Family and Childcare Trust

Childcare and early education funding in London Report for Greater London Authority, March 2018

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Acknowledgements

We are very grateful to the Greater London Authority for funding this project. For more information about the Mayor's support for early years education and childcare please see https://www.london.gov.uk/what-we-do/education-and-youth/support-families-and-early-years/early-years-and-childcare

The authors would like to thank the childcare providers who kindly agreed to be interviewed for this project. Thanks also to colleagues at the Family and Childcare Trust, particularly Joshua Cottell who conducted many of the interviews.

About the Family and Childcare Trust
The Family and Childcare Trust aims to make the UK a better place for families. We are a leading national family charity in the field of policy, research and advocacy on childcare and family issues, with over 40 years' experience. Our on-the-ground work with parents and providers informs our research and campaigns. We focus on the early years and childcare because they are crucial to boosting children's outcomes throughout life and supporting parents to work.

Charity number: 1077444 Registered company number: 3753345

Summary

This report looks at funding of early education in London in autumn 2017, shortly after the introduction of the 30 hour extended entitlement. It is based on policy and research analysis, additional analysis of Childcare Survey data, and qualitative interviews with 35 providers.

Variation within London

- On average, London boroughs get more early education funding than other local authorities, but there is very significant variation within the capital: from £4.93 per three or four year old child per hour to £8.53 per child per hour.
- In 2018/19, twelve local authorities saw increases in funding, averaging 8 per cent. Nine saw reductions, averaging 5 per cent. There is no change for the others.
- Nationally, two year olds are funded at a higher rate than three and four year olds as their care is more expensive. However, the majority of London boroughs receive less funding per hour for two year olds than for three and four year olds.
- 'Transitional protection' smooths out changes to the amount local authorities' funding changes from 2016 to 2020. In 2018/19, 12 London boroughs lose out from this protection compared to if changes were made immediately, and nine benefit.

Free entitlement rates and parents' fees

- In about three fifths of London boroughs, the average price paid by parents of three and four year olds exceed the average payments that settings receive from Government. Settings in these areas may be more vulnerable to losing money due to the extension of the free entitlement, as parents will be paying for less care.
- This figure will vary a lot between settings, and fees paid by parents are likely to change further as the impact of the extension of the free entitlement and tax free childcare continues to be felt

Understanding childcare delivery costs

- It is difficult for providers to produce an accurate figure for the hourly cost of childcare delivery because their inputs are complex and constantly changing – for example, different occupancy rates through the week and year, and children's different ages.
- Childcare providers do not tend to be financial experts, and this can make it harder for them to cope with the complexities of the childcare funding system.

Providers' views on the 30 hour entitlement

- Most providers we spoke to were concerned that the 30 hour entitlement would have a negative impact on their finances. A few felt it would be positive as it would give a more reliable income.
- Providers also raised concerns about the administrative time required to manage the 30 hour entitlement and the fact that payments are made in arrears.
- Many providers were uncertain about the impact of the entitlement on their business, with questions about parents' willingness to pay for 'optional extras' such as lunch.

Other concerns for providers

- Some providers reported that they now receive less support from their local authority, and that this results in higher direct costs, for example for training.
- There were particular concerns about the sustainability of services for children with special educational needs and disabilities (SEND), and some providers worried that they would be frozen out of services.
- Some setting managers cited price inflation, minimum wage increases and rising recruitment costs as potential future pressures.

1. Government support for childcare in London

1.1 The free entitlements

All three and four year olds, and some two year olds, are entitled to free childcare funded by the state. Two year olds are entitled to 15 hours a week for 38 weeks per year if their family has a low income, if they have a disability, or if they are have been looked after by the local authority. All three and four year olds are entitled to 15 hours per week for 38 weeks per year, and those who have working parents[1] are entitled to 30 hours per week for 38 weeks per year from September 2017.

1.2 Other forms of funding

Elements of childcare are also funded by the Department for Education, directly or in kind, through:

- The Early Years Pupil Premium, for children aged three and four whose families receive certain benefits or are or have been in care, pays for the additional costs associated with deprivation (similar to the school-age Pupil Premium)
- The SEN Inclusion Fund and Disability Access Fund, which pay for the additional costs of support for children with special educational needs and disabilities
- Local authority support through early years teams, for example to deliver training and business support, or access to subsidised premises
- Cross-subsidy by schools of their early years provision from other elements of their budget

Many parents get help with their childcare bills through tax-free childcare or childcare vouchers (higher income families) or universal credit/working tax credit (lower income families). These pay a proportion of the price of childcare charged by providers, up to a set cap each week, month or year, and are funded by the Department for Work and Pensions and Treasury.

