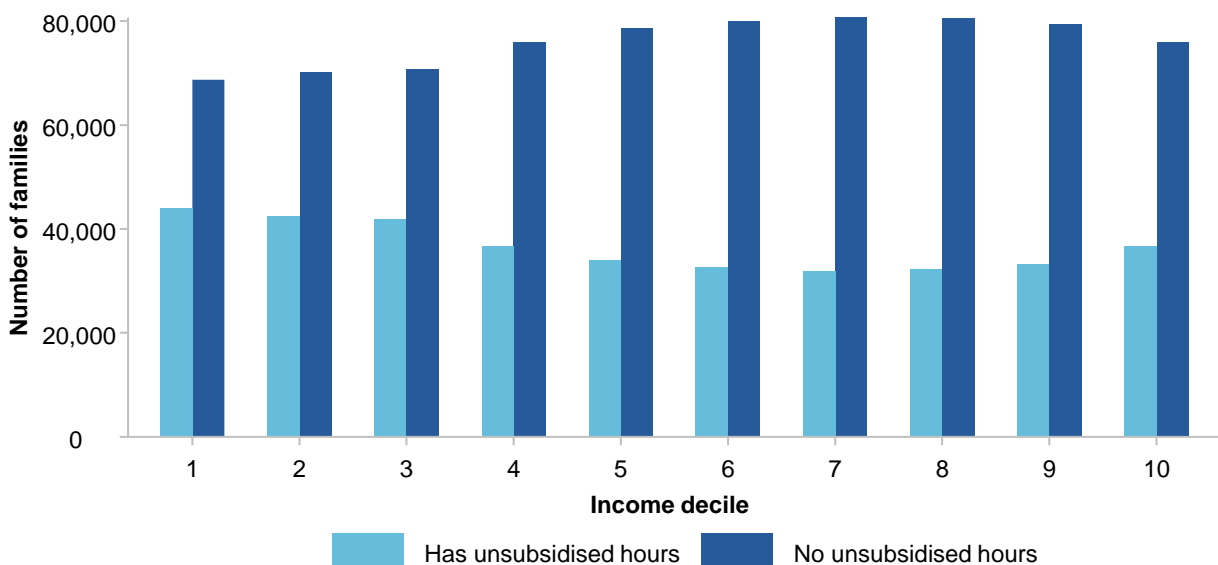
<sup>21</sup> If reported incomes are an accurate reflection of actual incomes, the relatively low incomes of some families accruing unsubsidised hours raises the question of how families are paying for those hours. The AIFS evaluation made similar observations and suggested that some families may be drawing on other economic resources (such as assets and support from families or friends) (Bray et al. 2021, p. 79).

**Figure 6.11 – Families with 12–18 eligible subsidised hours have lower incomes<sup>a,b,c</sup>**  
**Median family income by weekly eligible subsidised hours and whether accrued unsubsidised hours, 2021-22**



**a.** A family’s maximum subsidised hours can change through the year. Weekly eligible subsidised hours for a family is based on half of the family’s median fortnightly eligible subsidised hours, as reported in weekly-level data for the financial year. Weekly hours are used, rather than fortnightly hours as defined in CCS policy, to allow a simpler comparison with data at the weekly level, but could overstate unsubsidised hours if families use substantially different hours of ECEC across each week of a fortnight. **b.** Median family income is the median of incomes across families, where the income for each family is the median of their reported incomes in the financial year. **c.** Families with a median of no eligible subsidised hours and no unsubsidised hours represent less than 0.01% of families and are excluded from this figure. Source: Productivity Commission estimates based on DoE administrative data (unpublished).

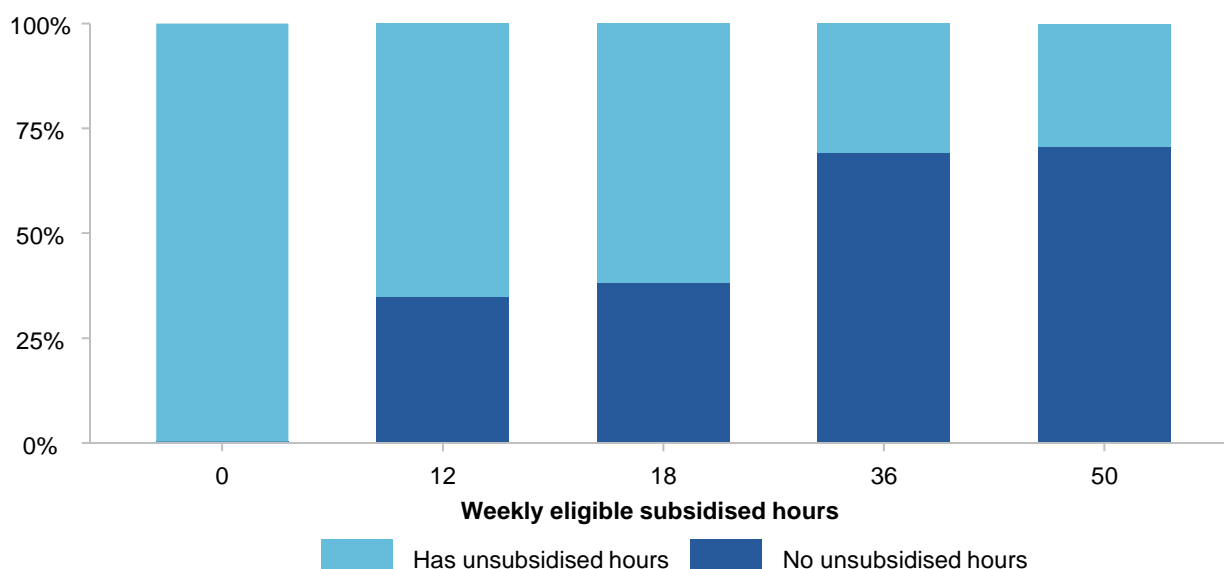
**Figure 6.12 – Lower-income families are more likely to have unsubsidised ECEC hours<sup>a,b</sup>**  
**Number of families with and without unsubsidised hours by income decile, 2021-22**



**a.** See figure 6.11 note a. **b.** A family’s median reported income through the year was used to calculate deciles. Source: Productivity Commission estimates based on DoE administrative data (unpublished).

**Figure 6.13 – A large proportion of families with 12–18 eligible subsidised hours a week accrue some unsubsidised hours each year<sup>a</sup>**

**Proportion of families accruing unsubsidised hours by eligible subsidised weekly hours, 2021-22**



a. See figure 6.11 note a.

Source: Productivity Commission estimates based on DoE administrative data (unpublished).

While the activity test caps subsidised hours for some families, its mere existence may discourage ECEC participation. Parents or guardians may not understand their reporting requirements or what activity types are eligible, and/or be concerned about a potential CCS debt if they misreport their activity hours and as a result may choose not to send their children to ECEC.

Services and inquiry participants expressed concern about families' understanding of eligibility for subsidised care under the activity test particularly where the parent or guardian had casual or intermittent working hours or completed non-paid work (Bray et al. 2021, p. 48). The guidance for casual or irregular hours of work is that parents or guardians should provide an estimate of the highest number of hours they expect to work in a fortnight for the next three months which then determines their eligible number of subsidised hours (Services Australia 2022a). However, families may not know or understand how intermittent working hours can affect their number of subsidised ECEC hours due to unclear advice from Services Australia. Some may think that their number of subsidised hours is dependent on their actual work hours each fortnight, and that if they enrolled their child to cover the maximum number of hours they might work and those hours did not eventuate, that they would have to pay unsubsidised rates for the difference. As a result, they may only enrol their child for the number of hours they are confident they will work. This likely makes it challenging for these families to increase their working hours when there is an opportunity to do so.

Some families may even choose not to access ECEC due to the complexity of the activity test and the need to understand what activities are eligible and how activity levels affect their eligible number of hours of subsidised ECEC. The Smith Family's *Small Steps, Big Futures* report notes that some families did not

understand that CCS is available for preschoolers<sup>22</sup> in the year before school regardless of their parent or guardian's activity levels (2021, p. 19). Several submissions discuss these issues (box 6.3).

### **Box 6.3 – Submissions regarding families' experiences with the activity test**

The requirements of the activity test are difficult to navigate for some families who are unsure as to which activities satisfy the test's guidelines, or who have fears about the financial consequences of incorrectly reporting their activity ... [The activity test] is especially problematic for families with unpredictable incomes [and] those with casual work and/or short-term contracts. (SNAICC, sub. 133, pp. 19–20)

Families on the bottom rungs of the activity test are more likely to have irregular work patterns, insecure work, or other complexities ... they still need ECEC but pay a much higher out-of-pocket cost because they don't meet, or cannot navigate, the Services Australia notification process for the overly complex activity test. (Goodstart Early Learning, sub. 125, p. 31)

The CCS activity test has ... contributed to significant uncertainty for parents in casual employment or a range of changing employment arrangements due to the ongoing risk that they will fail to meet the activity test and generate over-payment debts. In its current form the activity test is not inclusive of shift workers and casual workers who experience uncertain work hours. (NSW Government, sub. 158, p. 6)

Further, from discussions with the Department of Education (pers. comm., 6 November 2023), the Commission understands that families' activity levels are not actively audited. This means that if a family's activity levels change such that it would change their subsidised hours entitlement and the family does not report it, there will be no impact on the number of their subsidised hours. There is an incentive for families to update their activity levels when they increase as it could result in an increase in subsidised hours. However, there is not the same incentive when activity levels decrease. If families update their activity levels when they decrease such that their number of subsidised hours entitlement decreases then they will no longer be eligible to receive a higher number of subsidised hours. However, those families who do not update their decreased activity levels would continue to receive the same number of subsidised hours. This is inequitable as those families who update their activity level are worse off compared to those that do not update their activity levels.

In its report to the Australian Government, the Interim Economic Inclusion Advisory Committee identified that the activity test in its current form:

- is poorly designed and punitive
- contributes to children from the poorest households missing out on subsidised ECEC
- leaves low-income families most likely to be paying extra for unsubsidised care
- acts as a barrier to some parents participating in the labour force and working more hours
- has significant administrative complexity for little benefit
- produces a risk of overpayment for casual employees (Interim Economic Inclusion Advisory Committee 2023, p. 69).

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<sup>22</sup> Preschoolers attending preschool at a CBDC service are eligible for 36 hours of subsidised ECEC regardless of their parent or guardian's activity level (DSS 2023a).

The report also noted the uncertainty and complexity associated with the activity test can dissuade ECEC usage by families and usually these families are living with disadvantage (Interim Economic Inclusion Advisory Committee 2023, p. 68). The OECD has also noted that it is important that any work requirement to receive childcare cost assistance is balanced with additional measures for low-income families (OECD 2020, p. 10).

