Title: Childcare Payments Bill 2014 **IA No:** **Lead department or agency:** HM Revenue and Customs **Other departments or agencies:** HM Treasury	**Impact Assessment (IA)** **Date:** 18/11/2014 **Stage:** Final **Source of intervention:** Domestic **Type of measure:** Primary legislation **Contact for enquiries:** tax-free.childcare@hmrc.gsi.gov.uk

Summary: Intervention and Options

RPC Opinion: Not Applicable

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, Two-Out?**	**Measure qualifies as**
£m	£m	£m	No	NA

What is the problem under consideration? Why is government intervention necessary?

Finding reliable, high quality, affordable childcare is a major concern for working families. The high cost of childcare can be one of the largest parts of most working families' household budgets - and for some families it does not pay to go to work. Survey data suggests that many more mothers would move into work or increase their hours if they could arrange reliable, affordable, convenient, good quality childcare. The Government believes there is a powerful case for improving access to childcare. The current scheme to support parents with the cost of childcare, Employer Supported Childcare (ESC), is neither effective nor fair, as many working families are unable to access support.

What are the policy objectives and the intended effects?

The Government is committed to promoting aspiration and rewarding work. The high cost of childcare is one of the biggest financial challenges that working families face; for some parents it does not even pay to go to work. The Government will provide support equal to 20% of total childcare costs, up to an annual limit of £2,000 Government support per child. This is equivalent to basic rate tax relief on childcare costs up to £10,000 per year. The Government wants the scheme to be as accessible and user-friendly as possible. The scheme will be operated through flexible online childcare accounts and will be introduced from autumn 2015. It is estimated that up to 1.9 million families will be eligible for support within the first year.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

The Government could have done nothing to further support parents with childcare costs, relying on the existing tax exemption in ESC for those able to access it. However, this would have failed to provide support to the more than half of all employees who cannot access ESC, as well as self-employed parents. The Government could also have sought to mandate employers to offer ESC. However, this would have placed an unacceptable burden on business, and would have done nothing to support the self-employed, or to address the other weaknesses of ESC, such as the way it disadvantages lone parents by basing support on the number of eligible parents rather than the number of children. Instead, at Budget 2013 the Government announced the new scheme, delivering support to all eligible families through childcare accounts. The Government consulted on how accounts should be delivered: in the private or public sector, and by one or multiple provider(s). The Government subsequently announced NS&I as the scheme's account provider.

Will the policy be reviewed? It will be reviewed. **If applicable, set review date:** 12/2018

Does implementation go beyond minimum EU requirements?			No		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** Yes	**< 20** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** N/A	**Non-traded:** N/A	

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.

Signed by the responsible SELECT SIGNATORY: Date: 18-11-14

Summary: Analysis & Evidence

Policy Option 1

Description:

FULL ECONOMIC ASSESSMENT

Price Base Year	PV Base Year	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	**High:** Optional	**Best Estimate:**

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate				

Description and scale of key monetised costs by 'main affected groups'

The main Government cost will be top-up payments to parents, to be spent on childcare. The gross costs are estimated at £285/825/940/990m; net costs (given reduced ESC spend) will be £245/660/645/590m. There will also be an administration cost, which will be settled once the scheme's details have been finalised. Employers offering ESC (vouchers or directly-contracted) will gradually see the NICs saving from which they currently benefit reduce when the disregard is closed to new entrants.

Other key non-monetised costs by 'main affected groups'

The ESC voucher market is currently funded from an employer NICs disregard. The Government announced at Budget 2013 this disregard will be phased out when the new scheme is introduced. Some voucher providers may seek to offer services in ESC which employers and their staff value that can be funded outside a NICs disregard; others may not, and will either move to other lines of business or - at some point - close. Childcare providers may experience one-off costs preparing for the new scheme.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate				

Description and scale of key monetised benefits by 'main affected groups'

All working families will be able to access support of up to £2,000 per child per year, provided they meet the eligibility criteria. Around 1.9 million families will be eligible, of which 1.25 million are likely to have qualifying childcare costs. Around 1 million families will be better off under the new scheme by an average of £600 per year. The vast majority of these families do not receive any support in ESC. As the existing support is being grandfathered, there will be no direct losers.

Other key non-monetised benefits by 'main affected groups'

As well as the significant financial benefits, parents will benefit from a simple and flexible scheme designed to be easy to use, and from improved access to childcare. Childcare providers will also benefit from the simple nature of the new system as well as from more parents being able to access childcare. The Government also expects employers to benefit from the effects of a far greater number of employees being able to receive support with their childcare costs.

Key assumptions/sensitivities/risks | **Discount rate (%)** |

The scheme will be introduced from autumn 2015 and be fully operational within a year of the scheme's introduction.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			In scope of OITO?	Measure qualifies as
Costs:	**Benefits:**	**Net:**	No	NA

Evidence Base (for summary sheets)

Background

Finding reliable, high quality, affordable childcare is a major concern for working families[1]. For many parents it is difficult to find good childcare, and the high cost of childcare can be one of the largest parts of most working families' household budgets.