1.3 How the free entitlement rates are calculated by the Department for Education

Funding rates per hour for three and four year olds are the same for the 15 and 30 hour entitlements. They are calculated at a local authority level, based on a core funding rate with supplements reflecting the proportion of children on free school meals, the proportion of children with disabilities, and the proportion of children who speak English as an additional language. There is then an 'area cost adjustment' based on the costs of providing services at a

1 Defined as both parents or a lone parent earning the equivalent of at least 16 hours as a week at minimum wage, and less than £100,000/year.

local authority level, and a smaller cost adjustment based on the rateable value of early years premises.

In practice, this calculation is changed for 2017/18 and 2018/19 by the promise that no local authority will receive less than £4.30/hour, and 'transitional protection' which guarantees that authorities will not lose more than 10 per cent of their funding compared to 2016 rates by 2020, and no area will gain more than 22.9 per cent.

Funding rates per hour for entitled two year olds are calculated by the Department for Education (DfE) on a similar, but distinct, formula.

1.4 How funding is distributed by local authorities

Historically, local authorities have been able to distribute their funding from central government at their own discretion. Government is now moving towards an assumption of equal funding for all settings – local authorities are required to have a standard hourly funding rate for all local providers by 2019/20 for two year olds and three and four year olds.

The DfE has provided supplementary funding until at least 2019-20 to protect maintained nursery schools' funding at 2016-17 levels, as these have historically been funded at a higher rate. However, in five London boroughs, the DfE calculations estimated that nursery schools already received less than the new universal base rate, so they did not allocate supplementary funding to those boroughs. This means that out of 80 maintained nursery schools in London, 14 are not receiving the supplementary funding.

Local authorities are allowed to use supplements for different settings in the local area which vary funding up to a maximum of 10 per cent of the total allocation. This must include deprivation, and may also include rurality/sparsity, flexibility for parents, quality, and English as an additional language. Local authorities are also limited in the amount of funding they can retain for their early years activities (for example training and business support) – this is capped at 7 per cent for 2017/18 and 5 per cent from 2018/19.

1.5 In practice: funding rates in London

Average rates for three and four year olds in London are higher than the average for England, but there are very significant variations. DfE for 2018/19 rates are highest in Camden at £8.53/hour and lowest in Bromley at £4.91.[2] The England average is £4.77. The impact of transitional protection in London also varies significantly: 12 local authorities are affected by the 22.9 per cent cap, and would receive more money if it was not in place. Conversely, nine local authorities are helped by transitional protection, and would have less money if it was not in place.

Compared to 2017/18, 2018/19 rates remain the same in 11 boroughs, increase in 12 boroughs, and reduce in nine boroughs. Among boroughs which have rates reduced, the average drop is 5 per cent. Among those where they have increased, the average change is 8 percent. Rates drop more in boroughs which had higher 17/18 rates, so the range within

2 The City of London does not have a separate early years grant and is not included in the calculations for this section

London drops from £4.26 to £3.72. Camden remains the highest-funded borough but Bromley replaces Bexley as the lowest. Note that these comparisons do not take into account the changing rules for the amounts local authorities can retain, which are described above.

The variation in funding rates for two year olds is much less: 12 London local authorities receive £6.50/hour, 10 receive £5.92 and 10 receive £5.66. This means the majority of London local authorities receive less funding for two year olds than they do for three and four year olds - very different to the national picture, where on average authorities receive 62p per hour more for two year olds than three and four year olds. Holding other things equal, we would expect costs for two years olds to be higher than for three and four year olds due to different rules on staffing ratios for this younger group.

2. Relationship between prices, free entitlement rates and costs

Outside of the free entitlement, childcare providers are free to set their own prices. As in all markets, these will reflect both their actual delivery costs and what parents are willing and able to pay.

Family and Childcare Trust's Childcare Survey collects information from local authorities on the prices parents pay for childcare outside of the free entitlement.[3] The most recent data was collected between November 2017 and January 2018, in the first months of the 30 hour free entitlement. This is published at regional and sub-regional (inner/outer London) level but individual local authorities' data is not shared. For this project, we have presented local authority data in bands so that they cannot be identified.