## **Other aspects of administrative complexity can make it harder for families to understand and access the CCS**

Difficulties in families understanding ECEC subsidy arrangements has been an enduring issue. The Productivity Commission's 2014 inquiry into ECEC found that the system at the time was complex and that families had difficulty understanding their entitlements under the then dual subsidy approach (PC 2014, p. 44). Some elements of the 2018 Child Care Package were intended to make the system simpler (including by shifting to a single CCS approach). However, the package also introduced additional complexities, such as the hourly rate cap, more detailed activity testing and delivery of all assistance through Centrelink. A survey found that parents were weakly positive about the new CCS being easier to understand than the former subsidy system, but 43% still 'neither agreed or disagreed' with this statement when asked both shortly after the introduction of the CCS and one year after (Bray et al. 2021, pp. 41–42).

While the 2023 Cheaper Child Care Package has made adjustments that may simplify understanding of the CCS, such as the change to a simpler sliding subsidy rate with changes to family income, other sources of administrative complexity remain (box 6.4).

### **Box 6.4 – Submissions about administrative complexity in the Child Care Subsidy system**

The process [of understanding which subsidies families are entitled to] can be complicated, and families can get overwhelmed, particularly if literacy is also a concern. (The Hive Mount Druitt (United Way Australia), sub. 64, p. 3)

The inherent complexity in the CCS system, including its frequent changes, confuse families using Family Day Care ... The lack of education to families about fee caps and the impact on their subsidies if educators charge over the fee cap [causes] friction between educators and families. (NSW Family Day Care Association, sub. 89, p. 9)

Many families either do not know of the supports available to them or need additional assistance to engage and participate due to the complexity of the system ... Language is a common barrier. Many services use acronyms or terms that families (and most service providers) struggle to understand. It is even more challenging for recent migrants who are unfamiliar with Australian public services or speak English as a second language. [Brotherhood of St Laurence] staff frequently find that translated resources are inaccurate and confusing, causing families to disengage. (Brotherhood of St. Laurence, sub. 96, p. 7)

All families, especially disadvantaged families and families with fluctuating incomes, face challenges to navigate the system and avoid overpayments and debts. (Victorian Government Department of Education, sub. 146, p. 8)

## Families can find it difficult to understand how much CCS they are entitled to

The multiple components of the CCS subsidy calculation can make it challenging for families to understand whether they are eligible for the CCS, and how much they might be eligible for.

- A draft finding from the ACCC's September interim report was that 'The Child Care Subsidy is complex for parents and guardians to understand and it is difficult to estimate out-of-pocket expenses' (ACCC 2023b, p. 160).
- The AIFS evaluation found that, on average, parents viewed that they had 'somewhat of an understanding' of various aspects of the CCS in September 2019 (Bray et al. 2021, p. 44). The effect of activity hours was less understood than the effect of family income on CCS entitlements. Families that worked variable hours were more likely to report lower understanding overall.
- A more recent 2021 survey commissioned by The Front Project (2021, pp. 43–44) indicated that among parents of children aged 0-5 years who were not yet at school, about half agreed that working out eligibility for ECEC subsidies or government benefits was straightforward. However, 27% disagreed with the statement, including 9% who strongly disagreed.
- The Department of Education's (unpublished) parent survey in June 2023 found that the effect of the number and age of children on CCS entitlements was less understood than the effect of family income and activity hours. 37% of families using ECEC considered they understood the effects of number and age of children in paid care on CCS entitlements either well or very well – these shares were 40% and 47% for activity hours and family income respectively. That said, at least another third of parents considered they had 'somewhat of an understanding' across all these questions.

Some of the challenges with understanding CCS entitlements relate to how different components of the calculation interact when families change their circumstances. For example, if a parent decides to increase their working hours, their family's income may increase, which would reduce their CCS rate. But their activity hours would also increase, so they may be eligible for a greater number of subsidised care hours. Parents or guardians transitioning from income support to employment face the additional challenge of figuring out how their income support and rent assistance payments would be affected, as well as the cost of ECEC (Bray et al. 2021, pp. 48–49). Parents or guardians may also have the further challenge of the number of eligible subsidised hours reducing if they were previously exempt from the activity test. Additional income may also impact the amount of Family Tax Benefit A and B a family receives and may have implications for how much income tax and Medicare levy a family is liable for. (Paper 4 discusses the impact of the withdrawal of income support on labour force participation.)

The HCCS rate is no longer linked to the CCS rate, adding an additional layer of complexity. When the HCCS was first introduced, it was set to be a 30% higher subsidy than the CCS up to a maximum of 95% (DoE 2021). However, since 10 July 2023 the CCS has been streamlined (such that the CCS rate decreases by 1% for every \$5,000 of family income over \$80,000) but the HCCS has remained largely unchanged (figure 6.3 illustrates the CCS and HCCS in 2022-23 and 2023-24).

Changes to ECEC session lengths can also have opposing effects on CCS calculations. As described above, some families may face lower out-of-pocket expenses with shorter session lengths so that fewer care hours are unsubsidised, while others may be better off with longer session lengths so that the hourly fee is more likely to be within the CCS hourly rate cap. These calculations are difficult to understand without assistance or detailed knowledge of the design of the CCS. That said, among CBDCs that offer multiple session lengths, the patterns of usage of particular session lengths appear to align with the number of subsidised hours that families have (ACCC 2023b, p. 174; Bray et al. 2021, pp. 155, 169). This indicates that families are, to an extent, choosing session lengths that lower their out-of-pocket expenses at these services, either through their own understanding or with support from services.

Tools are available to help families understand the CCS and out-of-pocket ECEC expenses. For example, the Australian Government's Starting Blocks and Centrelink websites include calculators that estimate out-of-pocket expenses (with the Centrelink calculator covering all Centrelink payments and services). However, neither calculator allows families to easily compare the effect of changes in circumstances (such as changes in work hours or session lengths) on their out-of-pocket expenses. Further, other factors may limit the usefulness of these information sources to families, such as low awareness (with only 10% of surveyed ECEC users reporting that they were aware of Starting Blocks) and outdated or missing fee information on the Starting Blocks website (which relies on services to update fee information) (DoE 2023 Starting Blocks Survey Report (unpublished)). That said, families are more likely to use websites of ECEC services themselves to access information, including on fees and out-of-pocket expenses (DoE 2023 Starting Blocks Survey Report (unpublished)), and some large providers have added cost comparison features to estimators on their websites to fill this demand (Bray et al. 2021, p. 49).

Services themselves can also support families in understanding their CCS eligibility and entitlements, including in the effect of session lengths described above. More than 85% of services considered that they had at least a good understanding of the 2018 Child Care Package by July 2019 (Bray et al. 2021, pp. 50–51). Some major ECEC providers employ staff dedicated to supporting families applying for government subsidies (Goodstart Early Learning, sub. 125, p. 61–62). However, services are not always able to assist families with their CCS application and enrolling for ECEC through myGov (described further below) and not all families may reach out for assistance.

### **Families experiencing disadvantage may find it particularly difficult to engage with the CCS system**

Families must apply for CCS through Centrelink (administered by Services Australia), and then register their enrolment in an ECEC service through myGov in order to receive the subsidy. These processes are not always well understood and issues can be difficult to resolve and also emerge throughout the process. In the AIFS evaluation (Bray et al. 2021, pp. 54–56, 234), services described a number of issues that families face, such as:

- delays in Services Australia processing CCS applications for a minority of families, which are sometimes due to processing errors or incomplete or inaccurate documentation on immunisation records or birth certificates
  - however, the time to finalise CCS claims in less than 28 days has improved from 67% in 2018-19 to 87% in 2022-23 (Services Australia (unpublished))
- Services Australia staff providing incorrect, incomplete or inconsistent information and advice to families, including in relation to ACCS
- families not knowing they need to confirm their enrolment in ECEC through myGov, and services finding it difficult to support them as they did not have visibility of what the families needed to do
- services not being able to support families, including for ACCS applications, as they are prevented from liaising with Services Australia on specific queries about families
- long wait times, lengthy exchanges and slow resolutions on the phone with Services Australia (for families) and the CCS Helpdesk (for services and providers).

More than half of parents of school age or younger children surveyed by Thrive by Five (2022) agreed that the thought of having to go through Centrelink to apply for support they were entitled to (such as CCS) would put them off applying for it. Half of parents also agreed that the possibility of making a mistake in a Centrelink application would put them off seeking support they were entitled to.

Some families may find it particularly difficult, or be reluctant, to access CCS and ACCS, and hence require additional supports to access ECEC, for example due to:



- cultural and language barriers (Bray et al. 2021, pp. 54, 234; Brotherhood of St Laurence, sub. 96, p. 7) (this is discussed further in papers 2 and 7)
- distrust of government organisations and stigma associated with a child being identified as ‘at risk’ in order to access ACCS (Child Wellbeing), especially for Aboriginal and/or Torres Strait Islander families (Bray et al. 2021, pp. 233–234, 333; The Smith Family 2021, p. 17; Goodstart, sub. 125, p. 29)
- fear of making mistakes in their application, leading to CCS debts (discussed further below)
- complex or uncommon family circumstances that make the application process less straightforward, such as:
  - needing to calculate activity hours when engaged in intermittent work (Bray et al. 2021, p. 49)
  - changes in a child’s custody or living arrangements that require the child’s new guardian to reapply for the child’s CCS (Goodstart Early Learning, sub. 125, p. 35)
  - children under the care of an informal kinship carer, who are not recognised in eligibility for ACCS (Grandparent) (Bray et al. 2021, p. 249).

Issues and delays in accessing CCS and ACCS can be financially challenging for families and can mean that children experiencing disadvantage are unable to access care in the meantime, especially where services are asked to charge families full fees before they are approved to receive CCS (Bray et al. 2021, p. 234). This can lead to families incurring debts to services (described further below).

Measures in the 2023-24 Australian budget were aimed at reducing administrative complexity for ACCS (Child Wellbeing) by supporting enrolments to be ‘assessed in a more streamlined manner, [and] reducing double handling and the risk of potential gaps in entitlement for the subsidy’ (DoE 2023a).

The potential impacts of some of these administrative challenges were illustrated to an extent in the midst of the COVID-19 period. The Australian Government made ECEC free between 6 April 2020 to 12 July 2020, and removed requirements for families to apply for CCS or meet eligibility requirements. Goodstart Early Learning found that although some families reduced their attendance at Goodstart centres during this period, others enrolled or increased their children’s attendance. Families who were not previously able to access CCS (due to failing the activity test or the visa status of refugee families) were able to during the free period, and nearly half of Aboriginal and/or Torres Strait Islander children increased their days attended – including those for whom ECEC was already free due to eligibility for ACCS. Removing the administrative burden and Centrelink process, reducing stigma of accessing care, and Goodstart’s own engagement processes, were nominated as contributors to the increased ECEC usage during this time (Wong et al. 2021, pp. 10–11).