Survey data suggests that more than half of mothers not in paid work would prefer to be in paid employment if they could arrange reliable, convenient, affordable, good quality childcare.[2] Similarly, nearly a quarter of employed mothers say they would increase their working hours if they could arrange such childcare.[3]

The Government believes that there is a powerful case for improving access to childcare: to ensure that parents are supported to work, if they choose to, and have fulfilling careers with potential for progression; and that children have the best possible start to life through high quality early education.

The current scheme to support parents with the cost of childcare, Employer Supported Childcare (ESC), is neither effective nor fair, as many working families are unable to access support.

Summary of policy

Currently the Government provides support to working parents via a tax exemption and National Insurance (NICs) disregard which supports the ESC scheme. However, ESC is offered by less than 5%[4] of employers and one of the main drawbacks of the scheme is that many parents are unable to access it, either because their employer does not offer it or because they are self-employed. The new scheme – Tax-Free Childcare – will be available to many more families, including the self-employed and those whose employer does not offer ESC. At Budget 2013 it was announced that the tax exemption and NICs disregard for ESC (childcare vouchers and directly-contracted childcare) would be gradually phased out when the new scheme is introduced.

The new scheme is targeted at working families and is a wider, fairer and better way to help with the costs of childcare. All households in which all parents work but do not receive Government support through tax credits, Universal Credit or ESC (childcare vouchers or directly-contracted childcare) will be eligible for the scheme, so long as all parents meet the minimum income level and no parent is an additional rate taxpayer. It will offer workers 20% support towards their childcare costs up to an annual cap of £2,000 Government support per child – the equivalent of basic rate tax relief on annual childcare costs of up to £10,000 per child. The scheme will be operated through online childcare accounts and will be introduced from autumn 2015.

It is estimated that the scheme will be available to up to 1.9 million[5] families. Of these, around 1.25 million[6] will be likely to have qualifying childcare costs and be eligible to receive support from the scheme within the first year.

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[1] Childcare and early years survey of parents, 2012-2013

[2] Huskinson, T. et al (2014), 'Childcare and early years survey of parents 2012-2013' DfE SFR06/2014

[3] Childcare and early years survey of parents, 2012-2013

[4] HMT and HMRC, 'Delivering Tax-Free Childcare: the Government's response to the consultation on design and operation' Annex B https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/293084/PU1607_Tax_free_Childcare_response.pdf

[5] HMT and HMRC, 'Delivering Tax-Free Childcare: the Government's response to the consultation on design and operation' Annex B. This estimate does not take into account possible changes to future work patterns as a result of Tax-Free Childcare (although such changes are accounted for in cost estimates). Therefore more than 1.9 million parents may become eligible.

[6] HMT and HMRC, 'Delivering Tax-Free Childcare: the Government's response to the consultation on design and operation' Annex B. This estimate does not take into account possible changes to childcare usage as a result of Tax-Free Childcare (although such changes are

Of the 1.25 million families expected to have qualifying childcare costs, there will be around 1 million 'winners' (families who will be better off as a result of the scheme), including around 1.3 million children. The vast majority of these families would not qualify for any support were the new scheme not introduced.

Because the ESC tax exemption and NICs disregard will remain open for existing scheme members, the remaining 250,000 families will not be worse off as a result of the changes, but will maintain their current level of support whilst they have eligible children, remain with their employer and the employer continues to operate the scheme.

All working families which are eligible for the new scheme will be able to receive 20% support towards their childcare costs, up to an annual limit of £2,000 Government support per child. The amount they actually receive will vary from family to family, dependent on their childcare costs.

For those who are not able to receive support through ESC – for example, because they work for an employer which does not offer the scheme, or are self-employed – their 'gain' from the introduction of the new scheme will be the entire support available. For those who are also eligible for ESC but better off in the new scheme, their gain will be the increase in support received. Some families will be better off in ESC than switching to the new scheme, and will be able to remain in ESC for as long as they have eligible children, provided their employer continues to offer the scheme and they remain with the same employer.

The case studies below show a range of scenarios:

- a single parent family (which is not in receipt of support through tax credits or Universal Credit) with one child with childcare costs of £5,000 would receive £1,000 support in the new scheme if they meet the eligibility criteria. If the parent does not work for an employer which offers ESC, they would be £1,000 better off per year as a result of the introduction of the new scheme;
- a working couple (both basic rate taxpayers) with one child with childcare costs of £10,000 will qualify for £1,866 support through ESC if both parents work for employers offering the scheme, and £2,000 through the new scheme if they meet the eligibility criteria. They will gain an increase in support of £134 by switching to the new scheme;
- a working couple (both basic rate taxpayers) with one child with qualifying childcare costs of £8,000 would receive £1,866 in ESC if both parents work for employers offering the scheme, and £1,600 in the new scheme if they meet the eligibility criteria. They will be better off remaining in ESC, and will be able to do so for as long as they have eligible children, provided their employers continue to offer the scheme and they remain with the same employers.

For the one million families who gain from the introduction of the new scheme, the average additional support that they will receive is £600 per year, equivalent to a total benefit of £50m per month.