Analysis in this section is based on the average prices record for parents using 25 or 50 hours of childcare: for three and four year olds this is ten chargeable hours per week, on the assumption that parents will have used their free 15 hours, or 20 chargeable hours per week, on the assumption that parents will have used their free 30 hours. Hourly rates for some providers can vary depending on how much time parents need: in general, hourly prices will be lower if the child is in the setting for longer, but the extent of variation is different from provider to provider.

On the assumption that 95 per cent of funding is passed from local authorities to providers, as is required in the statutory guidance, the average price parents pay for childcare for two year olds is higher than the 2018/19 free entitlement rate for two year olds in two fifths of local authorities. The average price parents pay for childcare for three and four year olds is higher than the 2017/18 free entitlement rate in just under half of local authorities for which we have data.

Boroughs in which average prices parents pay exceed free entitlement rates at 95 per cent pass-through[4]

	Three and four year olds	Two year olds
At 2018 prices	58%	50%

This data should be treated with caution. Local authorities do not have to have an equal funding rate for every setting or a pass-through rate of exactly 95 per cent – many will pay different providers different amounts based on local supplements. Similarly, average prices for parents vary considerably within boroughs. As such, the proportion of providers for whom prices paid by parents exceed free entitlement rates will be different to these headline figures.

3 For more information on how the data is collected and analysed, please see the methodology section of the report: download from www.familyandchildcaretrust.org

4 Based on useable price data from 24 local authorities for two year old prices, and 23 for three and four year old prices

3. Early years childcare delivery costs for London

3.1 Estimates of delivery costs in London

There have been a number of studies into the actual costs of delivering childcare at a national level. Some of these have data at regional level, but there is no reliable data available at a borough or sub-regional level in London.

The most recent independent study of costs in London was the cost element of the SEED (Study of Early Education and Development) study, funded by the Department for Education – fieldwork was conducted in December 2015 with 166 settings in England, and broken down at regional levels. This found that costs in London were the highest in the country: the hourly cost of delivering childcare for a two year old was 70 per cent higher in London than in Yorkshire. The study also found significant variations between types of setting, with costs at private nurseries lowest and those at maintained nursery schools highest. The Department for Education's most recent Survey of Providers does not provide an hourly cost, but shows that costs 'per place per year' are more than twice as expensive in London than in the South West and West Midlands, although it is possible that part of this difference is due to children attending for longer hours.

A full description of recent studies of early years childcare costs and prices can be found in Appendix 1.

3.2 Components of delivery costs

For almost all childcare settings, staff costs make up a significant majority of costs – the proportion varies, but the SEED study found that the average is about three quarters. The remaining quarter is usually split between premises costs (rent or mortgage) and other costs: these will include insurance, food and other consumables, utility bills, play equipment, and so on. Similarly, the NLH Partnership study found that staffing made up 73 per cent of costs for private nursery providers, and the Department for Education's Survey of Providers found that staff costs account for 73 per cent of costs for private and voluntary providers, rising to 80 per cent for maintained nurseries.

3.3 Methodological and practical issues with delivery cost calculations

Assessment of 'real' childcare delivery costs outside of detailed (and usually fairly small) studies is complex – most childcare providers are either small organisations, or fairly small parts of schools. They are not usually financial specialists, and local authorities offering business support report that business managers sometimes find it difficult to accurately estimate their hourly delivery cost (as opposed to the price that is charged to parents). Nurseries which are part of chains may have more resources available for analysing their costs, but because they may be able to share back office costs, they are unlikely to be typical.

There are also methodological questions about how staff and overhead prices should be ascribed per child per hour, so even a provider with detailed records could produce a number of different but all reasonable hourly cost estimates. This is particularly complicated for childminders as they are using the same space for housing as for work, and must decide what proportion of their housing cost to attribute to their business. For all providers, calculations based purely on staffing and space ratios are unlikely to be accurate because settings will be unable to work at full capacity all the time, and cannot legally operate above capacity.

4. Provider cost drivers in London

This section reports the findings of 35 interviews with representatives from childcare settings across London. The aim of this research was to gain a broad understanding of the cost pressures faced by childcare providers in London, and how they expect these pressures to develop. In order to capture a range of views and experiences, interviewees were recruited from a variety of childcare settings: including (stand alone) maintained nursery schools but excluding nursery classes in primary schools. Please refer to the methodology section in Appendix 2 for more details.

Because this is qualitative research and the sample was not statistically representative, we have not given percentages of providers giving specific responses.