Research from overseas suggests that reducing the administrative burden of applying for ECEC for lower socio-economic status families can increase children’s ECEC attendance and mothers’ labour force participation. A study of lower socio-economic status families with children aged under three years in Germany, for example, involved providing information and customised assistance in applying for Germany’s universal ECEC system. This led to increased enrolments in ECEC relative to those who did not receive this assistance, and improved mothers’ full-time employment and earnings (Hermes et al. 2022, p. 25).



#### **Draft finding 6.2**

#### **Complex ECEC subsidy arrangements can be a barrier to access for some families**

The information available to families when they are working out their Child Care Subsidy entitlement can be confusing and create substantial uncertainty as to their entitlements. Navigating this complexity can be much more difficult for those with low levels of English and / or computer literacy. For some families, this level of complexity creates a substantial barrier to ECEC access, and in some cases, means they choose not to access ECEC.



## Concerns about debt may reduce ECEC participation for some families

Families receiving CCS do not immediately get the full benefit of reduced out-of-pocket expenses when their child attends ECEC – as noted above, 5% of a family's CCS is withheld by Services Australia until the end of the financial year. The aim of this measure is to provide some protection for families from a potential CCS debt if they underestimate their annual income or misreport their activity hours. Families are required to report their estimated income and activity levels when applying for CCS. This reported income and activity level is then used to estimate their eligible CCS amount. Families are also expected to update their reported income and activity levels with any changes in their circumstances as these changes could impact their eligible amount of CCS. At the end of the financial year, a reconciliation occurs which takes into account a family's actual annual income and a CCS debt may arise if the family's income is higher than what was reported during the year. CCS debts can also arise, and CCS eligibility ceased, if a family has not lodged a tax return two years after the end of the financial year or have not notified Services Australia that they are not required to lodge. The withheld amount is used to either pay any CCS debts that arise during reconciliation or is refunded if there is no debt. The 5% withholding rate is set by default when families apply for CCS and can be changed up to two times a year. In the December 2022 quarter, the median withheld amount per child was about \$10 per week for families in the first five income deciles. For families in the sixth to ninth income deciles, the median withheld amount per child ranged between about \$6 and \$8 per week and falls to about \$2 per week for families in the tenth income decile (Productivity Commission estimates based on DoE administrative data (unpublished)). This makes sense given that lower-income households are eligible for higher amounts of CCS compared to higher-income households.

### The possibility of a CCS debt can discourage ECEC participation

The potential for a CCS debt however can discourage ECEC participation for some families. Families may have limited understanding of the intricacies of the CCS and therefore overestimate the potential for a CCS debt. And this even applies for families who are in receipt of CCS. For example, a survey of childcare users completed as part of the AIFS evaluation found that parents' self-reports indicated that the 5% withholding amount was the least well-understood aspect of the CCS (Bray et al. 2021, p. 44). Further, AIFS reported that about half the parents surveyed were worried about a CCS debt if they did not get their activity details right and about 40% were worried about the possibility of a CCS debt at reconciliation (Bray et al. 2021, p. 137). That said, during interviews with lower-income parents, there was a lower level of concern about the reconciliation process (Bray et al. 2021, p. 137) which suggests that concerns about debt were not concentrated at the lower part of the income distribution. Families yet to apply for CCS would likely have even less understanding of this aspect of the system. Concerns about debt may have also been heightened given Robodebt.

### Most families do not end up with a CCS debt

Data for 2021-22 also indicates that relatively few families incur CCS debts – among the 90% of families with reconciled incomes, 18% incurred a debt, with a mean debt of \$1,268 and a median of \$461 (Services Australia (unpublished)). For the 2019-20 financial year, under 18,000 families (about 1% of families receiving CCS) had not lodged their tax return two years later. As at 30 June 2023, about 40% of these families still had an outstanding debt with a mean amount of \$4,433 (Services Australia (unpublished)). For these families who had not lodged their tax return two years later, debts are likely to fall once they confirm their income because the amount of debt raised reflects the total amount of CCS that was paid to the family. Once a family confirms their income, the amount of CCS that they were entitled to will be deducted from the debt (further information about balancing and debt can be found in appendix D).

There is an incentive for families to reconcile their CCS entitlements at the end of the financial year because if they fail to do so by one year after the end of the financial year, they stop receiving CCS payments (DoE 2023b) and have to pay full fees for ECEC. Further, if a family does not confirm their income by two years after the financial year, their CCS eligibility is cancelled and they need to reapply to receive it again. CCS is also not backdated for the period before income is confirmed (DoE 2023b). However, as children age out of the ECEC system, families have less of an incentive to reconcile their CCS entitlements. This may partly explain why there are about 6,500 outstanding non-lodger debts for 2018-19 and 7,400 for 2019-20 (Services Australia (unpublished)). Non-lodger debts occur as a result of the customer not confirming their family income (lodging a tax return, or advising Services Australia they do not need to lodge a return for the applicable financial year) within two financial years of receiving CCS.

Similar to 2021-22, analysis of 2018-19 administrative data shows that relatively few families incur a CCS debt. Modelled estimates suggested that 32.5% of families with reconciled incomes had a debt with the mean level being \$638 per annum and the median \$225 but only half of these families (16.1%) had a debt in excess of the 5% withholding amount (with a mean level of \$1,059 and median of \$580) (Bray et al. 2021, p. 135). For this group, their debt represented on average (at the mean) 16.7% of benefits received with a median amount of 10.1% (Bray et al. 2021, p. 135). Although this is a substantial percentage of benefits, it is only a small percentage of income with the mean and median debt levels amounting to 0.6% and 0.4% of income respectively (Bray et al. 2021, p. 135). Further, the modelling estimated that lower-income families had virtually no CCS debt up to and including the third decile. CCS debt was estimated to be largest for the highest 5% of earners at around 0.9% of gross family income (Bray et al. 2021, p. 136).

A debt is more likely for higher-income families as a result of the structure of the CCS (as in the income thresholds, rates and tapers). For the 2021-22 financial year, approximately 243,000 families had a CCS debt (Services Australia (unpublished)). Information received from Services Australia shows that a higher proportion of high-income families (incomes over \$100,000) had a debt compared to lower-income families. 11% of families with a debt in 2021-22 had reconciled incomes below \$100,000 (Services Australia (unpublished)). 55% of families with a debt had reconciled incomes between \$100,000 and \$200,000 and 34% families with a debt had reconciled incomes over \$200,000 (Services Australia (unpublished)).

### **Families can also incur debts to ECEC services**

A range of reasons can give rise to family debts to ECEC services, including:

- delays in processing CCS applications
- third party software and Services Australia generating incorrect or inconsistent information
- families not understanding the two stage enrolment process and not confirming their enrolment
- when back pay of CCS is made directly to the families rather than to services and services are unable to recover it from families
- when subsequent ACCS applications are not approved but the family continue to use the same number of ECEC hours (Bray et al. 2021, pp. 137–138).

Guidance from Services Australia states that services should charge full fees until a CCS application has been approved. However, in reality, many services charge families based on what they estimate will be their CCS eligible amount as many families do not have the financial resources to pay full fees. A debt could then arise either due to a misalignment with a service's estimate of CCS eligibility and a family's actual eligibility or due to delays in processing CCS applications beyond the 28 day limit of backdating CCS (Bray et al. 2021, pp. 137–138). Services were further concerned with the wellbeing and safety of the child if services pursued recovering the debt (Bray et al. 2021, p. 138).

The issue of backdating will be partially addressed through 2023-24 Budget measures that expand the exceptional circumstances criteria that can be applied to applications to backdate ACCS (Child Wellbeing) by more than 28 days (Australian Government 2023, p. 98).

Families may also incur debts to ECEC services as a result of unsubsidised hours. As discussed earlier, families eligible for fewer hours of subsidised ECEC tend to have lower incomes and also tend to accrue a higher number of unsubsidised care hours. Families receive no subsidy for unsubsidised hours which means that families are liable for the full fee for those hours. Given this, these families may not have the financial ability to pay for ECEC which may result in a debt to the service.

### **Overall there is scope to improve current subsidy arrangements**

For most families, the CCS is effective in improving ECEC affordability especially for families who have a reasonable level of income and consistent, stable and predictable working hours. However particular cohorts within the population face larger affordability barriers – including families with low incomes, Aboriginal and/or Torres Strait Islander families and families from culturally and linguistically diverse backgrounds, families with certain structures (including single parent and multiple birth families) and families who have restricted residency in Australia and are not eligible to receive CCS.

The activity test and administrative complexity also present barriers for certain cohorts within the population, such as families where parents or guardians work variable and unpredictable hours and those from culturally and linguistically diverse backgrounds. The complexity of the design of the CCS and difficulties navigating the CCS system make it challenging for some families to understand and access subsidised ECEC which may discourage ECEC participation.

The potential for CCS debt can also discourage ECEC participation for some families although the AIFS evaluation found that lower-income households were less likely to incur a CCS debt and were less concerned about a potential CCS debt (Bray et al. 2021, p. 137).

## **6.3 Improvements to subsidy arrangements would assist families with affordability**

Many changes could be made to subsidy arrangements to improve affordability for families. Some relate to the design of the CCS and the calculation of subsidy entitlements; others involve simplifying the system to make CCS easier to understand.

### **Improving affordability by adjusting the design of the CCS**

The Commission has considered a suite of adjustments to the design of the CCS that could improve affordability. Most build on each other, providing higher levels of support for families at each step (table 6.4). The first option relaxes the activity test and the second couples that change with a lift in the subsidy rate for lower-income families (those earning up to \$80,000 a year) to 100% of the hourly fee, up to the hourly rate cap. Subsequent options add highly subsidised ECEC for all other families (those earning more than \$80,000 a year) to the policy mix. These changes will primarily affect families with children aged 0–5 years, and the preliminary modelling focuses on this cohort.

In line with the terms of reference to consider a universal 90% subsidy, a policy option where the only change to current settings is an increase in the CCS rate to 90% of the hourly fee, up to the hourly rate cap, for all families (option six) is also modelled.