Policy description

Current scheme

There are three forms of ESC, each of which attracts a tax exemption and NICs disregard. An employer can give its employees childcare vouchers worth up to a maximum £55 per week (depending on the earnings of the employee), on which there is a tax exemption for the employee and a NICs disregard for the employee and employer. Employees can use these vouchers to purchase childcare provided by any childcare provider which is registered by an

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accounted for in cost estimates). Therefore more than 1.25 million eligible families may have qualifying childcare costs. The number of 'winners' could similarly increase.

appropriate regulatory body. Alternatively an employer can pay for childcare up to a maximum of £55 per week for their employees directly (depending on the earnings of the employee), typically entering into a contract with a childcare provider, and paying for childcare on the employee's behalf. This is known as directly-contracted childcare. The third form of ESC – which will not be directly affected by the changes – is workplace nurseries, where an employer provides childcare for their employees on their own premises or by combining with other employers to jointly finance and run a nursery. There is no limit on the tax exemption or NICs disregard for this benefit.

When ESC was introduced, it was thought that the scheme would be set up and administered by employers themselves; it was not anticipated that a separate industry would develop to deliver the scheme. This market sprang up independently and there is no statutory regulation in it, although since its inception in 2010, some voucher providers have become members of the Childcare Voucher Providers Association (CVPA), which has a code of conduct. In the majority of cases, employers use this market to get a third party voucher provider to administer their ESC scheme. Employees establish salary sacrifice arrangements with their employer, whereby an employer withholds part of an employee's salary, or 'salary plus' arrangements where the benefit is provided in addition to salary. Agreed amounts are paid into a childcare voucher account which the employee can use to pay for childcare. The amounts so paid – up to the limits specified above – are exempt from income tax for the employee and subject to a NICs disregard for both the employee and the employer.

In most instances employers pay the voucher provider a fee for operating the accounts. This is more than outweighed by the level of NICs savings that they make from the scheme if they deliver ESC through salary sacrifice arrangements. The fees payable for this service are generally invisible to the parent.

In ESC there are a number of different providers operating in an open market. If they wish to use a voucher provider, employers can choose which one to use, typically basing their choices on a series of factors, including the standards of service they provide and the level of fees they charge. Voucher providers range in size of business from very small specialist firms offering only ESC vouchers to those who are part of large corporate groups with a range of other business-to-business services such as marketing, research and human resources; other voucher or pre-paid products; and nurseries and early-years education.

Why the tax exemption and National Insurance disregard for ESC are being removed

The ability for ESC to provide wide ranging, effective and fair support to working families is limited by a number of drawbacks:

- its coverage is limited: less than 5% of employers currently offer an ESC scheme to their employees; this means that more than half of all employees are unable to receive support[7];
- it is not available to self-employed parents;
- it is generally not available to those paid at the National Minimum Wage;
- the tax exemption and NICs disregard is of no benefit to employees earning below the relevant thresholds[8];
- it is poorly targeted, with no maximum income limit; and
- it pays no regard to the number of children in each family and disadvantages lone-parent families, offering greater support to two-parent families where both work for employers which offer ESC.

[7] HMT and HMRC, 'Delivering Tax-Free Childcare: the Government's response to the consultation on design and operation' Annex B

[8] In 2014-15, those born after 5 April 1948 generally do not pay income tax on the first £10,000 they receive; this figure is slightly higher for those born earlier. Employees generally do not pay NICs on the first £153 they earn per week.

In addition, the employer NICs disregard is poor value for money for taxpayers. The disregard generates a saving for employers of up to 13.8% of the cost of the childcare vouchers provided. This is a significant Government cost (forgone receipts) in the scheme which is not spent on childcare – effectively an administration fee. Moreover, as the NICs saving generally outweighs the cost to an employer of either administering the scheme itself or paying for a voucher provider to do so, the NICs disregard has a significant deadweight cost.

As was announced at Budget 2013, the tax exemption and NICs disregard offered in ESC (childcare vouchers and directly-contracted childcare) will be closed to new entrants when the new scheme is introduced. This long lead-in time and 'grandfathering' of the scheme has given employers, voucher providers and others involved in ESC time to make preparations.

Employees who are in an ESC scheme when the scheme is closed to new entrants will be able to continue benefitting from the tax exemption and NICs disregard for as long as they have eligible children, provided their employer continues to offer the scheme and they remain with the same employer. Such parents will have the option of remaining in ESC or switching to the new scheme, but they cannot – except during a limited transition period when moving to the new scheme – simultaneously be in receipt of Government support through both schemes. As the tax exemption and NICs disregard will remain available to existing members who choose to stay in the scheme, these arrangements will remain open for an extensive period of time.

The provision of workplace nurseries will not be directly affected by the introduction of the new scheme; workplace nurseries will continue to be subject to their existing tax exemption and NICs disregard.

Impact of removing the tax exemption and NICs disregard from ESC

Parents

Parents who are in receipt of the ESC tax exemption and NICs disregard when the new scheme is introduced will be able to continue to receive it for as long as they have qualifying children, their employer continues to offer the scheme and they remain with that employer. As such there will be no direct cash losers as a result of the changes.

At the appropriate time, the Government will provide information for parents who are eligible for both schemes to inform their decision on which support would be most suitable for them. This will include an online calculator.

Childcare providers

Childcare providers will experience a transitional period during which they receive payments for childcare provision from ESC and the new scheme. The Government will continue to work with childcare providers, employers and current voucher providers to ensure that the two systems run smoothly together, and that any guidance needed is provided in good time.