4.1 Common cost drivers

For the majority of childcare providers the categories of delivery costs are broadly the same. With the exception of childminders who do not have an assistant, staffing represents the major cost for all of the interviewees we spoke to. As well as salaries for employees, childcare providers spend a significant amount of their budget on training staff. Supporting childcare workers to undertake training is a requirement of the Early Years Foundation Stage framework, and all settings must ensure their childcare staff members complete a number of compulsory training courses on first aid, safeguarding and food safety. It is also common to provide additional training, depending on the needs of the setting. As well as the fees for the training course, settings must also pay the wages for staff attending the training and also for the members of staff covering their absence.

After staffing, the second largest costs for providers are the rent or mortgage repayments spent on the premises. Following these, common costs include a range of fixed charges, including business rates, insurance and utility bills, and ongoing expenses covering food, equipment, activities and educational resources.

4.2 Variation between settings

Though the drivers that make up delivery costs are broadly universal, there is wide variation in the financial pressures that providers face. This is for a number of reasons including the type of the setting, where it is located, the age and needs of the children that attend, as well as a range of individual factors.

4.2.1 Location

As this present research involved London-based providers only, it is not possible to draw comparisons with settings elsewhere in the country. The SEED study however, which is the largest recent research in this area, showed that settings in London spend more on staff costs and premises costs than areas outside the capital, though 'other' costs are not significantly higher. This reflects wider economic patterns: London has high wages and high premises costs (for both domestic and commercial properties), but the prices of consumables and utilities are less variable.

There is limited data available on differences in delivery costs between childcare providers across London. However, certain cost pressures are likely to depend on location. Premises costs are highly variable across the city: rateable values for commercial properties are more than three times higher in the borough with the highest rate than in the borough with the lowest. For childminders, the median price of a house varies significantly between areas.

The national living wage and the London Living Wage are the same for all London boroughs, but salaries for teachers (who are generally employed in nursery classes and nursery schools) are higher for Inner London boroughs. While market rates for staff are likely to vary between boroughs, data is difficult to analyse – there are no datasets specific to childcare workers which break down to borough level. Insurance costs may also vary between areas, but 'other' costs such as food and materials are unlikely to show significant variation at borough level.

Finally, the social and economic background of the local population also shapes the financial pressures that childcare providers experience. Many of the interviewees related the difficulties or successes they faced as a business to the characteristics of the families in their local area. In wealthier parts of London, where more parents are in full time employment, providers find it easier to sell additional hours to parents, and to charge higher fees. One provider who operated in a particularly high income area explained that they did not expect the 30 hour offer to impact their business, because all of the families that attended the setting were above the upper income threshold of £100,000 per year. In more disadvantaged areas, a higher proportion of children take up funded hours only, and the number of children with special educational needs and disabilities (SEND) also tends to be greater.

4.2.2 Level of local authority support

Cost pressures for providers are also influenced by the local authority they operate under. Local authorities have widely different allocations for funded childcare (see section 1.5) and across London interviewees report varied experiences with levels of business rate concession offered by councils, the price and availability of training provided, as well as the support offered to childcare providers. While some feel that local authority support has improved over recent years, most believe that it has diminished significantly, particularly in relation to supporting children with SEND.

> *"I have seen quite a lot of cuts to training recently. Apart from the safeguarding course, we now have to pay for a lot of the training and also the SENCO [special education needs coordinator] funding has gone down somewhat as well. We are now covering more of [the] paperwork which entails more training and more costs."*
> **Private nursery, Inner London**

Interviewees also suggested that there was significant variation in how local authorities supported settings to deliver the 30 hour offer, though providers generally acknowledged that councils were themselves hindered by a lack of information from central government. Planning for the 30 hour offer was considered to be more effective where early years teams were able to provide proactive support, guidance and reassurance through regular forums, meetings and telephone contact.

4.2.3 Type of setting

Some cost variation is driven by the different types of ownership and organisation. While maintained settings (schools and standalone nursery schools run by a local authority) are unlikely to have to pay premises costs, they are required to employ a head teacher, qualified teachers and a SENCO. These are generally paid more and have better employment terms than other childcare workers. Though statutory ratios permit qualified teachers to look after more children aged three to four, one head teacher told us that it is not possible for them to operate at these ratios, due to the additional needs of the children they support. Maintained settings also have to adhere to the Schools Admissions Code which imposes stronger duties to support children with SEND, and may therefore have a higher proportion of children in this group.

