

Comparing \$10/day flat fees with income tested child care fees

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11/24/2013

With thanks to Laura Coulman and other experts for their insightful comments and moderating influence; any errors, omissions and departures from orthodoxy are solely my fault.

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Introduction

This purpose of this document is to address and stimulate discussion about key policy and implementation issues surrounding proposals to implement a \$10/day child care fee from the perspective of Ontario's child care system and specifically from the point of view that respects the system management role played by Ontario's municipalities. In comparison of the \$10/ day fee and existing income-testing procedure in use for determining subsidy eligibility it is not advocating for perpetuation of the subsidy system as the best way to fund child care in Ontario. Rather, it suggests that an income test is a fair and equitable way of determining user contributions (parent fees) to the cost child care under any funding regime, including full base funding.

Context

Child care affordability remains a significant issue in Ontario. Across Canada, different provinces have adopted varying approaches aimed at reducing costs incurred by parents while they pursue employment or education activities. While none have followed the lead of Quebec in the provision of \$7/ day fees, both Prince Edward Island and Manitoba have both capped user fees. However, even capped fees can present a significant stress for low and middle income families. Thus some form of fee assistance is required. In most provinces this takes the form of fee subsidies. In most provinces other than Ontario, however, these are also capped and families may have to make up the difference between the fee subsidy and the price charged by service providers.

Originating in British Columbia, a movement toward improving affordability through capping fees at \$10/day is gaining momentum and public support. In its current form, the \$10/day flat fee campaign promises affordable child care in which a full-day child care space will cost a

parent \$10/day and a part-day space will cost \$7/day. Families with annual incomes¹ under \$40,000 would not pay any fees.

As we shall discuss later, this approach is substantially different from the current approach to user fees in Ontario, where less than half the children are supported through a subsidy the amount of which is determined by a sliding scale. The remainder of families pay the full price charged by individual service providers.

Recent changes to existing provincial child care funding mechanisms have sparked discussions in many Ontario communities about alternative funding and parent fee models. Many municipalities, in fulfilling their mandated role as child care system managers, are intensively studying and evaluating potential funding models with the intent to promote equitable and affordable access to quality child care programs.

User fees and program funding

Should we dispense with user fees altogether? Child care is both a public and a private good. To the extent that there are demonstrated short and long term societal benefits from early education and care, it is reasonable (not to mention a good investment) that society as a whole should shoulder a significant portion of the cost of the program. However, because the individual family also benefits from child care in terms of ability to participate in the labour force, some degree of co-payment is warranted. Higher income families also benefit more from the federal Child Care Expense Deduction which reduces that part of the income of the lower earner that is taxed at the highest rate.

For the purpose of this discussion, it is useful to separate the issue of how funding for child care services is determined and delivered into operators' hands from how user fees are determined, calculated and collected.

¹ From the documentation the definition of annual family income (i.e. gross, taxable or net) is not clear; later we will see that this presents some issues in modeling the impact of the proposals.

Specifically, while affordability of child care is of crucial importance to families, the actual user fee mechanism should not be confused with the fundamental issues of public policy, funding and management of child care systems.

Ontario's income test and the \$10/day plan

Be it in Ontario or British Columbia, regulated child care is very expensive for a working family yet program staff wages and benefits are low, usually below "living wage" thresholds. As a result, it would be impractical and, indeed, unethical to seek improved affordability through reduced compensation of ECE staff.

Regulated child care is in short supply, especially in urban areas where demand is high – and very complicated to deliver in rural and remote areas where combination of low child density and large travel distances often results in short and unstable supply.. The situation is not helped by lack of system vision, planning and integration of services, at both provincial and local levels. And finally, government funding of both fee subsidies and wage supports is inadequate to meet the need.

There are significant differences between the two provinces as well as similarities. Probably the most significant is the regulatory framework; in Ontario, municipalities have a legislated role in funding, planning and management of early learning and care services. On the other side of the ledger, unlike in most provinces, child care subsidy is not an entitlement in Ontario; this can lead to lengthy waiting list and force middle income families to pay full price even when they are clearly eligible for fee subsidy.

The financial eligibility rules for fee subsidies differ radically between the two provinces as well:

- a. BC - limited eligibility for subsidy, cap on subsidy; families have to top up their subsidized user fee to meet the widely ranging prices charged by service providers
- b. Ontario – financial eligibility is based on price of service; eligibility for financial assistance ceases when the income tested fee exceeds the price of care. There is

no cap on amount of subsidy and the income tested fee applies without regard to family size or number of children in child care.