Employers

Once the tax exemption and NICs disregard have been closed to new entrants, employers currently offering ESC will gradually see reductions in the NICs savings from which they currently benefit. As some of the current NICs savings cover employers' administration costs – and usually a fee to a voucher provider – the loss in benefit will be partly offset by a corresponding reduction in costs if the employer chooses to wind down its scheme. As such the real loss in benefit to employers will be significantly less than the actual loss of the NICs disregard.

Employers affected vary in size from micro to large, but in general it is larger-than-average employers which offer ESC.

As the tax exemption and NICs disregard will continue for existing members of the scheme, there will be no requirement for employers to, for example, adjust existing pay arrangements. Employers will simply not be able to enrol further employees onto the scheme and receive a NICs disregard, or the employee receive a tax exemption or NICs disregard.

Employers which do not offer ESC – the vast majority of employers – will not be affected by the removal of the tax exemption and NICs disregard.

ESC voucher providers

There is likely to be an increase in demand for childcare vouchers before the tax exemption and NICs disregard are closed to new entrants, as additional employers and employees decide to access the scheme.

Once the tax exemption and NICs disregard have been closed to new entrants, demand for childcare vouchers under ESC is likely to fall over time. Announcing at Budget 2013 the decision to remove the tax exemption and NICs disregard (over two years in advance of its implementation), and allowing those parents in the scheme at that point to remain in it if they wish, are intended to give voucher providers sufficient lead-in time to plan for and respond to the changes and ensure that there is a gradual, rather than sudden, reduction in demand. Larger providers with diverse business portfolios may seek to re-focus resources into other areas, while smaller providers may seek to diversify their business activities. Over time, as demand contracts, smaller providers that are not able to diversify may be absorbed into larger providers or close.

Voucher providers in the existing scheme may experience a rise in enquiries from parents and childcare providers in the run-up to or following the introduction of the new scheme, some of which may need to be redirected to the scheme's account provider, and / or HM Revenue and Customs.

New scheme

The new scheme will address the shortcomings of ESC and will be available to many more parents, including those who are unable to benefit from the current scheme such as the self-employed and those whose employer does not offer it. It will be available to all families in which all parents earn above a minimum income level, no parent is an additional rate taxpayer, and all parents meet the other eligibility criteria.

Eligibility

Eligibility to receive Government support under the new scheme will depend on meeting the following criteria:

- both parents (or a lone parent) must be in paid work;
- children must be under the age of 12. Disabled children must be under the age of 17;
- the parent must be 16 or over and be responsible for, and normally live with, the child;
- both parents (or a lone parent) must not be in receipt of any Government support through tax credits, Universal Credit, ESC (childcare vouchers or directly-contracted childcare) or other Government-funded support with childcare costs such as a Childcare Grant or an NHS Bursary. (Accessing a Government-funded childcare place, such as the 15-hours-per-week early years offer in England, will not affect entitlement to the new scheme. Eligible working parents will be able to use the new

scheme to help pay for any additional childcare they need in addition to their free entitlement.);

- both parents (or a lone parent) must not be an additional rate taxpayer;
- all parents (except for newly self-employed parents as explained below) will need to meet a minimum income level, set at £52 per week on average over the course of an entitlement period (or for self-employed parents, as also explained below, a tax year).

Where a family currently receives the tax exemption and NICs disregard in ESC and wishes to move to the new scheme, they must commit to telling their employer, within three months of applying for the new scheme, that they no longer wish to receive the tax exemption and NICs disregard[9]. This will allow a limited period (up to three months) of dual provision to ensure there is a smooth customer journey. This avoids requiring families to leave the ESC tax exemption and NICs disregard before applying for the new scheme. If the family changes its mind and decides to stay with ESC then they will have to repay any government support they received under the new scheme.

The minimum income level will be based on a parent working eight hours per week at National Minimum Wage. Based on the current rate of the National Minimum Wage for those aged 21 or over, parents would each have to earn £52 a week on average to qualify for the new scheme, or around £676 across a quarterly entitlement period. For parents who are under 21 or apprentices, the minimum income level will be based on the rate of the National Minimum Wage which applies to them. The current rate (2014) of the National Minimum Wage is £6.50 per hour for those aged 21 and over; £5.13 per hour for those aged 18-20, £3.79 per hour for under 18s and £2.73 per hour for an apprentice.[10]

A major difference between ESC and the new scheme is that self-employed parents will be able to receive support with their childcare costs in the new scheme. The minimum income level will apply to them in a similar way, and will be based on their net profit, defined as total receipts less expenditure incurred in running the business (excluding capital expenditure). This will provide parity with the treatment of employed parents. However, to reflect the fact that many newly-established businesses do not make a profit, self-employed parents will not need to meet the minimum income level during the first four entitlement periods (around twelve months). In addition, to reflect the fact that many self-employed people do not make a consistent level of profit across the year, self-employed parents will alternatively be able to meet the minimum income level on an annual basis. This will be assessed using their expected income for the tax year.

In excluding those parents liable to pay the additional rate of income tax, income from all sources will be taken into account, not just employment or self-employment. The additional rate currently applies to those individuals whose income is £150,000 or more per year. In addition, individuals who are taxed on the remittance basis will not be eligible. The Government estimates that, because of these upper income criteria, 100,000[11] families who otherwise would be, will not be entitled to the new scheme.