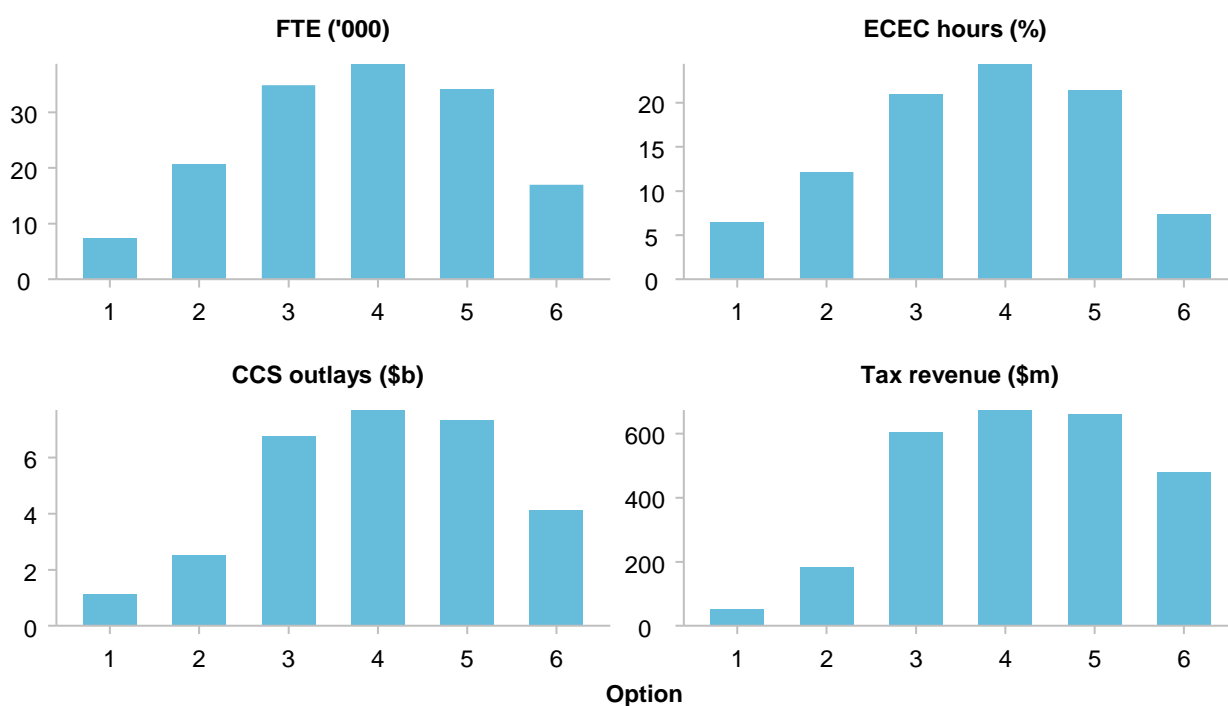
The Commission has undertaken preliminary work to estimate the changes in labour force participation, demand for ECEC and net costs to government that might stem from each option (box 6.5). As levels of support to families rise, so too do each of these outcomes (figure 6.14).

**Table 6.4 – Modelled Child Care Subsidy policy options**

Option	CCS rate	Higher CCS rate	Activity test	CCS hourly rate cap
<b>1: Relax the activity test for all families and retain income testing</b>	No change – based on current income test for all days of ECEC	No change	None for three days of ECEC per week (72 hours per fortnight), and no change for days four and five	No change
<b>2: Relax the activity test for all families, and increase the subsidy for low-income families</b>	100% for families with incomes under \$80,000 No change for other families	100% for families with incomes under \$80,000 No change for other families	For all families, none for three days of ECEC per week (72 hours per fortnight), and no change for days four and five	No change
<b>3: 90% subsidy for three days for all families, relax the activity test, and increase subsidy for low-income families</b>	100% for families with incomes under \$80,000 For other families, 90% for three days of ECEC (72 hours per fortnight) and current income test for days four and five	100% for families with incomes under \$80,000. For other families, at least 90%, and highest rates above 90% remain as they are for three days, and current income test for days four and five	For all families, none for three days of ECEC per week (72 hours per fortnight), and no change for days four and five	No change
<b>4: 90% subsidy for all, remove the activity test, and increase subsidy for low-income families</b>	100% for families with incomes under \$80,000 For other families, 90% with no income test	100% for families with incomes under \$80,000 For other families, at least 90%, and highest rates above 90% remain as they are	None	No change
<b>5: Free ECEC for low-income families, flat fee ECEC expense per day of \$10 for other families, no income test or activity test</b>	None – free for families with incomes under \$80,000, and flat fee for other families	None	None	None
<b>6: 90% subsidy for all</b>	90% for all families	No change	No change	No change

**Figure 6.14 – Changing the CCS setting results in an increase in ECEC use – but comes at a cost<sup>a,b</sup>**

**Results of preliminary modelling of different options for changes to the CCS**



**a.** Results based on preliminary modelling of changes to the CCS, as outlined in table 6.4. Box 6.5 details the method and assumptions behind these results. **b.** FTE: full-time equivalent workers.

Source: Productivity Commission estimates.

While all these options come at a cost to taxpayers, some changes are necessary to enable universal access and address shortcomings in the CCS.

The Commission recommends that the Australian Government implements the two policy changes underpinning option two – relaxing the activity test and lifting subsidies for lower-income families – as this will most likely deliver benefits to Australian children, families and the broader community that exceed the costs of policy change. The suite of options are discussed in more detail below.

### **Box 6.5 – Preliminary modelling of changes to the CCS**

Preliminary modelling of changes to the CCS was undertaken to estimate the effects of potential policy changes on labour supply, ECEC demand and fiscal costs (appendix F). The approach involved estimating changes in out-of-pocket expenses that would arise from policy changes, for families with children aged 0–5 years in the ABS 2019-20 Survey of Income and Housing data. Then ‘elasticities’ from the literature were applied to estimate how families might respond by increasing hours of work and hours of ECEC. It is assumed that those who are not working or not using ECEC make decisions about work and ECEC in an increment of three days, while those who are already working or using ECEC consider the change in out-of-pocket expenses over up to two days if they are using one day of ECEC, and one day if they are using two to four days of ECEC.

Elasticities were drawn from Gong and Breunig (2017, p. 32), which estimated that a 1% fall in out-of-pocket expenses increases:

- hours of ECEC by 0.203% and ECEC participation by 0.125%
- hours of work by 0.081% and labour force participation by 0.055%.

These elasticities indicate that families’ decisions about hours of ECEC are more responsive than hours of work to changes in out-of-pocket expenses. This is because some families who are already working replace informal care with formal ECEC after ECEC becomes cheaper. And some families use ECEC for reasons other than work (such as for study, volunteering, housework or social activities). Further, hours of ECEC are typically lower than hours of work, which means that the same hours increase can appear as a larger percentage increase for hours of ECEC due to its lower base.

Fiscal costs were estimated by applying proportional increases in aggregate CCS outlays, as estimated using the survey data, to CCS outlays estimated by the Department of Education for 2023-24. These costs were adjusted based on the Productivity Commission’s analysis of the Department’s administrative data, to account for the observation that assumptions made using the survey data tended to overstate the number of unsubsidised hours of care that families have under the activity test.

The results are sensitive to a range of assumptions, such as the elasticities used and the number of extra days of work and care over which families consider their change in out-of-pocket expenses. A wide range of elasticities have been estimated and used in the literature – a doubling of elasticities implies an hours of ECEC or hours of work response that is double the size for every 1% fall in ECEC expenses.

The model has a number of limitations. It is assumed that increases in ECEC demand and labour supply are fully accommodated by the ECEC and labour markets, without any changes in ECEC fees or wages. The model is also not able to take into account broader benefits – such as benefits of reducing system complexity, educational benefits to children, benefits that easier access to ECEC may have in searching for a job, and longer term benefits of increased labour force participation including on skill development, productivity and reduced reliance on welfare payments.

While this technique improves on some past analysis of CCS policy changes that only examine the effects of some components of the CCS regime, or that are estimated for much broader groups of families, more sophisticated modelling options exist. The Productivity Commission’s final inquiry report will include updated estimates of the effects of CCS policy changes by using a behavioural microsimulation model. This models individual families’ decisions to choose work and care hours through preferences that are unique to the family’s characteristics, rather than by applying broad-based elasticities.



## **A modified activity test would enable more families experiencing vulnerability to access ECEC**

Modifying the activity test, such that all families can access at least three days (up to 30 hours) of subsidised ECEC a week, would relax the requirement that ties children's participation in ECEC to their parents' or guardians' activity. Income testing and the CCS hourly rate cap would remain in place under this option. Activity testing should also remain for families who wish to use more than 30 hours of ECEC per week.

Similar recommendations have been made in other recent inquiries into ECEC, for example:

- the draft recommendation in the ACCC Childcare inquiry's interim report released in September 2023 noted that consideration should be given to 'removing, relaxing or substantially reconfiguring the current activity test, as it may be acting as a barrier to more vulnerable children ... accessing care and creating a barrier to workforce entry or return for some groups' (ACCC 2023b, p. 30)
- the final report of the South Australian Royal Commission into ECEC recommended that the Australian Government change the CCS to 'enable all families to access up to three days a week of care without the need to meet any activity test' (SA Government 2023, p. 7)
- the interim report of the NSW Independent Pricing and Regulatory Tribunal's Review of ECEC found that the activity test particularly affects low-income families who are Aboriginal and/or Torres Strait Islander, and/or who are living in remote areas, with a draft recommendation that the activity test 'should be reviewed as a priority' (2023, p. 3).

Although the activity test was intended to increase labour force participation, it is unclear if it has had this intended effect, and it makes it harder for some families to participate in ECEC (section 6.2).

Relaxing the activity test would improve affordability for families who were previously allowed fewer than 30 hours of subsidised ECEC per week (typically lower-income families). These families are currently charged the full fee for any hours of care used over their subsidised entitlement. It will mean that fewer families are charged for unsubsidised hours and more families are able to access subsidised ECEC. Improving affordability would encourage these families to use more ECEC, enabling them to spend more time on other activities, including working.

The preliminary modelling<sup>23</sup> finds that relaxing the activity test leads to an estimated 1.2% increase in total hours worked by single parents and secondary workers in couple families with young children – the equivalent of 7,300 full-time employees. A larger increase of 6.5% is estimated for the total hours of formal ECEC attended by children. Most of this increase is estimated to arise from families who were not previously using ECEC prior to the policy change. There is a slight increase in estimated ECEC hours by families who were already using ECEC, who experience a fall in out-of-pocket expenses due to having fewer unsubsidised hours (figure 6.15).

Beyond increasing subsidised hours, modifying the activity test would have benefits that are not captured by the modelling. It would reduce some of the administrative complexity of the CCS, making it easier for families to understand their eligibility for subsidised ECEC. This is particularly important for families with variable patterns of work (such as people in casual jobs), who may be more likely to find the current activity test challenging to understand and/or administratively burdensome (section 6.2). It would also lessen families' concerns about incurring CCS debt if their hours of activity change and provide people who are looking for work greater certainty in their access to a number of hours of subsidised ECEC while they are searching for a job. Impact

<sup>23</sup> It is assumed in this modelling scenario that current tiers of the activity test are removed, such that all families can access 72 hours of subsidised ECEC per fortnight (36 per week on average). This would enable all families to access at least three days of subsidised ECEC per week.