Translating the \$10/day flat fee into the Ontario context

The policy issues

A flat fee is inequitable, as with this approach, as family income increases, the family's cost of child care as a proportion of income decreases. Lower income families will still pay much higher proportion of their income toward the cost of child care. This solution just shrinks the problem. The problem (and the core principle) remains: if the problem of inequity is not solved (only shrunk), then it is possible for it to grow again.

A flat fee is also inequitable because it penalizes families with more than one child; an equitable approach would, by relating family fee to family income, avoid discriminating against larger families.

Even if it is quite low, a flat fee will still lead to crowding out low income families, particularly if there is insufficient child care capacity and high demand; this was one of the unintended consequences of introducing the \$5/day fee in Quebec.

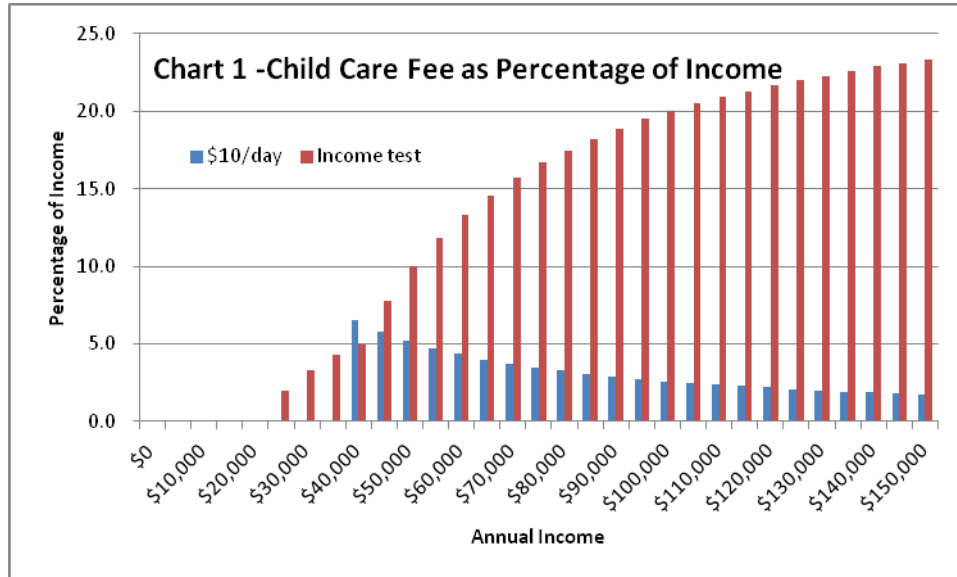
Another detail that may have an undesirable effect: a \$1 increase in income from \$39,999 to \$40,000 will suddenly result in a \$2,610 dollar annual fee per child (see Charts 1 & 2 below).

Alternatively, a more equitable approach would be to gear the fee to income. This can be done as a flat percentage of income or at an increasing rate to a predetermined maximum. The current Ontario income test exempts all taxable income below \$20,000, charges 10% of all taxable income between \$20,000 and \$40,000 and increasing to 30% for all income above \$40,000.

Thus, using the current Ontario income test currently used in subsidy determination to determine the parent fee would be more equitable, although not perfect. Because it does not cap on financial eligibility, does not limit family size, and has no abrupt threshold leading to an steep fee increase. Using the Ontario income test would not force a family to seek cheaper,

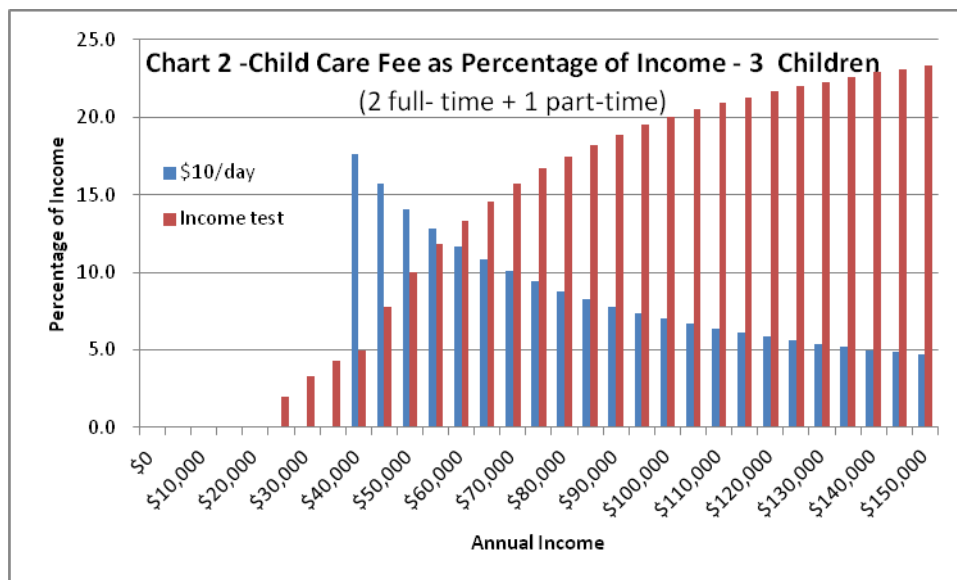
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and often lower quality care just because the fee above a cap is prohibitive. Access to quality child care should not be the exclusive domain of those who can afford it, either through full fee or paying a surcharge on top of what the subsidy system is willing to pay.