Childcare accounts will be central to the delivery of the scheme. They will act as an intermediary between parents and childcare providers. Eligible parents will be able to open a childcare account online; pay money towards their childcare costs into that account; and have the

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[9] In the case of a parent who is reconfirming their Tax-Free Childcare eligibility, and who has a new partner who is currently in receipt of ESC, their partner must commit to telling their employer, by the end of the parent's Tax-Free Childcare entitlement period for which they are reconfirming, that they no longer wish to receive the tax exemption and NICs disregard in order for the family to continue in the new scheme. Alternatively, they will be able to leave the new scheme to enable the partner in ESC to continue to benefit from the tax exemption and NICs disregard in that scheme.

[10] HMT and HMRC, 'Delivering Tax-Free Childcare: the Government's response to the consultation on design and operation' p. 20

[11] HMT and HMRC, 'Delivering Tax-Free Childcare: the Government's response to the consultation on design and operation' p.18

payments topped up automatically by the Government at a rate of 20p for every 80p paid in by parents, up to an annual limit of £2,000 Government support per child. They will then allocate this money to the qualifying childcare provider(s) of their choice, with the account provider making payments direct to the childcare provider(s).

The first consultation on Tax-Free Childcare looked at the options for delivering childcare accounts. In May 2014 the Government published a further consultation on options to deliver Tax-Free Childcare accounts. In July 2014, following consideration of the responses to both consultations and the evidence on all of the options, the Government announced that National Savings and Investments (NS&I) will be the scheme's account provider.

Parents will only be able to use their accounts to pay for childcare which enables them to undertake paid work. However, this requirement will be applied flexibly to ensure that parents on sick leave, maternity, paternity and adoption leave, or households where one member of a couple is in work and the other is in receipt of Carer's Allowance or contribution-based or 'credits only' Employment and Support Allowance are able to access support. This means that approximately 50,000[12] additional families will be able to receive support through the new scheme, compared to what would otherwise be the case.

Parents

As set out above, the Government is widening its support so that more families will be eligible for support, in particular the self-employed and those whose employer does not offer ESC. All eligible families will be able to benefit by up to £2,000 per child per year. So for a family with two children, the scheme will be worth up to £4,000 per year, depending on their childcare costs.

All eligible parents with children under 12 or disabled children under the age of 17 will be able to receive support through the new scheme within the first year of its introduction.

To benefit from the scheme, parents will need to complete the registration process to confirm their eligibility, and reconfirm this via a light-touch process each quarter. The scheme is being designed with user needs at its heart to ensure that this process is as simple as possible for families. This includes learning from the experiences of previous schemes such as tax credits; conducting customer research; and supporting the digital development with user testing. The Government will also issue guidance and online tools – including an interactive calculator – to parents to further support a smooth customer journey. (The first tranche of draft guidance was published on 16 October 2014.)

Qualifying childcare

Support will only be provided where a parent uses childcare which is formally registered or approved. For these purposes, this will mean childcare which is registered with Ofsted in England, with equivalent authorities in Scotland, Wales and Northern Ireland, or other recognised regulatory bodies such as the Care Quality Commission. This is consistent with the rules of ESC, tax credits and Universal Credit. Those childcare providers who are not required to be registered with one of these bodies, and who currently do not voluntarily register, may choose to do so where possible, and pay a small annual charge associated with voluntary registration, along with any associated costs such as first aid certification.

Approved childcare can include care provided by nurseries, playschemes, childminders, nannies and schools.

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[12] HMT and HMRC, 'Delivering Tax-Free Childcare: the Government's response to the consultation on design and operation' p.20

Childcare providers

Childcare providers range in size of business from micro to large and will incur costs in familiarising themselves with the new scheme and ensuring that their systems are also able to receive payments from the new scheme. The Government expects these costs to be broadly proportionate to the size of the business.

Once the new scheme is introduced, childcare providers may see an increase in business.

Employers

Employers will be able to play a role in the new scheme if they wish – for example, by providing information about the scheme to their employees, or making payments into childcare accounts on their behalf. Any such action will be entirely voluntary, so there will be no new burdens on employers. This is in contrast to the alternative way of extending support with childcare costs mentioned above: mandating employers to offer ESC. This would have placed significant administrative costs on employers, including small businesses with relatively few employees, and increased unfairness and poor value for money of the existing scheme, as outlined above.

Regardless of whether they choose to be directly involved in the new scheme, the Government expects that employers will benefit from the effects of a far greater number of employees being able to receive support with their childcare costs. This will be particularly significant for employers who do not offer ESC, whose employees will be able to access support for the first time. The Government expects small- and medium-sized enterprises to particularly benefit from this.

Ensuring compliance with the scheme

Parents will register for the scheme online and provide details to enable HMRC to confirm their eligibility. They will also reconfirm their eligibility on a quarterly basis.

A series of compliance rules will be introduced to ensure that support is only provided where it is rightly due and to counter cases of carelessness, deliberate error and fraud. This will be underpinned by real-time checks of HMRC data, supported by gateways for the exchange of information between HMRC and other public bodies, to ensure that parents do not claim Government support towards their childcare costs from multiple sources. The Government is considering the options for collecting information on employees in receipt of ESC to prevent double claiming.