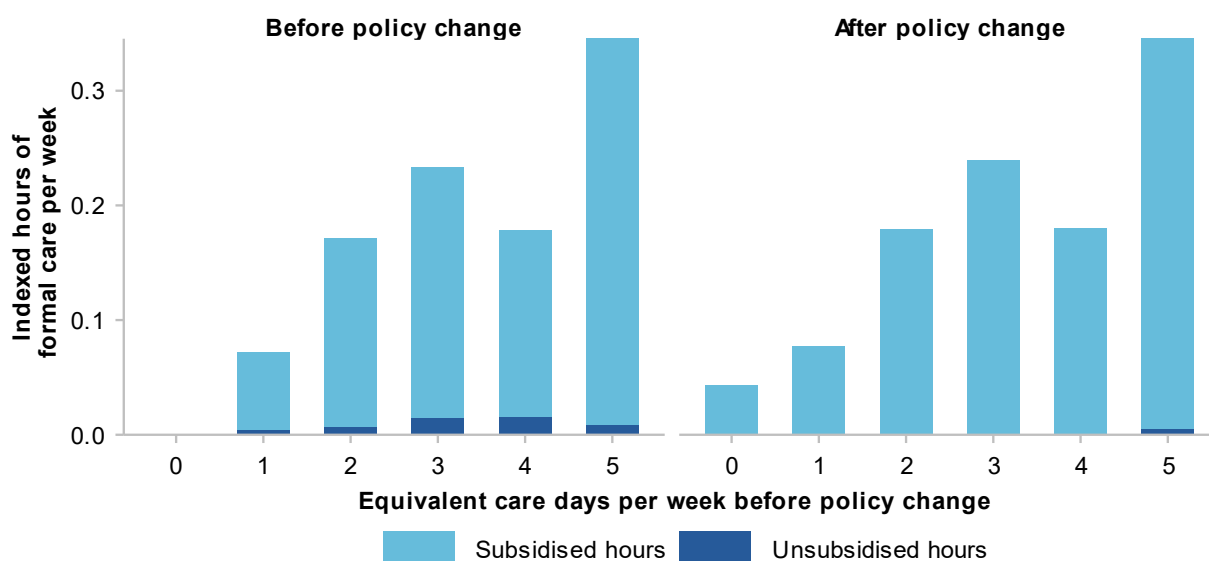
Economics and Policy (2023, pp. 5, 26–27) estimated that allowing all children to access three days of ECEC would increase labour force participation by about 40,000 women through reducing job search costs.

Relaxing the activity test would also assist in enabling children to attend ECEC consistently as families would continue to receive subsidised ECEC for three days even if their activity levels drop temporarily. Attendance in ECEC would support educational outcomes for children, particularly for children from families experiencing disadvantage who may be more highly affected by the activity test.

At the same time, activity testing for parents seeking more than 30 hours of ECEC would retain some of the labour force participation incentives that underpin the activity test, by offering a larger number of subsidised hours to families with higher activity levels, including time spent working. While some parents could choose to reduce their work hours due to not having to meet an activity test, the evidence for this is uncertain given that past tightening of the activity test did not substantially raise labour force participation (section 6.2).

**Figure 6.15 – Many unsubsidised hours of ECEC would become subsidised by relaxing the activity test<sup>a,b</sup>**

**Estimated indexed number of ECEC hours before and after relaxation of the activity test, by subsidised hours status and by equivalent care days before the policy change**



**a.** Equivalent care days calculated as weekly formal care hours divided by 10, rounded up. **b.** Hours of formal care per week are indexed to a value of one for the total care hours before policy change.

Source: Productivity Commission estimates.

The Australian Government could consider phasing the introduction of a modified activity test, for example, starting with lower-income families, in order to allow time for supply to respond to increased demand and to evaluate the effects of the change before relaxing the activity test more widely.

Overall, the increase in costs to the Australian Government associated with this policy change are estimated to amount to \$1.1 billion per year, or about 9% of the estimated CCS outlay for 2023-24.<sup>24</sup> Lower-income families benefit most from the change; families within the lowest 20% of the income distribution account for about half of the increased costs to government. Relaxing the activity test will also affect higher-income families who are not eligible for subsidised hours under current arrangements because they do not meet the

<sup>24</sup> This compares to an estimate by Impact Economics and Policy (2023, p. 28) of \$1.3 billion for abolishing the activity test.



activity test. These families account for about one fifth of the estimated increase in total hours of care. However, because these families have higher incomes, and therefore lower subsidy rates, the costs to government of their increase in ECEC participation are relatively low.

To a small extent, the increased costs to government will be offset through a rise in tax revenue as parents work more. Income tax revenues from increased labour force participation are estimated to be about \$53 million per year. Associated falls in transfer payments were not estimated as part of the preliminary modelling, but are also expected to occur because income testing means that families' entitlements to transfer payments taper down as their incomes increase (examples demonstrating this are in appendix D).

Although three days of care has been characterised as 30 hours above, in practice 30 hours could be spread across more or fewer than three full days depending on daily session lengths. Many families are charged for hours that they do not use. Creating incentives for session lengths to match children's attendance would help to ensure that these subsidised hours are spread across actual hours of attendance. The Commission is considering ways to encourage services to offer greater flexibility around session lengths (paper 7).

The Commission is also considering the levels of activity that should be required for hours above 30 hours of subsidised ECEC per week (or 60 hours per fortnight), and is seeking input on the relative merits of different options. Some options could include:

- retaining the current activity test for hours of care over 60 hours per fortnight. This would allow 60 subsidised hours for all families, up to 72 hours of subsidised hours for families with 16 to 48 activity hours per fortnight, and up to 100 hours of subsidised care for those with more than 48 activity hours. While this is a simplification of the current activity test, it would still retain some complexity. Further, the level of activity required at the first tier of the activity test (at least 16 hours) would be more than the increase in subsidised hours at that tier (an increase of 12 hours, from 60 to 72 hours per fortnight)
- simplifying the number of activity test tiers further by allowing 60 subsidised hours for all families and up to 100 subsidised hours for those with more than 48 activity hours. However, this would penalise families who are currently eligible for up to 72 hours of subsidised care due to having 16 to 48 hours of activity
- simplifying the number of activity test tiers by allowing 72 subsidised hours for all families and up to 100 subsidised hours for those with more than 48 activity hours. This would allow families using session lengths of less than 12 hours a day to access more than the three days of subsidised care per week.



### Information request 6.1

The Commission is seeking views on the costs and benefits of options to modify the Child Care Subsidy activity test. Draft recommendation 6.2 would relax the activity test to allow all families to access up to 30 hours of subsidised care a week (60 hours per fortnight) regardless of activity, providing a step towards universal access. Options for the levels of activity that should be required for hours above 60 hours of subsidised care per fortnight could include:

- retaining the current activity test for hours of care over 60 hours per fortnight. This would allow 60 subsidised hours for all families, up to 72 hours of subsidised hours for families with 16 to 48 activity hours per fortnight, and up to 100 hours of subsidised care for those with more than 48 activity hours
- simplifying the number of activity test tiers further by allowing 60 subsidised hours for all families and up to 100 subsidised hours for those with more than 48 activity hours
- simplifying the number of activity test tiers by allowing 72 subsidised hours for all families and up to 100 subsidised hours for those with more than 48 activity hours.

The introduction of a modified activity test could also be phased, for example, starting with lower income families, in order to allow time for supply to respond to increased demand and to evaluate the effects of the change before relaxing the activity test more widely. The Commission is seeking views on the costs and benefits of a phased introduction, and which cohorts of families would benefit most from being able to access a relaxed activity test earlier.

## **Making ECEC free or low cost for low-income families would encourage new enrolments**

As noted above, the CCS leads to relatively high out-of-pocket expenses for the lowest income families (figure 6.1). And while out-of-pocket expenses as a share of income are reasonably similar for many cohorts, that does not mean that they affect families equally. Out-of-pocket expenses equal to 10% of income can represent a larger financial burden for a family earning \$80,000 per year for example, than one with an income of \$200,000 per year. In other words, ECEC is relatively more expensive for those who can least afford it. This is likely contributing to lower participation rates in ECEC for lower-income families.

An increase in the top subsidy rate to 100% of the fee up to the hourly rate cap for lower-income families (those earning up to \$80,000 per year) would reduce their out-of-pocket expenses; in some cases, where charged hourly rates are below or equal to the hourly rate cap, ECEC use will be free for these families. In implementing this policy change, all families who hold a Health Care Card should automatically receive the 100% subsidy rate, reducing administrative complexity. The Commission is investigating further options to reduce administrative complexity (discussed below).

As described in section 6.2, the experience of the COVID-19 period – when ECEC was free for all families without a need to demonstrate eligibility – showed that a reduction in out-of-pocket expenses and administrative complexity likely encouraged more families experiencing disadvantage to enrol their children in ECEC (Wong et al. 2021, pp. 10–11). Similar to the changes in the activity test, this is likely to support better educational outcomes for children, and may also have benefits for their families, as using ECEC may enable them to find work or link them to additional support services.

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Currently, the top rate of CCS is 90% of the hourly rate cap and applies to families with incomes of up to \$80,000 per year, and the HCCS rate for these families is 95%. Raising the subsidy level for both the CCS and HCCS for families earning up to \$80,000 per year will have implications for the way in which rates taper down from 100%. The Commission will consider this further for the final report. A balance is needed between avoiding taper rates that are too steep (which can result in greater workforce disincentive effects) and taper rates that are too low (which can lead to families on high incomes having relatively high subsidies, and the fiscal consequences associated with that). The Commission is also considering a simplified tapering of HCCS to be more closely aligned to the CCS (discussed further below).

Preliminary modelling was done on the potential effects of increasing the top subsidy rate to 100% for families with incomes up to \$80,000 per year, in addition to relaxing the activity test. Among the modelled population, 30% of families with children aged 0–5 have incomes up to \$80,000 per year. Under this policy option, it is assumed that CCS and HCCS rates for families with incomes over \$80,000 per year are equivalent to current subsidy rates.

The policy changes are estimated to lead to a 3.4% increase in total hours worked (equivalent to 20,700 full-time employees) by single parents and secondary workers in couple families with young children. Hours of formal ECEC are estimated to increase by about 12%, with about two-thirds of the increase attributed to families who were not previously using ECEC. The fiscal cost of reforming the activity test and lifting the CCS rate for lower-income families is estimated to be about \$2.5 billion per year or a 20% increase on the estimated CCS outlay for 2023-24, partly offset by income tax collections of about \$180 million per year. The lowest family income quintile is estimated to receive more than half of the total increase in CCS expenditure across all families.