The impact of the \$40,000 threshold and “per space fee” compared to a “family fee” is clearly demonstrated when examining a case of family with three children. Thus under the \$10/day plan, a family with three children (two preschool and one school-age) would pay \$7,047 or 17.6% of its income compared to \$2,000 or 5% under the current Ontario income test rules. At the higher end of the income continuum, the \$10/day plan would mean that the family would have to contribute only 4.7% of their income.

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While it may be tempting to dismiss this inequity as simply a design issue, its source lies deeper than that. The flat fee approach is inherently inequitable in that it reduces the proportion of family income spent on child care as income increases.

Practical implications of a \$10/day fee

In the following paragraphs we will be using City of Toronto's child care system data as an illustration of some of the implementation issues associated with a \$10/day plan.

There are more than 58,000 licensed spaces in more than 920 centres in Toronto². At any given time less than 40% of these spaces are filled with subsidized children, the rest paying "full fee"³.

- The estimated annual cost of operation for the 58,072 spaces is \$637.3 million.
- City, provincial and subsidy user funding accounts for \$322.4 million, while full fee users pay the remaining \$314.9 million.
- Revenue from full fee parents under a \$10/day plan would bring in \$84.0 million, resulting in a new cost to the funding bodies of \$230.9 million. In addition, the funders would have to replace \$3.9 million loss of revenue from current subsidy users with

² This analysis focuses primarily on centre based care, which provides the majority of regulated spaces, as there are some information gaps about the small family home child care sector that does not accept subsidized children.

³ Full fee does not represent the actual cost of these spaces since most benefit from some, albeit minor, level of government funding in form of wage and occupancy subsidies. In this context "full fee" represents the price charged by the service provider.

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incomes under \$40,000 and additional \$7.3 million loss of revenue from subsidy users whose fees would be reduced to the flat fee of \$10/day or \$7/day for part-time care.

In total, the funders (Ontario and the City of Toronto) would have to add \$242.1 million to the existing funding in order to accommodate the \$10/day flat fee proposal.

This expenditure would not increase the number of spaces in the system, improve wages of Early Childhood Educators or lead to improvement in program quality. In addition, introduction of the flat fee approach would not improve equity of access in under-served areas of Toronto or directly lead to expansion of infant and toddler care.

Although the child care costs and prices are higher in Toronto than most other places in Ontario, one could expect the total province-wide cost of a \$10/day flat fee initiative to be approximately \$1 billion; again, this would be without an increase to staff compensation or the supply of child care spaces.

Concluding comments

It would seem that there are better ways to deploy an additional \$242.1 million, should it become available. With this fund, it would be possible to simultaneously advance on the following initiatives:

- Gradually expand the number of income-tested (and eliminate the current subsidy waiting list) while expanding the licensed capacity. Preliminary analysis suggest that all existing full fee families could be accommodated under income testing with sufficient funding left over to gradually expand the system.
- Increase affordability by adjusting various parameters of the existing income test:
 - Increase the level at which user fees are assessed from the current \$20,000 to, at least, keep pace with inflation
 - reduce the tax-back rate to the reduce maximum percentage spent on child care services at any given family income level

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- Provide increasing amounts of base funding to eligible service providers through capping fees for the younger age groups at affordable levels, ultimately converting the current demand based system into a supply managed model.
- Improve compensation of all program staff, including introduction of a portable pension plan
- Invest in quality improvement through measures such as mandatory, compensated professional development

Invitation to a conversation

The purpose of this paper was to begin a public conversation about ways of determining user contribution to funding necessary to operate child care programs. Obviously the larger the system funding by governments, the less dependence there will be on user fees. Yet, as long as there is a need for users fees, it behoves us to consider the fairest and most equitable methods for determining individual family contribution.

I welcome any comments and will endeavour to find a forum in which we can discuss this issue publicly.

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