Exchequer costs

	2015/16	2016/17	2017/18	2018/19
Gross cost	-£285m	-£825m	-£940m	-£990m
Net cost	-£245m	-£660m	-£645m	-£590m

The gross cost represents the estimated post-behavioural spend on Tax-Free Childcare. The net cost is smaller than the gross cost as it includes the estimated savings from closing to new entrants the tax exemption and NICs disregard in ESC.

The net figures can be found in the Budget 2014 policy costings document: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/293740/PU1638_policy_costings_budget_2014.pdf.

Administration costs

HMRC will incur costs to set up and administer the new scheme. The final costs are not yet available as they will only be settled once the precise details of the scheme have been finalised.

Economic Impact

It is not possible to produce a full, monetised cost-benefit analysis of the scheme due to insufficient data and evidence, as well as limits to how reasonably such costs and benefits can be monetised to provide meaningful results.

The Government will conduct a Post-Implementation Review two years after the scheme has been fully implemented, to assess whether Tax-Free Childcare is meeting the objectives it has been designed to achieve. This will assess, for example, whether parents (particularly those who are currently unable to access any support with their childcare costs) are able to access and use the scheme effectively to help with their childcare costs. In advance of the Post-Implementation Review, HMRC will be exploring how to measure the impact of Tax-Free Childcare on the labour and childcare markets.

The Government's assessment of the economic impacts, consistent with the Green Book approach, is set out below.

The fiscal costs of the scheme, as set out above, are not considered a cost in the economic assessment as they represent a transfer from one set of agents in the economy to another. Similarly, the positive impact on household incomes for those who receive support under the new scheme are not included as an economic benefit.

Costs

Government

There will be administration costs for the Government in setting up and running the new scheme. These costs will be known once the scheme details have been finalised. In ESC, the Government is effectively paying administration costs of up to 13.8% of the value of vouchers through the NICs disregard to employers. This is Government expenditure on the scheme which does not go towards childcare costs. The Government expects the cost of running the new scheme to be lower, meaning more Government resources are spent on supporting working families with their childcare costs.

Employers

Employers which offer ESC will, over time, lose the employer NICs disregard which they currently receive. As the financial benefit of the NICs disregard funds both administration costs within the employer and fees for voucher services, the real loss to employers will be significantly less than the actual level of the NICs disregard. Advance notice (at Budget 2013) and the gradual nature of the withdrawal will enable employers to prepare for this. Employers which do not offer ESC – the vast majority of employers – will not be affected by the removal of the NICs disregard.

There will be no compulsory additional administration costs to employers from the scheme, as there is no compulsory employer role. However, some employers are likely to wish to be involved, tailoring their role (and therefore the costs they face) to their individual circumstances and preferences. By comparison, the alternative option discussed above for extending support with childcare costs – mandating employers to offer ESC – would have added new burdens on all employers, especially small- and medium-sized enterprises with low numbers of staff.

Voucher providers

Organisations which administer vouchers under ESC are likely to see a gradual reduction in demand as the tax exemption and NICs disregard are phased out. The Government's announcement in March 2013 gave voucher providers an extended lead-in time to respond to the change, which should help enable them to diversify and minimise risks of closure. Further, as the tax exemption and NICs disregard will remain available to existing scheme members, they will remain open for an extensive period of time.

Parents

There will be some time (but not financial) costs for parents to enter the scheme as they have to register, set up an account, and reconfirm eligibility periodically. Such time costs are likely to be small relative to the financial benefits for parents of the scheme.

Childcare Providers

As with the current scheme, childcare providers will have some costs as they register to accept payments from the scheme's account provider. However, as the Government has announced that NS&I will be the sole provider of childcare accounts, childcare providers will only have to register with one account provider.

During the transition period, childcare providers will also administer payments under the current ESC scheme. The Government will continue to work with childcare providers, employers, current voucher providers and software providers to ensure that the two schemes run smoothly together, and that any guidance needed is provided in good time. (The first tranche of draft guidance was published on 16 October 2014.)

Benefits

Parents

Tax-Free Childcare will improve the affordability of high-quality childcare for working families, which can bring potential economic benefits in terms of labour supply and productivity.

Labour supply

There is strong academic evidence to suggest that reducing the price of childcare can have positive labour market impacts. In particular, childcare price subsidies can be effective at improving the proportion of mothers of young children who are in paid employment.

Evidence suggests that over half of non-working mothers would prefer to go to work if they could arrange reliable, convenient, affordable and good quality childcare[13]. The following table provides a summary of key academic studies on the effect of childcare prices on the proportion of mothers in paid employment. While few are specific to the UK we can use international estimates to gauge the likely effect of Tax-Free Childcare on the proportion of mothers who are in paid employment.