Maintained nursery schools have until recently received higher funding rates to reflect these greater delivery costs. Local authorities are now required to begin harmonising funding levels across all local settings according to their own universal base rate. The majority of maintained nursery schools are able to continue accessing higher funding rates until the end of this parliament, using supplementary funding provided by the Government. However, not all boroughs in London have qualified for the funding. A head teacher of a nursery school in one of these areas told us that following a 20 per cent reduction this year, their budget will continue to shrink by 20 per cent every year for the next three years.

> *"The single funding formula has been a death knell for maintained nursery schools because it implies that everyone is going to be doing the same job at the same cost. But if you've got a head teacher and employ teachers your costs are going to be greater."*
> **Maintained nursery school, Inner London**

April also saw the introduction of a new requirement for all employers in the UK with an annual wage bill of over £3 million to invest 0.5 per cent towards an apprenticeship levy. The majority of private childcare providers are exempt as they employ only a small number of staff. However, as workers in maintained settings contribute to the payroll of the local council, a share of the tax is taken from their annual budgets.

Some private and voluntary nurseries are part of chains – these may be large national groups or smaller, local arrangements. A number of providers told us that being part of a chain reduces overheads as resources and administrative tasks are shared. Greater expertise among back office staff, which settings can more easily afford if they are able to pool their resources, also helps to manage financial uncertainty and administrative challenges. Interviewees reported that this was particularly helpful when deciding how to manage the 30 hour offer. However, most childcare settings are not part of chains and will not access these economies of scale.

4.2.4 Occupancy rates

Providers will have the lowest hourly costs at times that their occupancy is highest. Occupancy is partly a function of providers' success at promotion, but may also depend on competition from other providers in the area, or local changes to employment rates, house-building, and demographic or migration changes. Occupancy also tends to be lower for newer settings compared to more established providers.

4.2.5 Age of children

Regulatory requirements for staffing and space vary according to the age of children, and so delivery costs in group settings will also vary: they are lowest for three/four year olds and highest for younger children. This is not usually the case for childminders, as the same person will be looking after children across the age range. Some providers, particularly nursery classes in schools, only take children above a certain age: this will impact on their costs. The SEED study of early education funding[5] suggests that settings which take children across the early years age range tend to 'even out' their costs to parents, cross-subsidising from older to younger children.

4.2.6 Proportion of children with SEND

Some settings will cater for more children with SEND, either through preference, because of the local prevalence of SEND, or, if it is a maintained setting, because they are required to do so. A number of providers reported that it is more expensive to cater for children with SEND as they often require greater attention, specialist staff or more expensive equipment. Funding and grants can be obtained from local authorities to cover some of these costs, but they can be difficult and time-consuming to acquire, and are only available in certain cases. Many interviewees said that these challenges had increased in recent years as the criteria for funding has tightened and local authority support had diminished.

> *"Because the local authority has made so many cuts it's getting harder for us to deliver a good service to children with SEND. Now only children with high additional needs get the funding but there are lots of children who still require greater attention. You make it work but now it's almost at breaking point."*
> **Private nursery, Outer London**

5 See Appendix 1 for full reference and details

Providers felt that delivering the 30 hour offer would exacerbate existing funding pressures related to SEND provision. One interviewee explained that while they are able to stretch their provision to support children with SEND for a short session, doing so for a full day becomes unmanageable, and compromises the quality of childcare they are able to offer for all children.

4.2.7 Variation between individual settings

Even among settings of the same type located close to each other, there will be some variation between costs. This could reflect active choices by providers to offer a higher standard of service: for example, staffing above minimum requirements, paying wages above market rates, providing more expensive resources and equipment, or offering extra activities and trips.

As well as the quality of service delivered, settings can choose what sort of childcare they offer. Some providers limit their provision to a small number of sessions during term time for a single age group, while others cater for a range of ages, for various time allocations, across the whole year. These choices will involve a balance between controlling costs and expanding sources of revenue.

Other variations are outside providers' control: for example rent or mortgage costs may vary according to when a provider opened. Some settings are able to make extra money by hiring out their spaces out of hours, and some have access to subsidised premises. Some of the providers we spoke to received discounts from the places of worship or local community charities that they rented spaces from. Others had special arrangements, including one provider that rented university-owned premises and paid lower rates in exchange for discounted childcare for students and university staff.

4.3 Experience in delivering funded places

Some of the providers we spoke to told us that that the rates they received for funded childcare were enough to cover their delivery costs. However, the majority of interviewees felt that they were insufficient, particularly for three and four year olds.