Reducing out-of-pocket expenses for some families could reduce their sensitivity to fee increases. Some providers might take the opportunity to raise fees more rapidly than they might otherwise have done, particularly in areas where many lower-income families live (or where there are few higher-income families who may change services if fee rises are excessive). The Australian Government should monitor changes in fees and out-of-pocket expenses on a regular basis to identify areas where movements are out-of-step with the sector norm. Increases that vary markedly from the norm should prompt closer investigation, and a regulatory response should be considered if they are not reasonable. To inform judgements about what reasonable increases might look like, the Australian Government should commission a detailed investigation of costs and profits across the sector every three years, along the lines of the work that the ACCC has been undertaking. This work will also signal if the hourly rate cap needs to be reset (described further below).



### Draft finding 6.3

#### CCS changes would reduce affordability barriers for lower income families

Many changes could be made to subsidy arrangements to improve affordability for families. The Commission has considered a suite of options to identify their effects on labour force participation, demand for ECEC and net costs to government, and their effectiveness in achieving universal access to ECEC.

Relaxing the activity test for all families and lifting subsidies for lower income families would target support to children and families who would benefit the most. Alongside improving availability, inclusion and flexibility, these changes to the Child Care Subsidy (CCS) would enable universal access to ECEC.

Preliminary modelling shows that relaxing the activity test for all families to allow at least three days of subsidised ECEC per week, and lifting the CCS rate to 100% for families with children aged 0–5 years who have incomes up to \$80,000, would increase:

- total hours of ECEC demanded by 12%
- hours of work by single parents and secondary earners in couple families with young children by 3.4% (or the equivalent of 20,700 full-time workers)
- Australian Government outlays on the CCS by 20% or \$2.5 billion per year.

Over half of the resulting increase in CCS expenditure would benefit families whose income is in the lowest 20% of the income distribution.



### Information request 6.2

The Commission is seeking views on how Child Care Subsidy taper rates could be designed if the top rate of subsidy was increased to 100% of the hourly rate cap, as proposed in draft recommendation 6.2. This includes options to adjust taper rates for the Higher Child Care Subsidy, available to families with multiple children aged five or younger in ECEC who are eligible for a subsidy.

## Resetting and indexing the hourly rate cap to better reflect costs of provision

Under the current CCS design, affordability for families becomes more challenging when fee growth outstrips increases in the hourly rate cap. While hourly rate caps are adjusted annually based on the CPI, labour costs are the biggest driver of ECEC costs, and labour costs have increased much faster than inflation over the past five years (ACCC 2023b, p. 30). Services increase fees to offset increases in operating costs and to maintain profits and surpluses. This has led to an increase in the proportion of CBDCs and FDCs charging above the hourly rate cap – for example, from 13% to 22% between 2018 and 2022 for CBDCs (ACCC 2023b, p. 167).

Resetting the hourly rate cap for each service type to better reflect costs of provision and changing the indexation approach to prevent the cap rising more slowly than provider costs (and, therefore, fees) would help to sustain affordability. The ACCC made a similar suggestion in its recent interim report, recommending that consideration be given to ‘determining an appropriate base for the rate cap and indexing the cap to more closely reflect the input costs relevant to delivery of childcare services’ (ACCC 2023b, p. 30).

But how should a new hourly rate cap be determined, and how should that figure be indexed going forward? As part of its Childcare inquiry, the ACCC has developed a database of costs from ECEC services (ACCC 2023b, p. 30). This could be used to estimate average efficient costs of provision, as a basis for determining the new hourly rate cap. Productive efficiency means that providers are able to deliver their services at the desired quality using the least amount of resources necessary to do so. Periodic review of fees and costs would help to ensure that there is regular oversight of these key determinants of ECEC affordability (as discussed above), and the reviews could inform adjustments in the hourly rate cap. In between any major adjustments to the hourly rate cap, indexation should better reflect changes in costs of providing ECEC. Indexation based on the Wage Price Index could be an option, given the importance of labour costs to providing ECEC services. A composite index could also be considered. The Commission is seeking views on ways to set and index the hourly rate cap.

The ACCC has also suggested considering rate caps that align with pricing practices for different service types, such as having a daily fee cap for CBDC instead of an hourly rate cap. The Commission considers that it is important that families have the flexibility to access shorter session lengths to promote affordability and ensure that taxpayer dollars are used efficiently. Creating stronger incentives for services to offer variable session lengths to match children's actual attended hours, and allowing remaining opening hours to be filled by other children (paper 7), would be preferred to introducing a daily fee cap.



#### **Draft recommendation 6.1** **Monitor rises in fees and out-of-pocket expenses**

The Australian Government should monitor changes in fees and out-of-pocket expenses on a regular basis to identify services where movements are out of step with sector norms. Increases that vary markedly should prompt closer investigation, and a regulatory response should be considered if they are not reasonable. To inform judgements about what reasonable increases might look like, the Australian Government should commission a detailed investigation of costs and profits across the sector every three years, along the lines of the work that the Australian Competition and Consumer Commission has been undertaking. This work would also signal if the hourly rate cap needed to be reset.



#### **Information request 6.3**

The Commission is seeking information on how the level and indexation of the Child Care Subsidy's hourly rate cap could be adjusted to better reflect costs of provision over time, including a higher hourly rate cap for non-standard hours, as proposed in draft recommendations 6.2 and 7.3.

### **Other options for CCS reform**

The terms of reference for this inquiry asked the Commission to consider a universal 90% subsidy rate. This would represent a significant change to the current system, as only children from low-income families currently have at least 90% of their ECEC fees subsidised.

Lifting subsidies for all families to at least 90% of the fee, up to the hourly rate cap, for three days of ECEC per week in addition to relaxing the activity test and a 100% subsidy for lower-income families (option three),

is estimated to lead to a 5.7% increase in total hours worked by single parents and secondary workers in couple families with young children, or 34,900 full-time workers. Total hours of formal ECEC are estimated to rise by 21%. This policy change is also estimated to add \$6.8 billion per year to government outlays on the CCS, an increase of 53%, and income tax collections are estimated to increase by \$600 million per year.

Further extending the 90% subsidy regime to five days, along with complete removal of the activity test (option four), is estimated to increase total hours worked by 6.3% (38,700 full-time equivalents), hours of ECEC by 24% and CCS outlays by \$7.7 billion per year, or 61%. Income tax collections are estimated to increase by \$670 million per year.

The fifth option considered, a flat daily fee, is used in parts of Canada and has the advantage of giving families certainty over ECEC expenses. The option modelled of a daily flat fee of no more than \$10 is estimated to increase total work hours by 5.5% (34,100 full-time equivalents) and total ECEC hours by 21%. CCS outlays are estimated to increase by \$7.3 billion per year, or 58%, and income tax collections by \$660 million.

If the only policy change were to extend a CCS rate of 90% of the fee up to the hourly rate cap to all families (option six), it is estimated that total hours of work by single parents and secondary workers in couple families with young children would rise by 2.8% (or the equivalent of 17,000 full-time equivalent workers). Hours of ECEC are estimated to increase by 7.4% and fiscal costs would rise by \$4.1 billion a year (or about one third), partly offset by higher income tax collections of \$480 million.

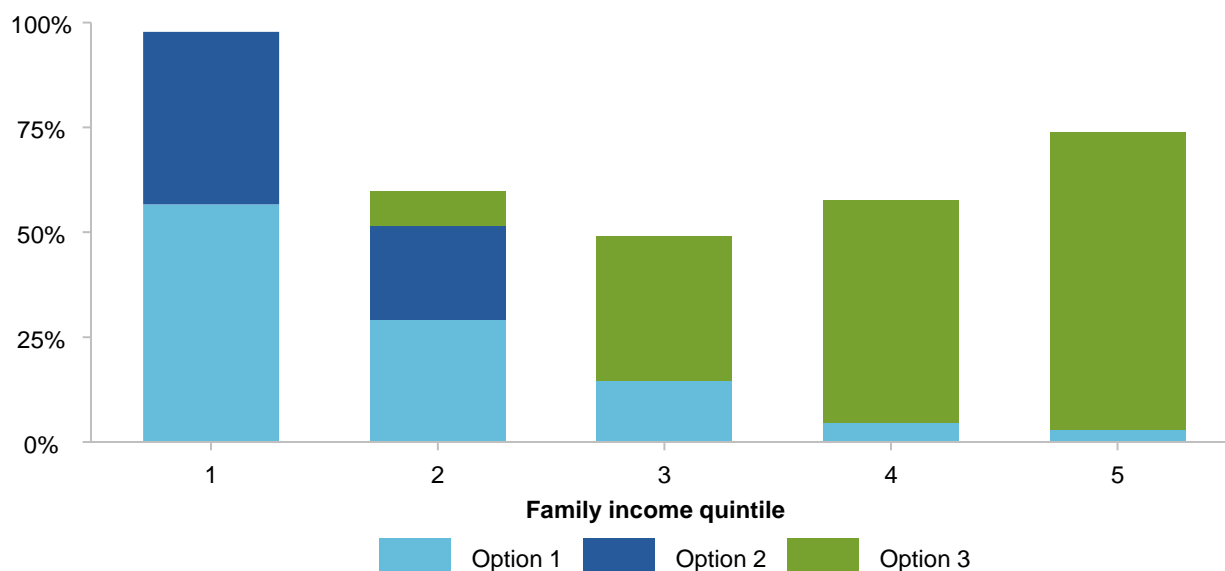
If the only reform implemented was either a 90% subsidy rate or a flat fee by (that is, with no change to the activity test or further increases to the subsidy rate for lower-income families), the main beneficiaries would be high-income families. This is because low-income families are already eligible for a 90% subsidy rate for the hours that they are allowed under the activity test, and would have similar out-of-pocket expenses under the option of a flat fee. In the absence of other policy changes, moving to a 90% subsidy rate for all families would have no benefit for lower-income families. Nearly 60% of the estimated increase in government outlays of \$4.1 billion a year would accrue to the 20% of families on the highest incomes (those earning \$200,000 and above per year) and nearly 30% to the second highest 20% (those earning between about \$150,000 and \$200,000 per year).

Combining a 90% subsidy rate or flat fee system with more targeted assistance aimed at lower-income families and relaxation or removal of the activity test (options three, four and five), would enable the benefits to be more evenly spread across different income groups.

Under option three, the 20% of families with the lowest incomes and the 20% with the highest (the lowest and highest income quintiles) experience the largest estimated falls in out-of-pocket expenses (figure 6.16). The highest income families would benefit considerably more from the rise in CCS expenditure, accounting for 35% of the increase compared with 23% for the lowest income families, because they use a larger number of hours of ECEC (figure 6.17). The estimated percentage increase in hours worked is highest for the lowest income parents under this option, as they have more scope to increase their work hours than the highest income families (figure 6.18).