[13] Childcare and Early years Survey of Parents 2014, covering the 2012-13 year

Summary of childcare price elasticities with respect to the proportion of mothers in paid employment

Academic Study	Child care price elasticity with respect to the proportion of mothers in paid employment	Country
Gong, Breunig and King (2010)	-0.29	Australia
Kalb and Lee (2008)	0 (married) -0.19 (single)	Australia
Wrohlich (2009)	-0.04	Germany
Kornstad and Thoresen (2007)	-0.12	Norway
Rammohan and Whelan (2005)	0	Australia
Viitanen (2005)	**-0.14**	**UK**
Andren (2003)	0	Sweden
Jenkins and Symons (2001)	**-0.09 (single mothers only)**	**UK**
Powell (1998)	-0.21 to -0.71	Canada
Kimmel (1998)	-0.92 (married) -0.22 (single)	USA
Blau and Hagy (1998)	-0.20	USA
Averett et al. (1997)	-0.78	USA
Cleveland et al. (1996)	-0.39	Canada
Blau and Robins (1988)	-0.38	USA
Connelly (1992)	-0.2	USA

Note: a negative elasticity means that as the price of childcare falls, the employment rate of mothers increases. For example, in the case of Gong, Breunig and King (2010) a 10% reduction in the price of childcare would lead to a 2.9% increase in the proportion of mothers who are in paid employment.

Notably, the majority of these studies, including the two UK papers, suggest that a reduction in the price of childcare would have a statistically significant positive impact on the proportion of mothers who are in paid employment.

In addition, a reduction in childcare costs can encourage mothers who are already employed to increase their hours of work. Evidence suggests that over one in five working mothers would like to increase their hours if they could arrange good quality childcare which was convenient, reliable and affordable[14]. In a study of the Australian labour market, Gong, Breunig and King (2010) find that the effect of cheaper childcare on employment is stronger for those mothers who are already in-work (i.e. the intensive margin) than for those who are out of work (i.e. the extensive margin), although the scale of this response varies between studies. The following table provides a summary of key academic studies on the effect of childcare prices on hours worked.

[14] Childcare and Early years Survey of Parents 2014

Summary of childcare price elasticities with respect to hours worked (for the female population)

Academic Study	Child care price elasticity with respect to hours worked by mothers	Country
Gong, Breunig and King (2010)	-0.65	Australia
Kalb and Lee (2008)	0 (married) -0.16 (single)	Australia
Wrohlich (2009)	-0.13	Germany
Kornstad and Thoresen (2007)	-0.17	Norway
Rammohan and Whelan (2005)	-0.12	Australia
Andren (2003)	-0.16	Sweden
Ribar (1992)	-0.74	USA

Note: a negative elasticity means that as the price of childcare falls, the number of hours worked by mothers increases. For example, in the case of Gong, Breunig and King (2010), a 10% reduction in the price of childcare would lead to a 6.5% increase in hours worked for in-work mothers.

Notably, all but one of these studies suggest that a reduction in the price of childcare would have a statistically significant positive impact on the number of hours worked by mothers who are in paid employment.

The Government expects a positive impact on both participation in employment and hours worked as a result of Tax-Free Childcare, although it is not possible to quantify this given the lack of evidence for the UK. Both of these labour supply impacts will have indirect second order effects, including increased household income (as these families increase their total hours of work) and increased tax revenues (from the extra household income). Given the uncertainty around the initial first-order impact, these have not been quantified and monetised.

The Government believes that the new scheme is likely to have a greater positive impact on labour supply than ESC. This is because the scheme will be more widely available, with up to 1.9 million families eligible for support, and because the scheme is better targeted through being restricting to households where all parents are in work and providing support on a per child basis.

The scheme will also mean that parents currently in receipt of tax credits or Universal Credit will be able to increase their income and still receive support with childcare costs; this is likely to encourage some employees to increase their hours at work where they are approaching the income limit of tax credits or Universal Credit, where previously they may have been discouraged from doing do.

As mentioned above, HMRC will explore how to measure the impact of Tax-Free Childcare on the labour market.

Productivity

Access to affordable, high-quality childcare can help improve productivity in the workforce by reducing absenteeism and problems with timekeeping associated with childcare emergencies.

In addition to increasing take-up of childcare from those parents who choose to move back into work or increase their hours, Tax-Free Childcare may also encourage parents to switch from informal to formal care. There have been numerous studies looking at the effect of childcare prices on formal childcare use. The following table provides a summary of these:

Summary of childcare price elasticities with respect to the use of formal childcare (for in-work mothers)

Academic Study	Child care price elasticity with respect to the use of formal childcare	Country
Viitanen (2005)	**-0.46**	**UK**
Powell (2002)	-1.48	Canada
Duncan et al.(2001)	-0.26 to -0.46	Canada
Cleveland et al. (1996)	-1.06	Canada
Ribar (1995)	-0.22	USA
Ribar (1992)	-1.86	USA

Note: a negative elasticity means that as the price of childcare falls, the use of formal childcare for in-work mothers increases. For example, in the case of Viitanen (2005) a 10% reduction in the price of childcare would lead to a 4.6% increase in the use of formal childcare for in-work mothers.

Wider Impacts

Child Poverty

The Government is committed to the goal of eliminating child poverty by 2020. The overall system of support with childcare costs is focused on those on low incomes. Those on tax credits can receive 70% support towards their childcare costs, and in Universal Credit, this will increase from April 2016 to 85% for each hour worked. In addition, the least advantaged 40% of two-year olds – as well as all three- and four-year olds – now receive 15 hours per week of free childcare.

Work remains the best route out of poverty and alongside this focused support, the broader package of assistance available through the welfare system will encourage and support parents to move into and progress in work.

Families

Tax-Free Childcare is explicitly designed to support working families. At all stages of the development of the scheme the requirements of working families have been a central determinant.