> *"The amount the government pays absolutely does not cover our delivery costs. The rate is actually insulting."*
> **Private nursery, Inner London**

Providers employ a range of strategies to manage insufficient funding rates. Most providers rely on parents making extra payments, such as for additional, more expensive hours, for additional services including food provision, or for late fees. Many providers considered it impossible to offer funded places to families without parents making additional payments. Some providers have decided not participate in the free offers, or have restricted the number of places available. This is the case for the 30 hour offer and the 15 hour offer for disadvantaged two year olds in particular.

> *"We are running a loss with the funded places, which means we've had to increase the rates for paid-for hours. It also means we will have to restrict the number [of funded places]."*
> **Childminder, Outer London**

Interviewees generally thought that delivering the 30 hour offer would lead to increased cost pressures. This is primarily because outside of the free entitlement there are fewer hours available for parents to purchase. Providers can often charge higher rates for additional hours paid for by parents.

> *"I'm not part of the 30 hour offer yet because I'm struggling as it is with the 15 hours. If I did the 30 it would probably put me out of business."*
> **Private nursery, Inner London**

The additional administration time required to manage the 30 hour offer was cited by many providers as another way that the scheme led to increased cost pressures. Interviewees referred to a number of extra tasks including planning delivery models, validating codes, reminding parents to apply and reconfirm in time, and supporting parents who had experienced issues.

> *"It's been a big mess, so I've spent hours and hours every week when I should have been doing other managerial things trying to sort out the funding."*
> **Private nursery, Outer London**

Finally, as more children use their additional 15 hours per week to stay for full day sessions, costs will increase to cover food and staffing over lunch, and will compound existing challenges in supporting children with SEND, as discussed above.

4.4 Financial uncertainty

Most interviewees expressed a clear sense of uncertainty regarding the costs they face in delivering childcare. This is less problematic for providers who have simple business models, or who benefit from greater financial expertise as part of a chain. However, most childcare providers do not have access to financial support. Interviewees also pointed out that most childcare delivery models are complex and involve a number of uncertainties. This means that cost calculations are challenging and unlikely to result in reliable figures.

> *"There are too many different things to disaggregate. I'm sure we could do an audit exercise to disentangle those different bits but we don't because it would take us a long time and it wouldn't have that much value for us. It would be a huge technical exercise."*
> **Maintained nursery school, Outer London**

A number of providers cited variable occupancy levels as a key source of uncertainty. As well as the number of children attending a setting, the age and individual needs of children can vary widely from throughout the week and throughout the year. This can make it difficult to accurately calculate hourly costs or make confident financial projections.

Interviewees also highlighted the difficulty in maintaining adequate staff levels. Unplanned staff absences are often expensive. Short term absences normally require costly agency cover, while permanent staffing issues can involve lengthy and expensive recruitment processes. Many providers believed that in recent years it had become increasingly difficult to recruit and retain good quality permanent staff.

> *"One of the big costs is recruitment itself, we're always running ads… because of vacancies our supply has been really expensive, we've had to pay vast amounts of money for agencies to come in and fill the vacancies."*
> **Not for profit nursery, Inner London**

Some interviewees felt that in certain ways the 30 hour offer could lead to greater financial certainty. The scheme could increase occupancy, and secure a steadier and more reliable source of revenue compared with additional fees paid for by parents. However, it was generally expected that the 30 hour offer would make it more difficult to anticipate delivery costs in the long term as well as the short term.

Despite considerable efforts to estimate take up, and prepare delivery models in consultation with parents and local authorities, most providers reported that they were not able to predict how the scheme would affect their budgets. A number of interviewees said that they would need to wait until they reviewed their finances before they could reliably understand the impact of the 30 hour offer.

Unlike other free childcare entitlements, funding for the 30 hour offer is not paid to providers in advance. Some providers have needed to draw on reserves to deliver the childcare offer while they wait for payments from the government, and others have taken out expensive loans. As many providers believe take up of the offer will increase over the coming year, these problems are expected to continue.

> *"We have to provide the additional 15 hours but we won't get the payments from the government until before Christmas which means we are faced with a cash flow shortage for the next three or four months."*
> **Private nursery, Inner London**

Another issue for providers is that it is difficult to predict how many parents will sign up, or remain eligible for the 30 hour offer throughout the year. Some providers felt that this would make it difficult to rely on projected occupancy levels, which normally increase over the year. Others were concerned that they would lose children to other settings if they were unable to offer a full 30 hour place. This is more problematic for providers in relatively disadvantaged areas, where changes to income are more likely push parents below or above the income threshold required for eligibility.