**Figure 6.16 – A 90% subsidy would benefit high-income families most while low-income families benefit from relaxing the activity test and targeted subsidies<sup>a,b</sup>**

**Incremental fall in weekly out-of-pocket ECEC costs based on baseline ECEC usage (%)**

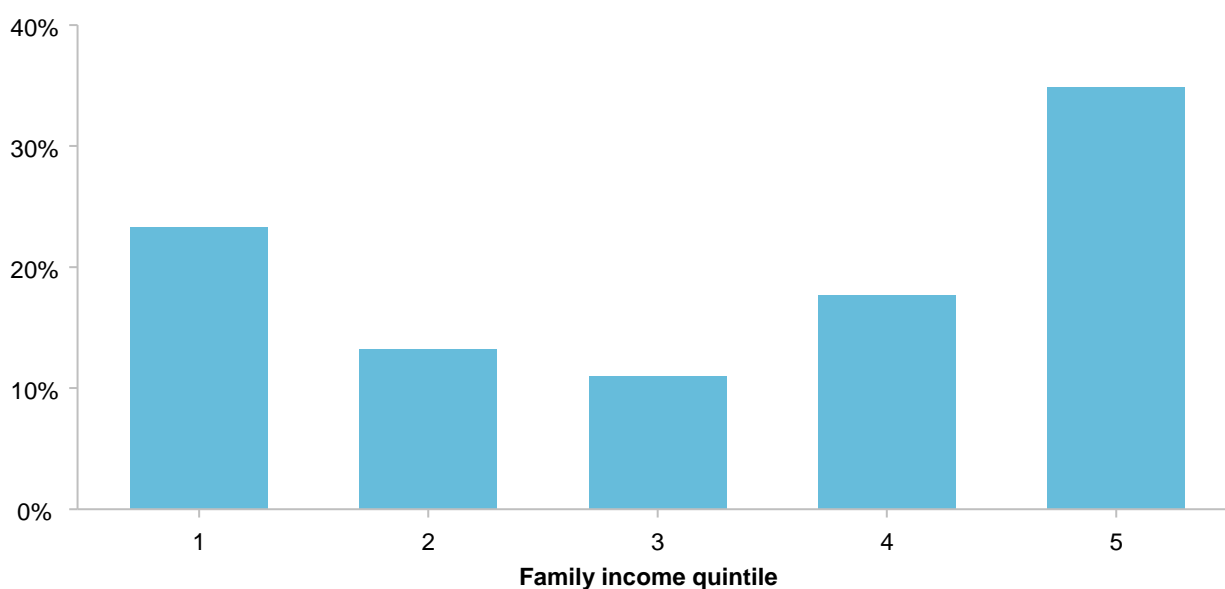


**a.** This policy change involves removing the first three tiers of the activity test (option one), raising subsidies for lower income families to 100% (added in option two), setting the subsidy for all other families at 90% for up to 72 hours of ECEC per fortnight for the first child and up to 95% for subsequent children, and the current subsidy regime for any hours over 72 per fortnight (added in option three). **b.** Family income quintiles are up to about \$60,000, \$100,000, \$150,000 and \$200,000, and over about \$200,000 for the fifth quintile.

Source: Productivity Commission estimates.

**Figure 6.17 – High income families would receive the largest share of increased CCS expenditure under option three<sup>a</sup>**

**Share of increased CCS expenditure attributed to families by income quintile (%)**



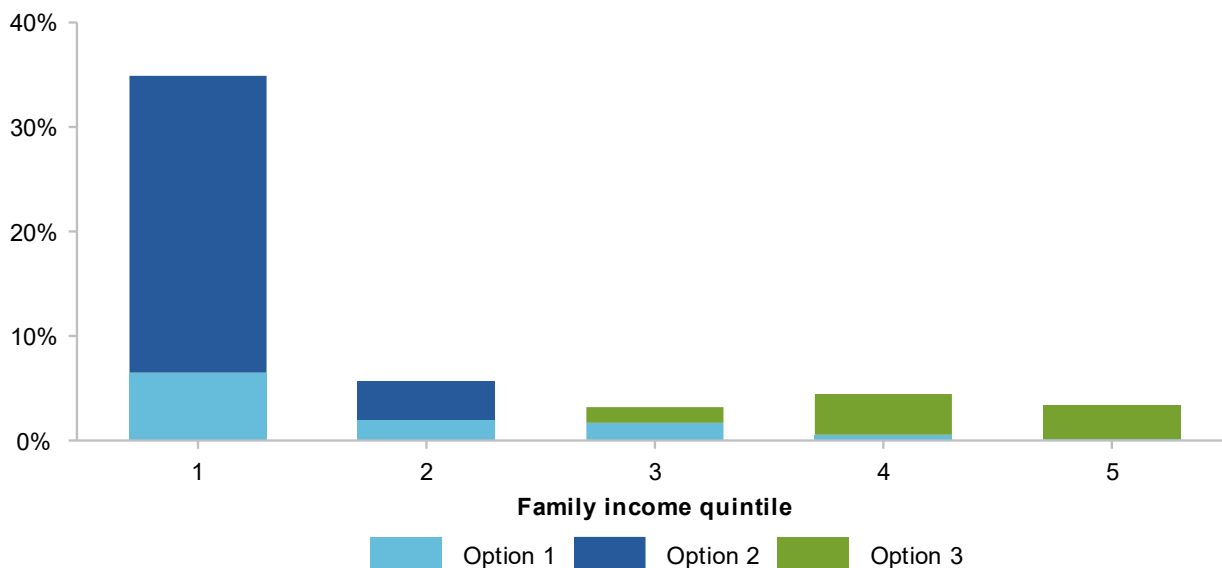
**a.** See figure 6.16 notes.

Source: Productivity Commission estimates.



**Figure 6.18 – Parents in the lowest income quintile would have the largest increase in their hours of work as a result of relaxing the activity test and targeted subsidies<sup>a,b</sup>**

**Incremental increase in hours worked under modelling of options one to three (%)**



a. See figure 6.16 notes. b. Incremental results in this chart are adjusted to sum to the overall change in hours worked for option three. Unadjusted results may not sum to the total for option three because of probabilities that were applied to determine which families begin working, that can lead to different families entering work under different modelled options.

Source: Productivity Commission estimates.



**Draft finding 6.4**

**Broad-based CCS changes would make ECEC more affordable for all families but come at a substantial cost to taxpayers**

Broad-based changes to the Child Care Subsidy (CCS) would reduce out-of-pocket expenses for all families and support larger increases in labour force participation – but come at a substantial cost to taxpayers.

For example, if in addition to relaxing the activity test and increasing the CCS rate for lower income families, the Australian Government were to extend a subsidy rate of 90% of the fee, up to the hourly rate cap, to all families for three days of ECEC a week, it is estimated that this would increase:

- total hours of ECEC demanded by 21%
- hours of work by single parents and secondary earners in couple families with young children by 5.7% (or the equivalent of 34,900 full-time workers)
- Australian Government outlays on the CCS by 53% or \$6.8 billion per year.

Preliminary modelling results show that policy options extending the 90% subsidy rate to all ECEC users or introducing a flat fee of \$10 a day have similar implications for labour force participation, demand for ECEC and net costs to government.

These options are more costly than a policy option that includes relaxing the activity test and increasing subsidy rates for lower income families. In addition, a disproportionate share of the increased government support would go to high income families – rather than to those experiencing disadvantage, who are most likely to benefit from greater access to ECEC.



### Draft finding 6.5

#### Lower income families would not benefit if the only change to the CCS were a 90% subsidy rate for all families

In line with the request in the terms of reference to consider a universal 90% subsidy, the Commission has assessed the potential effects of a policy option where the only change to current settings is that the Child Care Subsidy (CCS) rate increases to 90% of the hourly fee, up to the hourly rate cap, for all families.

It is estimated that this policy change would increase:

- total hours of ECEC demanded by 7.4%
- hours of work by single parents and secondary earners in couple families with young children by 2.8% (or the equivalent of 17,000 full-time workers)
- Australian Government outlays on the CCS by 33% or \$4.1 billion per year.

The policy change would have no benefit for low-income families, who are already eligible for a 90% subsidy rate. Nearly 60% of the increase in government outlays would accrue to the 20% of families on the highest incomes (those earning \$200,000 and above) and nearly 30% to the second highest 20% (those earning between about \$150,000 and \$200,000).

### Reforms with the largest benefits relative to the cost should be prioritised

Implementing option two – relaxing the activity test and lifting subsidies for lower-income families – would target the increase in support to the children and families who would benefit the most.

Higher levels of support (options three, four and five) would generate a somewhat stronger labour market response from parents, and potentially other social benefits including increasing gender equality and making more effective use of people's skills and education, but at a much higher additional cost to taxpayers. A disproportionate share of the increased government support (35% under option three, for example) would go to higher-income families (those currently earning about \$200,000 per year and above) and there would be more children from higher-income families increasing their participation in ECEC relative to option two. As described above, children experiencing disadvantage tend to experience greater improvements in educational outcomes as a result of attending quality ECEC, so increasing participation in ECEC for children from higher-income families may have more muted longer-term benefits relative to the increase in costs.

Overall, increasing the CCS rate to a universal 90% or introducing a flat fee for ECEC is likely to disproportionately assist high-income families, who already spend a lower proportion of their income on out-of-pocket ECEC expenses when compared to families in the lowest income decile. These options are costly but do not lead to significant increases in labour force participation, address the inequity created by the current CCS settings, nor support greater ECEC access for children and families experiencing disadvantage. These policy goals would be more effectively achieved through relaxing the activity test and increasing the subsidy rate for lower-income families. Increasing the hourly rate cap to better reflect costs of provision would also help to ensure that affordability for all families is maintained over time. These changes should therefore be a priority for policy action.



### Draft recommendation 6.2

#### Modify the Child Care Subsidy to improve affordability and access

The Australian Government should modify the Child Care Subsidy to allow:

- all families to access up to 30 hours or three days of subsidised care per week without an activity requirement
- families with annual income at or below \$80,000 should be eligible for a subsidy rate of 100% of the fee, up to the hourly rate cap.

In addition, the Australian Government should review the hourly rate cap associated with the Child Care Subsidy, and set a new cap based on the average efficient costs of providing early childhood education and care services. This should include consideration of a higher hourly rate cap for non-standard hours (draft recommendation 7.3). The hourly rate cap should be reviewed every three years to ensure it continues to reflect costs (in conjunction with other work mentioned in draft recommendation 6.1). In between these reviews, the hourly rate cap should be indexed at a rate that best reflects changes in the costs of provision such as wage indices or CPI.