As set out, ESC disadvantages lone parents by basing the level of support on the number of eligible parents, rather than the number of children. In the new scheme, all parents will be treated equally, with the level of support based on the number of children. The support available will not be affected by changes in household composition, provided all parents or partners in the household continue to meet the eligibility requirements such as being in work.

The new scheme will support families at key transition points. The quarterly entitlement period will ensure that parents will remain eligible for the remainder of the current entitlement period, regardless of any unexpected changes of circumstances. More broadly, the scheme will give parents confidence that – whoever their employer, and if they are self-employed – they will qualify for support with childcare costs when they return to work following the birth of a child, or when they move job, provided they meet the eligibility criteria. In addition, when parents take a period of parental leave, they will be able to continue to use the scheme for existing children. This will to help them to maintain their existing childcare arrangements.

The new scheme will help working families to make the best choice for them on how they support work with family life – if they wish to work. It will also allow other members of families – for example, grandparents – to help with childcare costs, with Government top-ups also available on these contributions.

Equalities Impacts

Families on lower incomes generally receive more generous support under the tax credit and Universal Credit systems and will therefore not be entitled to receive support under the new scheme. As working lone parents are more likely to have lower income levels than working couples, more lone parents will receive this generally more generous support through tax credits or Universal Credit. It is estimated, therefore, that of the families that will directly benefit from the new scheme, around 95% are headed by couples, and 5% are lone-parent families.

The scheme will support couples where one parent is in work (and meets the eligibility criteria) and the other parent is either a full-time carer in receipt of Carer's Allowance, or in receipt of contribution-based or 'credits only' Employment and Support Allowance. Such couples will be treated for the purposes of the scheme as if both parents are in work.

The scheme will predominantly support working age families but will be available to all those who have responsibility for raising a child, including working parents of retirement age and grandparents. Multiple people or parties will be able to pay into childcare accounts. This will give family members, including grandparents, and other parties the opportunity to contribute.

Eligible parents on a period of paid or unpaid maternity, paternity or adoption leave can continue to receive support from the new scheme for children who were eligible for the scheme before they began their period of leave.

In recognition of the fact that childcare costs for disabled children can remain high in later years, the scheme will support parents of disabled children under the age of 17. The Government is currently exploring what more might be done to give more support to those with disabled children – in particular whether it would be feasible to increase the maximum amount which parents of disabled children can pay into their childcare accounts, which in turn will attract a top-up payment from the Government.

The scheme will be simple for applicants as transactions will be carried out online. Although fundamentally a digital process, there will be small numbers of parents who are unable to engage with the scheme via online means, for example because of a disability. Alternative access routes will be offered to people unable to make claims online and the Government will ensure that appropriate assistance is available to allow such parents to engage with the scheme and gain access to support. Similarly, any childcare provider which does not have access to digital channels will be able to receive assistance.

The following areas have been considered and no impact identified: Competition; Wider Environmental Issues; Health and Well-being; Human Rights; Rural Proofing; Sustainable Development.

The Childcare Payments Bill will be supplemented by secondary legislation providing detailed rules on the scheme and the grandfathering of the tax exemption and NICs disregard in ESC. The draft regulations were subject to consultation between 14 July and 3 October 2014.

Post Implementation Review (PIR) Plan

Basis of the review:
The policy is to be reviewed two years after full implementation.

Review objective:
To assess whether Tax-Free Childcare is delivered effectively and supports working families as intended. In particular, it will cover:

- delivery: assessing the user journey;
- outputs: broadening access to government support with childcare costs, whilst ensuring effective compliance with the scheme; and
- outcomes: in advance of the PIR, HMRC will explore how to measure the impact of Tax-Free Childcare on the labour and childcare markets.

Review approach and rationale:
A mixture of approaches will be used including:

- analysis of internal administrative datasets;
- analysis of existing government survey data including:
  - the Family Resources Survey;
  - the Childcare and Early Years Survey of parents;
  - the Childcare and Early Years Providers Survey; and
- bespoke qualitative and quantitative analysis.

The review will consider a range of information from a variety of data sources to assess the potential impacts of the scheme. The review will draw on expertise across Government.

Success criteria:

There are several criteria that will determine whether Tax-Free Childcare has been successful. These will include, for example, parent and childcare provider views on how easy the new scheme has been to access and use.

Tax-Free Childcare will broaden access to Government support with childcare costs, in particular to those who had previously been excluded from Employer-Supported Childcare. The PIR will look at indicators such as take-up (particularly those who previously did not have access to Government childcare support) to consider the extent to which this has been realised. As mentioned above, HMRC will also be exploring how to measure the impact of Tax-Free Childcare on the labour and childcare markets.

Alongside this, the Government will consider operational information to review the implementation and delivery of the scheme.

A series of measures will take into account administrative, qualitative and quantitative data. This will include information in the form of surveys, case studies, tracking studies, administrative data and interviews / focus groups.

Monitoring information arrangements:

The evaluation will comprise a number of inter-related components including a live running review of the implementation and delivery, and ongoing analysis of policy outcomes and impacts. Elements of the assessment programme will be undertaken internally and others will be commissioned externally.

This approach to evaluation will ensure that potential impacts of the policy are covered, allowing for insight into future policy development and providing the opportunity to refine delivery and running of the scheme.
Reasons for not planning N/A