Lastly, as providing funded 30 hour places means that settings have fewer additional hours to sell to parents, many settings are dependent on charging for additional services, including meals, special classes and extra sessions. However, a number of interviewees were concerned that this would be an unreliable source of revenue in the long term. While parents this year may be happy to pay for additional services, viewing such arrangements as a substantial discount compared with what they would otherwise have paid for the additional hours, some providers feared that in the long term parents would increasingly opt out of paying for extra services.

4.5 Future financial viability

Most of the providers we spoke to were anxious about the financial sustainability of their setting, though some were unconcerned. As well as some of the problems outlined above, including diminishing local authority support and the effects of the 30 hour offer, interviewees highlighted a number of additional concerns.

A key issue for many providers is that delivery costs will continue to grow, due to increases in statutory minimum wages and employer pension contributions, as well as wider cost inflation. Providers are concerned that despite this there is no commitment to raise the free entitlement rates until 2020.

> *"Although the funding rate will stay the same there will be inflation and other cost pressures so overall there will be a real terms reduction."*
> **Maintained nursery school, Outer London**

More broadly, a number of interviewees are anxious about how further policy changes would affect their business, given the scale and impact of changes to childcare policy in recent years. Providers were particularly concerned about any changes that would require more time to be given to administrative tasks, more money to be spent on adaptations or resources, or more pressure to deliver new free childcare entitlements on insufficient funding rates.

4.6 Potential solutions

Providers have a range of options to manage the current and anticipated cost pressures described above. However, interviewees explained that many of these would be difficult for providers to implement.

In response to rising costs, some providers would charge higher fees to families for additional hours. But many more felt that parents would not accept any further price rises. Interviewees also reported that reducing delivery costs would be impossible without undermining the quality of childcare they delivered.

> *"I don't think we could make any savings because we're down to the bone now."*
> **Not for profit nursery, Inner London**

> *"These savings would impact on the quality of our childcare, so whichever decision we make, it's painful because we know they have a cumulative impact on that child's development."*
> **Childminder, Outer London**

A number of providers said that they would change their delivery model for the 30 hour offer, either by limiting places, or by introducing charges for extra classes or consumables, such as meals and nappies. Others perceived these arrangements to be divisive and incompatible with the ethos of their organisation, and many considered them to be impractical due to the need to manage food allergies, or because they lacked kitchen facilities and cold storage space. One interviewee feared that providers would start to 'cherry pick' the children they admitted, avoiding those who had additional needs or who were seeking funded hours only.

Some providers reported that they will need to withdraw from the 30 hour offer altogether, while others were concerned about losing business as a consequence.

"We will have to review it and if what is happening so far is an indication of what will happen in the future we will probably not be offering the 30 hours at all. It is too time consuming and the funding rate is nowhere near high enough."
Private nursery, Outer London

"But if we stop offering 30 hour places then parents will walk, and you'll end up with a handful of children and have to shut down."
Private nursery, Outer London

Interviewees highlighted a number of ways that local or central government could support childcare providers. Though most responses stressed the need to review funding rates to ensure they were sufficient, providers also explained that help with costs of resources, premises and facilities, equipment, and most notably business rates could help settings remain financially viable.

Similarly, another issue raised by providers related to the scaling back of support networks for settings to participate in. The coordination of provider networks was highlighted as something that local authorities could reintroduce to provide help for settings. Support networks were believed to be useful for sharing important information, resources and examples of best practice. They were seen as particularly important for new starters, as an opportunity to discuss issues with more experienced members, and for childminders as a way to reduce isolation and provide means for peer support.

Appendix 1. Existing research on early years childcare costs and prices

There is no research data on the costs of delivering childcare at a London borough or sub-regional level. A number of recent studies have made estimates of delivery costs at a London or England level: the most significant are set out below. Most research is commissioned by either the Department for Education or provider representative bodies.