## Improvements for families facing higher affordability barriers

A number of submissions to this inquiry (1<sup>st</sup> Impressions Early Learning Centre, sub. 91, p. 1; EYIA, sub. 97, p. 1; Paul Ramsay Foundation, sub. 148, p. 4) have suggested improving ECEC affordability for children from families that have restricted residency in Australia (such as temporary protection visa holders). Children from these families are not eligible to have their ECEC subsidised through the CCS meaning that it is likely that these families would have to pay full fees for their children to participate in ECEC. Given that these families are likely to have lived and/or may continue to live with adversity and that a high proportion of temporary protection visa holders end up becoming permanent residents in Australia (Parliamentary Library 2013), ensuring children from these families have access to affordable ECEC would be important to improve educational outcomes and career trajectories and support longer-term integration. These benefits would need to be contrasted with the costs of expanding CCS eligibility for these families.

Proposals considered in paper 5 to increase supply-side funding in thin markets, including geographically isolated areas, would go towards making ECEC more available in these areas. The Isolated Children's Parents' Association of Australia submission suggests that affordability could also be improved by expanding the Assistance for Isolated Children Distance Education Allowance, to include children receiving preschool education through distance education (sub. 58, p. 5). The Distance Education Allowance 'contributes towards incidental costs incurred by geographically isolated families whose student children are undertaking their education by distance education methods' (DSS 2023b, p. 57). Currently the Assistance for Isolated Children Distance Education Allowance is limited to those participating in compulsory schooling. The benefits of expanding the Distance Education Allowance would need to be contrasted with its costs.



#### Information request 6.4

The Commission is seeking views on the costs, benefits and practicalities of:

- expanding CCS eligibility to include families who have restricted residency in Australia such as temporary protection visa holders
- expanding the Assistance for Isolated Children Distance Education Allowance to include children receiving a preschool education in geographically isolated areas.

## Reducing administrative complexity could make ECEC subsidies more accessible

Improving families' understanding of CCS and the application process would assist in encouraging ECEC participation. This could be achieved by simplifying the CCS design (how the CCS is calculated, including eligibility requirements), simplifying the CCS system (how families apply for and manage CCS) and providing clear, accurate and easily accessible information to improve families' understanding.

### Simplifying the design of the subsidy would make it easier for families to understand their eligibility for support

Relaxing the activity test would make it easier for families to understand their CCS eligibility. This is explored above.

Streamlining the HCCS would also make it simpler for families to understand how much ECEC subsidy they are eligible to receive. Before the 2023 Cheaper Child Care changes, the HCCS was determined as the CCS rate plus 30 percentage points up to a maximum of 95%. But the policy changes mean the HCCS rate is no longer linked to the CCS rate. An option to simplify the subsidy settings would be to align the HCCS rate more closely to the CCS rate.

A number of submissions to this inquiry (Gowrie SA, sub. 25, p. 3; Early Learning and Care Council of Australia, sub. 153, p. 8) supported increasing the length of eligibility for ACCS (Child Wellbeing). ACCS (Child Wellbeing) is initially provided for a period of six weeks and services must apply for a determination for the relevant child to continue to be eligible for it. If the determination is approved, eligibility can be for up to 13 weeks and up to 52 weeks if the child is on a long-term protection order, in formal foster care or in a formal kinship arrangement (Services Australia 2022b).

Extending the length of eligibility for ACCS (Child Wellbeing) would reduce the burden on services to reapply and would assist in continued ECEC participation for the relevant children. If a child is deemed eligible to receive subsidised ECEC through ACCS (Child Wellbeing) it is unlikely that their circumstances would improve dramatically within the initial 13 week determination period. And for these children there are greater benefits from continuing to attend ECEC (van Huizen and Plantenga 2018, p. 219). For those children on a long-term protection order, in formal foster care or in a formal kinship arrangement, eligibility could remain indefinitely while their circumstances remain unchanged. For remaining children eligible for ACCS (Child Wellbeing), the initial determination period could be extended to 26 weeks with eligibility on reapplication also extended for to 26 weeks.

## **Simplifying the CCS and ACCS application processes would make it easier for families and reduce barriers to ECEC participation**

Administrative complexity could be reduced by allowing families who are already eligible for income support payments or a Health Care Card to be eligible for CCS automatically. Aligning similar processes across different payment types, for example family income reconciliation processes across CCS and Family Tax Benefit, would also assist with reducing complexity.

Another approach to reducing complexity for families would be to streamline data inputs across myGov services for use in CCS applications as was recently recommended by (NSW IPART 2023, p. 117). This could be achieved by utilising information provided as part of other income support payment applications, for example, families receiving Family Tax Benefit who have already submitted an estimated family income that would also be relevant to determine CCS rates.

Maintaining a child's eligibility for subsidised ECEC when their guardian changes, whether it be permanently or temporarily, would reduce or remove the risk of a child's ECEC attendance being disrupted. When, for any reason, the primary carer of a child may change (for example due to the parent no longer being able to primarily care for a child), the child's CCS eligibility would remain in place for a period of eight weeks while the new guardian puts in an application for CCS. This would provide consistency for the child during a period of uncertainty and change. There would be some administrative adjustments required to allow this flexibility.

Related to a change of guardianship, recognising informal kinship carers as carers under ACCS (Grandparent) would assist in reducing barriers to ECEC attendance for Aboriginal and/or Torres Strait Islander children. Currently to be eligible for ACCS (Grandparent) children must primarily be cared for by their grandparent or great-grandparent. Extending this to include informal kinship carers would recognise that for some Aboriginal and/or Torres Strait Islander children, their primary carer may change without any formal process and that their attendance at ECEC should not be at risk of disruption as a result of this. Data on the number of children in informal kinship care is limited. One piece of research suggests it may be at least 100,000 and could be as high as 450,000 children (Kiraly 2018, p. 3). For some Aboriginal and/or Torres Strait Islander children, their informal kinship carer may be a relative such as an aunt, uncle, sibling, other relative or a family friend rather than a grandparent (Kiraly 2018, p. 4) which would make these children ineligible to receive subsidised ECEC under ACCS (Grandparent). There may also be some administrative challenges with recognising informal kinship carers apart from Grandparents for the purposes of ACCS (Grandparent).

These options to reduce administrative complexity will be explored further for the inquiry's final report.

**Information request 6.5**

The Commission is seeking views on the costs and benefits of potential measures to reduce Child Care Subsidy (CCS) administrative complexity. These may include:

- streamlining the Higher Child Care Subsidy rate to be more aligned with the CCS rate over time
- allowing families who are already eligible for income support payments or a Health Care Card to be automatically eligible for CCS, and aligning processes that are similar across CCS and other payments
- extending the initial length of eligibility for Additional Child Care Subsidy (Child Wellbeing) from six weeks to 26 weeks and subsequent lengths of eligibility to between 26 and 52 weeks
- extending the length of eligibility for Additional Child Care Subsidy (Child Wellbeing) for those children on a long-term protection order, in formal foster care or in a formal kinship arrangement, while their circumstances remain unchanged
- extending Additional Child Care Subsidy (Grandparent) to recognise informal kinship carer arrangements
- maintaining a child's eligibility for CCS for a period of eight weeks when there is a change of guardian.

### **Providing clear, accurate and easily accessible information on CCS eligibility would make it easier for families to understand their CCS eligibility**

Providing easy to find and easy to understand information would assist in improving families' understanding of their CCS eligibility. This could be achieved by ensuring all information provided on government websites about how CCS eligibility is determined is consistent across sites, easy to find and navigate and easy to understand. The Australian Government should explore options to achieve this.

A calculator which allows families to estimate the amount of CCS they are eligible for under different scenarios (such as different working hours or income levels) would also assist in improving families' understanding of how their CCS eligibility is determined. The Starting Blocks website contains a dedicated CCS calculator but it does not allow for estimation of CCS eligibility under different scenarios. Extending this calculator so that families could estimate their CCS eligibility under different scenarios would assist families' understanding of the system. Improving awareness of the availability of this calculator would also be necessary given that awareness of the Starting Blocks website itself is low (ACCC 2023b, p. 183). The Australian Government should investigate the best way to achieve this.

For families who may find it challenging to access ECEC, support in navigating the system via alternative entry points can be helpful. One potential solution could involve a 'system navigator' role to help families understand the system, fees, forms and other enrolment processes (paper 7 discusses this further).

**Draft recommendation 6.3****Make information about CCS eligibility easy to find and understand**

The Australian Government should explore options to make information provided on government websites about CCS eligibility easy to find and easy to understand by families.



#### Draft recommendation 6.4

#### Improve the CCS calculator on the Starting Blocks website

The Australian Government should improve the functionality of the Child Care Subsidy calculator on the Starting Blocks website so that families can estimate their Child Care Subsidy eligibility under different scenarios (such as different working hours or income levels).

The Australian Government should investigate the best way to improve awareness of the availability of the CCS calculator on the Starting Blocks website.

### Improving families' understanding of CCS withholding and minimising debt and the potential of debt

As mentioned above, the 5% withholding rate is the least understood part of the CCS. Providing clear and easy to find information to families about the CCS withholding rate, and that it can be adjusted, would assist in improving understanding of how it works and its impact on out-of-pocket expenses at the time of fee payment to services. Information about the option to adjust the rate could be provided both during the CCS application process and whenever families have to update their details, improving visibility and knowledge about the rate.

Making use of greater linkages between government data sources could assist in reducing a family's potential for a CCS debt. The 2019-20 Budget announced as part of the expansion of Single Touch Payroll (STP) that STP information would be shared by the Australian Taxation Office to Services Australia to assist in streamlining Services Australia's interactions with customers (ATO 2022). It would include prefilling customer information, streamlining claims, enhancing Family Tax Benefit processes by sending SMS and email messages to customers when STP data showed changes in circumstances (such as changes to income and working hours), assisting Services Australia to pay customers the right amount and using STP data to understand customers' recent employment and income history when there are debts (ATO 2022).

STP information could similarly be used in regard to families' CCS eligibility. Similar to the enhanced Family Tax Benefit processes, SMS and email messages could be sent to families when the STP data indicates a change of circumstances. This should mean families are able to update their details in a more timely manner so that the period during which they receive the incorrect amount of CCS (based on more up-to-date information) is minimised which would minimise overpayment of CCS and the potential of a CCS debt.

The recommendations to relax the activity test would also assist in reducing the potential for a CCS debt. Under the current system, if a parent or guardian's activity level reduced and they were slow to update their activity details with Services Australia this could lead to a debt. This is because they may no longer be eligible for the same level of subsidised hours (as in their number of subsidised hours could be reduced) and they may incur a debt the CCS they had already received. However if the activity test is relaxed, the potential for this to occur is reduced as 30 hours of ECEC would be subsidised regardless of the parent or guardian's activity level.



**Draft recommendation 6.5****Prompt families to update their details with Services Australia**

The Australian Government should use Single Touch Payroll information from the Australian Tax Office to prompt families to update their activity and income level details with Services Australia.

**Draft recommendation 6.6****Provide better information to families about CCS withholding rates**

The Australian Government should provide clear and easy to find information to families about the Child Care Subsidy withholding rate during the Child Care Subsidy application process and when families update their details with Services Australia.

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