Source	Date	Methodology	Delivery costs & breakdown	FEEE rates	Price to parents
Study of Early Education and Development (SEED): The cost and funding of early education, Blainey and Paull (commissioned by Department for Education)	2017, Jan	Semi-structured interviews with 166 providers	Average cost – £4,747 p/w. £797 p/w for childminders, £11,144 p/w for maintained nursery schools - Staff – 75% - Venue costs – 12% - Other costs – 12%	Mean hourly FEEE rates received by providers – £4.93 for 2YOs and £3.93 for 3/4 YOs.	2YOs entitled to FEEE – £4.44 p/h Not entitled – £4.25 p/h. 3/4 YOs – £4.36 and £4.13.
Cost of delivering the early education entitlement Research report, NLH Partnership (commissioned by Department for Education)	2015, Nov	Qualitative interviews with 44 providers	For PVI settings: £5.39 p/h p/child for 2YOs and £3.51 for 3/4YOs - Staffing – 73% - Rent – 9% - Materials – 5% - Other costs – 13%	Average shortfall of £0.43 for 2YOs Average surplus of £0.22 for 3/4YOs	Not included in study
Review of childcare costs: the analytical report (written by Department for Education)	2015, Nov	Based on more than 2,000 responses from a 'call for evidence', followed by a series of roundtable events	Mean hourly cost per child: Private 2YOs – £5.87 Private 3/4YOs – £4.25 Voluntary 2YOs – £5.39 Voluntary 3/4YOs – £3.81 Childminders – £5.00-£6.12	Not included in study	Not included in study

Source	Date	Methodology	Delivery costs & breakdown	FEEE rates	Price to parents
Counting the Cost The Impact of a National Living Wage, Ceeda (commissioned by Pre-School Learning Alliance)	2015, Jul	Calculated unit cost p/h per child by tracking costs for the delivery of 186,712 hours of early years education and childcare for 5,635 funded and non-funded children in 100 PVI early years settings	For PVI settings: £5.97 for 2YOs £4.53 for 3/4YOs	Not included in study	Not included in study
Open book accounting review Phase 1 PVI Sector, KPMG (commissioned by Birmingham City Council)	2015, Jun	Surveyed 79 providers in Birmingham, including 64 day nurseries and 15 childminders Average cost summaries produced for different groups of settings	Day nurseries: <1YOs – £5.94 1YOs – £6.28 2YOs – £5.24 3/4YOs – £3.86 Cost of overheads (everything but staffing): £1.50 p/h per child for day nurseries, £1.14 for childminders	2YOs – £4.89 (shortfall of £0.35) 3/4YOs – £3.69 (shortfall of £0.17)	Not included in study
Process evaluation of the two-year-olds in schools demonstration project, Greene et al (commissioned by Department for Education)	2015, Jan	Self-completion surveys, finance surveys in 49 schools, and qualitative interviews in 8 case study schools	£5.05 for 2YOs – £3.00 – Indirect costs of delivery staff – £1.00 – other indirect staff costs £1.50 – other direct delivery costs	Not included in study	Not included in study
The value for money of children's centre services Evaluation of children's centres in England (ECCE) Strand 5, Gaheer and Paull (commissioned by Department for Education)	2016, Jul	Case study approach involving interviews with 24 children's centres selected to be representative of centre characteristics, region, and urban/rural from a larger set of 850 centres used for an earlier stage of survey	For children's centres: £9,616 p/w – Staff – 75% – Venue – 14% – Other – 10% – Service contract – 1%	Not included in study	Not included in study

Source	Date	Methodology	Delivery costs & breakdown	FEEE rates	Price to parents
Annual Nursery Survey 2017, National Day Nurseries Association (NDNA)		Annual survey of nurseries across the UK. Survey conducted online in Jan & Feb '17. Received 788 responses – 85% private sector, 10% voluntary, 3% maintained.		The average rate received from the local authority for funded places was £5.04 for 2 year olds and £3.94 for 3 and 4 year olds, leading to losses of £1.12 and £1.38 per hour respectively. 54 per cent of the nurseries surveyed were not covering costs of FEEE places for two year olds, rising to 85% for three and four year olds.	

Appendix 2. Provider research methodology

The research described in Section 4 draws on a series of telephone interviews with representatives from 35 childcare settings. The majority of providers were recruited from provider directories hosted online by local Family Information Services, which were sampled randomly. Others were contacted through the Family and Childcare Trust's existing network.

Interview participants included managers, owners and head teachers from a diverse range of settings and backgrounds. These included both childminders and non-domestic settings, but did not include nursery classes in schools because financial issues are very different for them. The providers were based in 14 different local authorities across London, and in total half of providers were in Inner London and half in outer London. They were also split between east and west and north and south London.

We over-sampled childminders and maintained nurseries relative to the number of children that they care for because of the importance of these settings to London's childcare economy. We have not given the locations of settings because this would risk identifying them.